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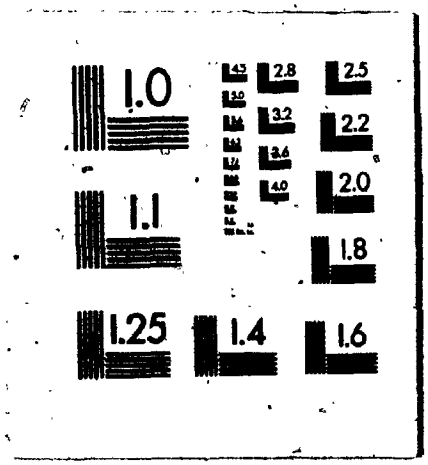

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Leslie Thomas MacDonald

Date of Birth — Date de naissance

Feb. 6, 1948

Country of Birth — Lieu de naissance

Canada

Permanent Address — Résidence fixe

102 Springhurst Avenue, Ottawa, Ontario, K1S 0E5

Title of Thesis — Titre de la thèse

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Professor K.Z. Paltiel

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Signature: L. T. MacDonald

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TAXING COMPREHENSIVE INCOME: POWER AND PARTICIPATION IN CANADIAN POLITICS, 1962-1972

by

© LESLIE T. MACDONALD

A thesis submitted to

the Faculty of Graduate Studies and Research

in partial fulfilment of

the requirements for the degree of

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Department of Political Science

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submitted by

Leslie MacDonald, B.A., M.A.

in partial fulfilment of the requirements

for the degree of Doctor of Philosophy

.....
Chairman, Department of
Political Science

.....
Thesis Supervisor

.....
External Examiner

Carleton University

October 2, 1985

Abstract

Pluralist notions of the diffusion of political power through citizen participation in politics and the democratic competition of different elites have been widespread in both scholarly and popular conceptions of political decision-making in Western democracies. During the 1960's and 1970's, governments in Canada often defended policies on the grounds that the public had been involved in their formulation and that all significant interests had been heard. Such was the case for the decade-long process of federal tax reform, which began with the appointment of the Royal Commission on Taxation (Carter Commission) in 1962, and culminated in the proclamation of the reformed Income Tax Act at the end of 1971. While the governments involved opened a number of institutional routes for a wide spectrum of individuals and groups to participate in the formation of tax policy, the public process was dominated at every stage by corporate business interests and their professional tax advisers. In spite of this near-monopoly over the debate in the public fora, the tax practitioners and corporate interests were unable to materially influence the internal decision-making processes of the Carter Commission, which recommended that all income, including capital gains, corporate profits and inheritances, be subject to personal tax at the same progressive rates. Implementation of this comprehensive tax base would have closed hitherto lucrative tax loopholes which had spawned a growing tax avoidance industry, and enabled a few wealthy individuals and families to control a major portion of Canada's corporate wealth. This study follows the developments which led to the perception by significant actors that the tax system needed reforming and traces the decision-making processes within the relevant governmental institutions. The return of the comprehensive income concept to the academic world of public finance texts from which it came demonstrates the political power of corporate capital and of the tax professionals in its service. At the same time, it reveals the political ineffectiveness of the great majority of Canadians earning employment income or confined to the economic margins of society.

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Putting together the many pieces of the tax reform puzzle took about as long for me as it did for the actual events to run their course. This study began as part of my course work in the doctoral programme at Carleton University in 1975, with the advice and encouragement of Professors Khayyam Paltiel, of the Department of Political Science, Irwin Gillespie of the Department of Economics, and Paul Pross, then a visiting Professor from the School of Public Administration of Dalhousie University. Professor Paltiel became my thesis adviser for the duration, commenting critically on some very rough draft chapters and periodically prodding me on with reminders that neither the participants in tax reform, nor ourselves, were getting any younger. Professor Gillespie became the second member of my thesis advisory committee. A former Research Supervisor for the Carter Commission, he helped me with some initial hypotheses and helped me locate a number of participants. His meticulous reading of the two penultimate drafts nipped many errors in the bud. Professor Leo Panitch, initially the third member of my advisory committee until he accepted an appointment at York University, provided wise counsel at the proposal stage and commented on the introductory chapter. I hope he will recognize his influence in "the meat and potatoes". I also wish to thank Professor V. Subramaniam of the Department of Political Science at Carleton, who helped direct my attention toward decision-making processes, especially those of Royal Commissions. Professors W.A. Mullins, J.M. Vickers and M.S. Whittington provided encouragement and assistance during my studies at Carleton. Successive supervisors of graduate studies and their assistants have goaded me on when earning a living and raising a family appeared to rule out completion of the dissertation.

Without the assistance of Mr. Harry A. Wilson, formerly of the Privy Council Office, Mr. Jim Whelan, the archivist in charge of royal commission papers in the Federal Archives of the Public Archives of Canada, and Professor Douglas Hartle of the Institute for Policy Analysis at the University of Toronto, I would not have been able to obtain access to the Carter Commission papers. The staff and commissionaires at the Public Archives and at the National Library in Ottawa enabled me to work in what must be one of the best research environments anywhere. John Shields spent many hours in the National Library indexing microfilmed newspaper articles, thus sparing me a good measure of tedium and eyestrain. Thanks also to the many fellow researchers with whom I was able to trade ideas, a valuable by-product of the excellent services of the National Library and the Public Archives which we shared.

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With all these people, and more, deserving thanks, the reader may be forgiven for wondering what part the author had in all this. Having failed to follow some of their advice, I must accept responsibility for the errors and short-comings that remain.

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Chapter I: Tax Reform and Liberal Democracy

Major Themes: Participation and Redistribution

Taxation, as a problem of political significance, is as old as government and as perennial as the budgetary process, yet the practical opportunity for major reform of a taxation system comes infrequently. In the case of federal income taxation in Canada, there have been only two general reforms since the original Income War Tax Act of 1917; the first resulted in the revised Income Tax Act of 1949, and the second culminated in the tax reform legislation of 1971.

The latter reform was by far the more comprehensive in that it involved a thorough scrutiny of the whole federal tax system. Although pressures for tax reform had been building since shortly after the 1948 reform, the official opening gun for the great tax reform tug-of-war was fired in August, 1962 by the Diefenbaker Government's appointment of Kenneth LeM. Carter to head the Royal Commission on Taxation. There followed a decade of public and private debate on tax reform which was not settled, to the degree that debate on taxation is ever settled, until the proclamation of the 1972 Income Tax Act.

It is probably no coincidence that this decade of tax reform was also the period of social policy initiatives of the successive

Diefenbaker and Pearson governments and of the "Just Society" orientation of the first Trudeau Government. The Carter Commission probably saw itself in tune with the reforming spirit of the times when it recommended "equity", or fairness, as the overriding objective for a reformed tax system within the context of an improved programme of progressive income redistribution.[1]

It was also a time when political leaders tended to encourage popular expectations that political institutions and processes were open to their participation, and that democracy implied a more sustained and effective level of citizen involvement than the periodic marking of ballots at election time. During this period many pressure groups were founded, and other trade and occupational groups which had hitherto concentrated their activities around service to their members, began to make specific demands on governments. The federal government actively encouraged many such groups by providing moral and financial support, and by actively seeking their advice.[2]

This norm of participation was sufficiently widely and strongly held for politicians and government officials to attempt to justify policies on the grounds that the public had been involved in their formulation. The results of tax reform were defended in such terms by the Hon. Edgar Benson, then Minister of Finance, when he introduced his tax reform budget in the House of Commons on June 18, 1971. The Government, he said, chose to respond to the Carter Report with the 1969 White Paper because it

> ...believed that a fundamental reform of the existing tax system was necessary and that all Canadians should participate in the development of this reform. The Government chose to express in a White Paper its view of what a tax system ought to be, and invited all Canadians and all levels of government to join in the discussion.[3]

Mr. Benson referred to this as "an important step in the evolution of participatory democracy in Canada."[4]

Much of the tax reform process was indeed marked by a high degree of participation of groups and individuals outside government, and by the influx of non-government people into public sector institutions involved in the process. The Carter Commission, consisting of people drawn from the private sector, and supported by a professional staff drawn largely from the universities and professional firms, was given a broad mandate to study and recommend reforms of the entire federal taxation system. The Commission welcomed and received briefs and submissions from three hundred organizations and individuals and heard approximately seven hundred witnesses while travelling to twelve cities across Canada.

Following the release of the Commission's Report in February, 1967, the then Minister of Finance, the Hon. Mitchell Sharp, announced that the Government would delay taking a firm position until it had received submissions on specified aspects of the Report from interested groups and individuals. Rather than taking the customary route of a budget speech and a ways and means motion in the House of Commons, binding the Government members to support tax legislation

they had never seen on pain of defeating the Government, the new Minister of Finance, the Hon. Edgar Benson, chose instead to present first its reform "proposals" in the form of a White Paper issued in November, 1969.[5] This was the signal for renewed and even more vigorous debate in the House of Commons and the Senate, in the mass media, at professional conferences and meetings of businessmen, and in specialized periodicals. Private individuals, businesses and groups sent thousands of pieces of correspondence and made hundreds of representations to the Minister of Finance and his officials and also to the two parliamentary committees studying the White Paper, one of which toured the country recording taxpayer reaction. The party system also appeared to give ample scope for different opinions. The NDP came out first in favour of the Carter Report, then later, with more qualified support for the White Paper. The Conservatives opposed both the Report and the White Paper, and Opposition Leader Stanfield toured the country speaking against the Government's proposals. The provincial governments, most of which opposed major aspects of the White Paper, also had several opportunities to make their points of view known and to bring their influence to bear, providing in the process additional pressure points for those attempting to influence the course of tax reform.

The extent of this participation is also a reflection of the fact that most people understand intuitively that, to a greater or lesser degree, they will have to shoulder the burden of the reformed taxes. Failure to participate when all are given the opportunity may result in one individual or sector of society having to pay higher taxes

while the burdens of others are reduced. Although it may be argued that all policy issues result in gains and losses to different segments of the population, the re-distributive nature of taxation issues is widely perceived, even if not correctly understood by most of the public. "Budget night in Canada" has become a popular spectator sport, with the electronic and print media habitually interpreting the event in terms of gains and losses for identifiable classes of taxpayers. In addition, taxation issues normally focus on a specific document, such as a budget speech and budget resolutions, a piece of legislation, or a written set of proposals such as the Carter Report or the White Paper, all of which are ultimately susceptible to evaluation in terms of dollars of tax liability for specific individuals and groups. The ease and accuracy with which such calculations can be performed may be deceptive, and large numbers of taxpayers are no doubt regularly deceived. This, however, does not stop people from thinking in such terms, no more than subtle differences in merchandise quality prevent the same individuals, as consumers, from comparing prices in the market place. To the extent that institutional channels permit, taxation issues therefore arouse public interest and participation because people feel compelled to participate.

While there have been cases of tax legislation framed to alter the economic position of specific taxpayers,[6] tax legislation as a rule operates on specified categories of taxpayers, such as those in a given income range, those engaged in defined activities, and so on. Taxes therefore influence in a systematic way the relative and

absolute economic positions of large classes of people. Sometimes this is a deliberate objective of policy decision-makers and sometimes it is the unintended consequence of tax policy initiated and implemented for other reasons. In the context of tax reform, the question of the distribution of the burden by income class, by social class or by other categories is not usually far from the surface. Taxation is one field of policy debate which, by its general, compulsory nature, by its susceptibility to comparative measurement, and by its widespread if grudging acceptance as a governmental policy instrument, is closely tied to controversies over the distribution of income and wealth.

The tax reform process thus brings together two themes reflecting widely-held concerns of the time. The first is implied in the concepts and slogans "equality of opportunity", "income redistribution", "vertical equity", "progressive taxation", and others, all supporting some movement in the direction of greater economic equality. To the extent that these concepts are popularly accepted, policies are likely to be defended on the grounds that they contribute toward this movement. At the analytical level, studies of fiscal incidence, that is, measurements of the distribution of the tax burden and benefits of public expenditure, are able to say something about the degree of success achieved by such policies.

The second theme, that of public participation in policy formation, was even more prevalent as a means of legitimation of policies regardless of whether or not they were also claimed to be

redistributive. This undoubtedly reflected the wide acceptance of this norm, and it must have had, and continues to have, some measure of descriptive validity in order to be effective as a means of legitimation.

Pluralist Conceptions of Policy-Making

Supporting and to some extent reflecting this common-sense notion of participation at a more analytical level are scholarly descriptions of policy-making in liberal democracies which assume or conclude that, in addition to electoral activity, there is a plurality of channels open to ordinary citizens to control the behaviour of people in government, and that the citizens themselves are motivated by numerous conflicting or "cross-cutting" interests, none of which remain permanently dominant or submerged. C.B. Macpherson[7] refers to this as "equilibrium democracy", or the "pluralist elitist equilibrium model", and cites Robert Dahl, among others, as one of its best known exponents.

While much of the interest group literature and many studies of political and bureaucratic decision-making would fit into this category, Canadian studies usually acknowledge that the different institutional environment from that of the U.S., notably the more dominant role of the executive in the Canadian parliamentary system, the relative strength of the federal bureaucracy, and the greater prominence of the provincial governments as actors in national

politics, significantly modify the pluralist nature of the political process. Paul Pross was in agreement with most students of interest group politics in Canada when he noted that interest groups had adapted to the institutional framework of the Canadian political environment by concentrating on securing and maintaining stable communication links to the primary centres of political decision-making, that is, to the Cabinet and the federal bureaucracy.[8] Similar observations have been made by Engelmann and Schwartz,[9] Van Loon and Whittington,[10] Robert Presthus,[11] and others. Pross was not departing from the mainstream scholarship in stating that "...the Canadian political system is based only to a limited extent on a pluralist approach to decision making."[12]

A more pronounced deviation from the pluralist model was published a decade earlier, in John Porter's analysis of the Canadian power structure, The Vertical Mosaic,[13] which found Canadian society to be dominated by a number of closed elites controlling the important institutions, including the formally democratic political structures. The existence of a large number of interest groups did not, in Porter's eyes, lessen the elite-controlled nature of the system, since "most groups and associations are themselves run on the oligarchic principle...".[14] Porter had said that the system fell short of becoming a monolithic oligarchy, or a "power elite" along the lines described by C. Wright Mills in the United States, because of the functional differentiation of the elites in Canada and the resulting competition among them.[15] Moderating and stabilizing this inter-elite competition was a shared system of values and a sense of

mutual recognition which Porter called the "confraternity of power". While he believed that the corporate elite, which was dominated by the economic upper-class, tended, itself, to be dominant over the other functional elites, he did not favour a Marxist or class concept of the structure of power.[16] Porter can be placed at the boundary of class and pluralist models of power: much of the empirical content of The Vertical Mosaic is a demonstration of the exercise of upper-class power through elite control of society's key institutions, yet he never explicitly arrived at that conclusion, since he saw several competing elites:

> The argument then is that leaders of the corporate world have to share power with the leaders of these other institutions. Power becomes diffused because of the specialized function of these other institutions.[17]

Society, according to this view, is dominated jointly by a plurality of elites; it is neither democratic pluralism nor domination by a ruling class; it is best described as elite-pluralism. It is probably a fair generalization to say that the Canadian political system is usually described as being more elite-dominated, or more closed to demands from non-elites, than is believed to be the case for the United States. While the labels differ -- John Porter's "confraternity of power", or Robert Presthus' "elite accommodation" -- most studies of interest group activity assume or conclude that the political process is under some degree of elite control exercised through some form of inter-elite co-operation, and that the resources and effectiveness of contending interests differ widely. Nevertheless, most also appear to share the belief that a large number

of different interests are competing with each other and with other institutions in order to influence the course of public policy, and in so doing, allow non-elites a significant though indirect influence on policy-making.[18]

Recent applications of economic models to political decision-making, which have come to be known under the heading of "public choice" theories, also share the view of a basically pluralist political system. The various public choice models work on the idea of individual rational actors trying to maximize their individual level of satisfaction by engaging in the political process. While the resources available to each are unequal, and the supply of public goods is usually determined within a bargaining or game mechanism rather than by the simple application of the market analogy to the electorate, the political process is characterized as one of competition among many individuals acting in collectivities. The first public choice model to gain widespread interest among students of politics was that of Anthony Downs,[19] followed by Mancur Olson,[20] and there have been several applications of different public choice models to Canadian political decision-making, including writings by Douglas Hartle on the making of budgetary policy.[21]

More narrowly focussed studies of political-bureaucratic decision-making, such as those of Richard Simeon,[22] Richard Phidd and Bruce Doern,[23] Richard D. French,[24] and David A. Good,[25] have little to say about the role of non-elites in the decision-making process. Consistent with their focus on the elites closely involved

in the decision-making process, most treat non-elites as part of the "policy environment" which affects the decision-making process through the mediation of elites. For Simeon, the chief constraints upon the relevant political-bureaucratic actors come from the strategies and tactics adopted by the other "players" in the "game": "The governmental elites at both federal and provincial levels play a crucial independent role."[26] The pluralist element in Federal-Provincial Diplomacy comes less from the participation of non-elites than from the mutual interaction of a plurality of elites, a feature common to most pluralist models. Simeon adopts Charles Lindblom's pluralist concept of "partisan mutual adjustment" in which "actors bring to the decision process different goals, perspectives, attitudes, resources, and strategies."[27] Richard French however, believes that the decision-making process is too pluralistic in its present form to allow for rational planning.[28]

Each, from his different perspective, appears to view either the process itself to be pluralistic, in the limited sense of contending autonomous elites, or at least the environment of political-bureaucratic decision-making to be fundamentally a pluralistic one. While all agree that some players pack more punch than others, none suggest that the outcome has been decided in advance: the game of policy-making may not be completely fair but neither is it rigged in favour of one interest or class. While recognizing the considerable diversity of these writings, and taking ambivalent views such as Porter's to be just outside the broad classification, I will refer to them, as does Macpherson, simply as pluralist models of democracy

since it is the idea of the plurality of social determinants of public policy which, for our purposes, essentially distinguishes them from elitist and Marxist models.

The works cited in the preceding paragraphs are offered for purposes of illustrating the pervasive, but not total, influence of the pluralist model of democracy on Canadian scholarship. Clearly, there is also a significant body of literature which is outside the pluralist category—even in the context of the broad meaning given to it here. An alternative set of models posits a ruling class controlling the key political and economic institutions, a perspective which could be arrived at by following Porter's empirical lead, but not his theoretical orientation. While these neo-Marxist or Political Economy writers do not deny that there is limited competition and disagreement among ruling elites or class fractions whose interests they represent, nor that subordinate classes can influence the course of public policy, either indirectly as perceived "public opinion", or more directly through mobilization around key issues or demands, they place the relationship of class domination in the economic sphere at the centre of the analysis of public policy-making.[29]

Objectives and Scope of the Study

Ideas linking mass participation in government and state-enforced redistribution of property are about as old as the study of politics. Since the days of ancient Greeks, there have been recurrent hopes and

fears that a greater measure of democratic government would result in a corresponding redistribution of wealth toward the lower classes. No attempt will be made here to even list the many polemical and scholarly works concerning this relationship, which would include the literature on class struggles, working-class and socialist parties, much of the modern political science literature on party competition and policy "outputs", as well as public finance writings on distributional implications of various government policies.

The present study places this old and recurring theme within the context of the recent period of Canadian tax reform from 1962 to 1972. Studies of the impact of tax reform indicate that no significant redistribution in favour of lower income-earners has occurred.[30] And yet government spokesmen at the time made so much of the point of widespread public participation. If there was widespread participation, why were the benefits of the reform not also widely distributed? By examining the history of tax reform the study seeks an answer to this question and assesses the tax reform process in terms of pluralist conceptions of democracy.

As the period in question encompassed a large number of changes in the tax system, and as the potential scope of influences on policy is very wide, this study focuses on one significant aspect of the tax reform process: the origin and disposition of the "comprehensive income concept". In its simplest formulation it is the proposal to tax all increases in economic power, however acquired, at the same (and implicitly, progressive) rates. It is sometimes referred to as

the "broad income concept", the "Haig-Simons income concept", after the two American public finance specialists who advocated it,[31] or, as Kenneth Carter is supposed to have quipped, "A buck is a buck." This particular policy proposal has been selected for an in-depth study because it is the key principle behind the Carter Report, and as it calls for the taxation of capital gains and other income accruing disproportionately to wealthy persons, it is closely related to questions of income redistribution. This study traces the recent history of the comprehensive income concept: where it came from; why people were looking for something like it; how it was introduced into the political decision-making process; how it was received by significant political actors; and what influence the proposal had on government policy. As a history of a specified policy option it will, at the same time, present a case study of the process of political decision-making and contribute toward an analysis of the structure of political power.

Methodology: the Decision-Making Framework

During the 1960's scholarly debate between the advocates of pluralist and elitist conceptions of political power, the former had relied on decision-making studies to show that a plurality of individuals and groups were instrumental in shaping government decisions, with only the elected elites being involved at all or most stages. The prototype of this genre is Robert Dahl's Who Governs? Democracy and Power in an American City, a study of municipal decision-

making in New Haven.[32] The "elitist" or ruling class proponents on the other hand usually argued from an analysis of the power structure, defining a set of institutional roles as composing the elite, then showing this elite to be composed of a small number of people with shared characteristics, experiences and values, recruited from a privileged upper class. Pioneers of this genre were Floyd Hunter,[33] C. Wright Mills,[34] and G. William Domhoff.[35] The ruling class theorists, their critics claimed, were trying to show who were powerful without demonstrating how their power was exercised, while the pluralists were criticized for selecting decisions on issues which were not sufficiently important for those who were really powerful, or for taking too restricted a view of the decision-making process. Bachrach and Baratz, for example, held that power was exercised as much in determining which issues were able to enter the arena of debate, as in affecting the outcome of those questions which actually did make it onto the political agenda.[36] One way of preventing important issues from being discussed, or preventing them from being discussed in a way which might threaten the interests of the powerful, would be by inculcating in the minds of the non-powerful an understanding of the question in terms which would deflect thought away from alternatives critical of the existing structure of power. E.E. Schattschneider referred to this continuous and pervasive effort to impress upon the masses a world view convenient to the holders of power as "the mobilization of bias".[37]

In tracing the events surrounding the place of the comprehensive income concept in the decade of Canadian tax reform, this study adopts

a decision-making framework, thus using the same general methodology as the adherents of the pluralist position in order to show how power was exercised. In selecting an issue of vital concern to those whom we hypothesize to be among the powerful, by following the development of that issue area well before the wholesale reform of the tax system became a political issue, and examining the parameters and limits of debate and the assumptions of political actors at various stages, the study also benefits from some of the critiques of the pluralists.

One can conceive of the subject matter of this study as being composed of an indeterminate chain of events situated within a much broader chain which we refer to as the process of public decision-making. One can imagine the latter composed of a multitude of individual decisions made by persons acting in various capacities, both public and private. Without pretending that public decisions can be understood simply as decisions of private individuals writ large, it is useful to think of the logical components of all decisions:[38]

1. Problem recognition: the decision-maker recognizes that he is in a position to make a decision, that is, he faces a situation or "problem" which may be met by two or more courses of action. At this stage there is dissatisfaction, even alarm at the new situation, combined with the vague feeling that "something must be done".

2. Problem definition: almost inseparable from problem recognition, it involves further mental processing of the

situation. The facts of the new situation are compared with experience of past problems in order to classify the new problem, thus making the search for solutions more manageable. Without a definition of the problem, the search for solutions could not even begin.

3. Search for alternative solutions: the definition of the problem tells one where to look amid the data of experience for solutions, or elements of solutions, which have been tried or considered for similarly-defined problems in the past.

4. Evaluation of alternatives: the probable consequences of choosing each alternative are weighed in terms of the effects of each on the goals or relationships valued by the decision-maker. This becomes progressively more complex with the number of alternatives considered, the range and complexity of the consequences, and the number and inter-relationships of the values considered to be relevant.

5. Choice of an alternative: the best or "least worst" alternative in terms of its expected consequences for whatever the decision-maker holds dear is chosen. If the exigencies of the situation do not allow sufficient time and resources for finding the optimum solution, the first one which appears to satisfy certain basic criteria might be chosen.

6. Evaluation of the solution: the effect of the chosen course

of action is observed. While asking, "Did it work?" the decision-maker is left facing a new situation. If he is not completely satisfied with, or oblivious to the changed situation, he is once again at the point of problem recognition and ready to incorporate into his experience, the relationships involving the original problem, the chosen solution, and the observed consequences. A little wiser, he then tries to cope with a new problem.

The context of this decision-making process could range from a simple problem confronting an individual to the complex and prolonged phases of the political decision-making processes of developed societies. In the case of the politics of Canadian tax reform, it involved millions of individual decisions by taxpayers concerning their respective tax liabilities and returns, their approaches toward the political process with respect to tax policy, the orientations and actions of a large number of political actors at each twist and turn of the process, including the actions of private and public organizations. All involved, in varying degrees of self-consciousness, the same logical phases of problem solving. In principle, we can combine these micro-decisions into a single decision-making process at the societal level: the recognition that the taxation system in effect at the beginning of the 1960's was somehow inadequate and that the system ought to be reformed, an operation set in motion and eventually accomplished through a number of policy instruments, including a Royal Commission, a governmental White Paper and legislation culminating in a new Income Tax Act which came into force in 1972.

While the societal-level decision is readily resolvable into several, and ultimately myriads, of component decisions, it is useful to retain the perspective of the single macro-decision as an organizing framework. This is not simply an arbitrary framework, as it is reasonable to suppose that the participants themselves understood that their own federal tax-related problems and decisions were components of a larger societal-level decision-making process. Were it otherwise, so many would not have troubled themselves to engage in the lobbying and other politically relevant activities which made them a part of the political process. It is reasonable to assume that most participants were aware that they were talking in terms of the activities of the federal tax-collecting and enforcing apparatus, as regulated by an identified body of legislation enacted by Parliament, the legitimate institution for making and setting down societal decisions binding on all Canadian residents.

At this macro-level, the stage of problem recognition arose out of the mounting dissatisfaction of taxpayers and tax professionals with the post-World War II tax system and the apparently insatiable appetite of governments at all levels for revenues, and culminated with the appointment of the Royal Commission on Taxation in 1962. We can view the work of the Royal Commission as comprising primarily the definition (or re-definition) of the problem, the search for alternatives, and the evaluation of alternatives phases. The period during which successive Liberal governments, assisted by the Department of Finance, tried to come to grips with the Carter

recommendations and formulate a defensible policy position, also fits within the evaluation of alternatives phase. The presentation of Bill C-273, the resulting debate and proclamation of the new Act can be seen as the actual choice of the "preferred" alternative.

Each of these phases of the macro-decision are themselves macro-decisions, involving corresponding phases within each. The appointment of the Carter Commission by the Diefenbaker government in August of 1962 was, as far as that government was concerned, a partial "solution" to a political problem which beset it: how, in the context of a pre-electoral situation, to counter escalating criticism of, and eroding confidence in, the government's economic policies. That solution, when combined with other political events, produced a changed situation and a new problem for the Pearson government of 1963: what to do with a "Tory" royal commission which would be investigating the tax and fiscal policies of earlier Liberal governments at a time when the new government was under pressure to unveil novel economic policies as part of its self-proclaimed "sixty days of decision". The Commissioners themselves were seized with their own collective problem of navigating their investigative machinery through complex political and organizational hazards in order to produce a report which would fulfill their ambitious terms of reference and persuade both the public and government that their recommendations should be adopted. Their solution was what became known as the Carter Report. This Report quickly changed the situation, presenting a new problem for the Pearson government of 1967: what action, if any, to take on a set of controversial

recommendations which, if adopted, might undermine the government's already precarious political support? And so on.

Tax Reform as a Decision-Making Process

In studying tax reform, we are considering not just decision-making, but political decision-making, since the decision is ultimately an authoritative one for the whole society, enforced by the state. While the society nominally regulated by that state may have many problems as recognized by any of its members, only some are, at any given time, raised to the level of political significance. We know that a problem or issue has reached this level of recognition when politicians take it into account in their decision-making, as indicated by their public statements, correspondence and other documents they create, records of meetings and any additional evidence we can uncover. When politicians behave in this way we can say that the issue has been placed on the political agenda.

Chapter II examines how the issue of tax reform made it onto the political agenda in 1962. This requires an introduction to the major "problems" in tax policy and administration at that time, showing how these problems developed out of past solutions to earlier taxation problems. Chapter II therefore traces the development of the federal income tax system from before its First World War origins to the eve of the appointment of the Royal Commission on Taxation. Factors relevant to the later reform period are given special attention: the

overall weight and importance of income taxes as opposed to other federal revenue sources, changes in the rate structure, the development of the tax professions, problems related to the definition of income for tax purposes, and the problem of the taxation of undistributed corporate earnings, better known as "surplus stripping". By the beginning of the 1960's, tax professionals and businessmen increasingly came to the conclusion that their various complaints regarding the nature and administration of taxes could best be resolved by a major overhaul of the taxation system rather than just the customary annual budgetary amendments. While placing the problem on the political agenda, they contributed their own definitions of it through professional conferences, corporate board meetings, business and professional periodicals, the popular press, and personal contacts among the two major political parties.

In describing the appointment and formation of the Royal Commission, Chapter III also examines the processes by which elite definitions of the problem continued to be propagated, largely through the press coverage of the decision to appoint the Commission. The chapter then examines the approach taken by the Commissioners and their staff to their terms of reference and how organizational processes within the Commission affected the Commissioners' definition of their task. A different organization, with different people in key positions, would almost certainly have produced a different report.[39]

The Commission stage included the evaluation of alternative recommendations for reform, which proceeded simultaneously and at

times even independently of the continuing process of problem definition within the Commission. Being parts of a substantial organization, the Commissioners and their staff at different levels did not all share in the same perception of the problem or of reform alternatives. The decision-making process at this stage was not simply an open-minded attempt at a definition of the problem followed by a search for and evaluation of alternatives, but also a protracted attempt at persuasion and education of one portion of the Commission by another. Chapter IV traces this search for alternatives within the Commission until the Commissioners finally hammered out a majority decision on key questions in late 1964 and early 1965. In struggling with themselves over the evaluation of alternatives, the Commissioners and their staff gradually arrived at a new appreciation of the problem.

The tax professionals had considered the salient problems of the definition of capital gains and of surplus stripping independently. The former they perceived initially as a problem to be settled by the courts using accepted principles of judicial interpretation. Then, as judicial decision-making failed to result in a consistent policy, the practitioners came to view it as a problem of arriving at a clearer legislative demarcation of income from non-taxable capital gains. The surplus stripping problem had been perceived primarily as an understandable (though slightly shady) response by hard-pressed owners of closely-held corporations to avoid financial ruin in the face of high income tax rates and heavy death duties.

However, the Commissioners' evaluation of the preferred

alternative eventually put forward by the Director of Research and some members of the research staff, caused them to view the problem in a new light. To a majority of Commissioners, the two problems -- the definition of capital gains and the problem of surplus stripping -- were really different aspects of a single problem. There was no clear distinction, nor could there be, between "income", which was taxable, and "capital gain", which was not; hence the erratic nature of judicial decisions on the question. At the same time, surplus-stripping could be seen as an attempt by owners of closely-held corporations to secure the same tax treatment for undistributed corporate income as was easily available to owners of corporate shares which could be traded on the stock market. The only equitable solution, the taxation of capital gains at the same rates as other income, also provided the solution to the related problem of the definition of capital gains. The definition of the latter would cease to be a problem because capital gains as such would be defined out of existence, becoming instead "income" to be treated like profit, rent or salary.

This solution also helped to rectify the existing gross departure from the principle of vertical equity, since most of the tax-free capital gains accrued to high-income taxpayers. In addition, the state's tax revenues would be secure from most existing tax avoidance devices and the extra revenue from taxing property gains would allow death duties to be eliminated and the top marginal rates of personal income tax to be reduced. An inseparable part of this alternatve was the integration of corporate income accruing to individuals with the

rest of their personal income, thereby taxing corporate-source income at personal progressive rates, though at lower rates than had existed before, and to tax it only once regardless of whether or not it was actually distributed to the shareholder.

This alternative, which the majority of Commissioners concluded would have made surplus stripping both impossible and unnecessary, was long an underdog in the Commission's consideration of a range of alternatives. It won out only after the failure of competing solutions to survive the critical scrutiny of the Commission's research staff, by its attractive simplicity, and the apparently definitive solution it offered to a number of complicated tax problems which had originally motivated the appointment of the Commission.

As persuasive as they may have appeared to members of the Commission's research staff, these facts did not speak for themselves. They required the relentless effort of Douglas Hartle in the key position of Director of Research who repeatedly played for time against pressure from the Minister of Finance and Carter to publish a more hasty report, while continuing to press forward his preferred alternative. The facts themselves were persuasively packaged in two key research studies on capital gains carried out by Geoffrey Conway, a research supervisor, who had from the beginning favoured the comprehensive income concept, and his assistant John G. Smith. Of critical importance was the presence of men at the head of the Commission who understood tax problems intimately and could fully appreciate the force of the arguments advanced by Hartle and Conway

and, once convinced, effectively defend that position as their own. Without personalities like the Chairman, Kenneth Carter, Commissioner J. Harvey Perry, and John Stewart, a trusted friend and colleague of Carter as Counsel to the Commission, all of whom possessed impeccable professional credentials, and who were, in the final analysis, unwilling to bow to what they saw as expediency, the comprehensive income concept would have remained confined to the academic writings of public finance specialists. Instead it gained the circulation and legitimacy of the key recommendation of a Royal Commission report, thus placing that policy option at the top of the political agenda.

Having examined the process leading the Commissioners to their decision, Chapter V then examines its content, the assumptions behind it and the reasoning advanced in its support. The exposition and analysis of the Report demonstrates both the strength of the Commissioners' statement of the comprehensive income concept as a policy proposal, and their perception of the limitations of any tax reform policy in a capitalist market economy which is open to the most powerful capitalist economy in the world. Though these limits to tax reform were derived from the Commission's research studies and from assumptions shared by most economists of the period, the reader will be reminded of the account in Chapter IV of the lessons learned by Kenneth Carter during his tax research excursions to the United States and Europe.

The Carter Report is also significant for the authoritative way in which it presented its research on the Canadian tax system. In order

to appreciate the impact of the Report on subsequent events, one must bear in mind that this Commission is unsurpassed by any other in terms of the thoroughness and depth of its research.[4] The Report did not simply tell its readers what was wrong with the tax system, it also took them from basic principles with which most might agree, and logically demonstrated that the solution recommended by the majority of Commissioners was the best possible one for Canada at that time. Chapter V also describes the reports of the two dissenting Commissioners, Emil Beauvais and Donald Grant, showing where and how they disagreed with the majority. Their objections were later picked up and amplified by many critics of the majority Report, and the Act of 1972 resembled more the alternatives favoured by Beauvais and Grant than it did those of the majority.

With the publication of the Report in February of 1967, the scope of the decision-making process once again widened to include all politically relevant members of society. At the same time, the process had also narrowed in scope, as important decisions were being made within Cabinet and the Department of Finance. The government and "the Department" had never been absent from the picture, but during the life of the Commission, they are treated in this study as external forces and considerations -- things that the Commissioners and their staff had to reckon with. Chapter VI, "Reaction to the Report", examines both the wider context, the reaction of the media and other non-governmental political actors to the Report, and also the narrower context, the events taking place within the government and the Department of Finance. Due to the secrecy in which government in

Canada operates, the level of information concerning the internal governmental processes falls far short of what was available on the operations of the Royal Commission or on the press coverage of various stages of the reform process.[40] Nevertheless, enough information concerning the decision-making process has been collected from secondary sources and interviews to sketch in the key events.

We can discern that the problem as defined by the government at that time was less one of choosing the best reform alternative, or which of the Commission's recommendations to implement (although such activities were taking place within the Finance Department), but more one of selecting an institutional process which would allow the issue of tax reform to percolate a little more before the government was forced to stake out its own position. The publication of the Report had not moved public opinion toward consensus, but rather created a lop-sided polarization of opinion on tax policy, one slanted against the comprehensive tax base. Opinion within the government was also divided, making any coherent decision unlikely. Something was needed to allow the various interests to fight it out, and in the process make their positions and the relative weight of their influence felt. At the same time, a policy statement on the Carter Report had been promised and was widely expected. The Opposition parties repeatedly raised the issue in the House of Commons and would not let it be forgotten. Yet the political costs to the government of taking a position for or against specific proposals in the Report were largely unknown. Chapter VII concludes that the White Paper served the purpose of tentatively indicating a tax reform policy while

encouraging everyone outside the government to criticize it. The political risks of this half-step toward tax reform were thus minimized, as the potential force of the opponents and supporters of reform alternatives could be gauaged before the government committed itself to any particular alternative.

The White Paper also served to re-define the problem of tax reform as it had been stated by the Commission. The Carter Report had said that equity, or fairness, was the primary objective of any good tax system, and that the other goals of economic efficiency, administrative simplicity, compatibility with the principles of democracy, individual freedom and federalism, though worthy values in themselves, depended for their effect upon the maintenance of an equitable taxation system, and thus were not essentially in conflict with the equity objective. The Report's coherent and persuasive formulation of the issue made compromise and tactical retreat difficult for the government, for it did not point to any clear trade-off among widely-desired objectives within which the government could manoeuvre. As long as those interests favouring progressive tax reform were wedded to the formulation of the Carter Report, they could not be marshalled to a compromise position which would be less objectionable to many business and professional interests which had and might continue to support the Liberal government. The White Paper, assisted by the passage of time and the short memory of popular journalism, re-defined the meaning of tax reform, thus shifting the fulcrum of the debate toward the political centre and allowing the government to organize a coalition in favour of the new definition of

"reform".

The White Paper viewed equity as an important objective but did not give it the logical primacy accorded it in the Carter Report. It departed from the comprehensive income concept in its treatment of corporate share gains, gifts and bequests, the mining and petroleum industries, among others. Nor did the White Paper have the same impregnable logic and coherence as the Carter Report. Its separation of closely-held and widely-held corporations for the taxation of capital gains and integration was an easy target for tax professionals. The increases in tax rates for middle-income Canadians aroused fierce opposition from that sector, and even from tax specialists and economists who had supported the Carter Report. The elimination of the low rate of tax on the first $35,000 of corporate income created a "small business" lobby dedicated to the eradication of the White Paper proposals. The proposed treatment of mining and petroleum income, though more generous than that offered in the Carter Report, united those industries with several provincial governments in fierce opposition. Put forth by the government only as proposals for public discussion, the one-sidedly critical tenor of the public response dictated major concessions from the government.

The White Paper debate made concessions to business and professional critics easier by providing a legitimizing ideology (that of public participation in policy-formation) and a legitimate arena (the House of Commons Standing Committee on Finance, Trade and Economic Affairs) in which to display the views of participants and to

announce the concessions. By encouraging "everyone" to "participate", the very substantial differences in the relative influence exerted by each would be blurred: a few wolves among a large herd of sheep might escape notice. Instead of making controversial concessions to business interests, the government could bow to the "public will" as interpreted by an unfettered committee of the House of Commons. The popular legitimacy of the Commons Committee and of its report was enhanced by juxtaposition with the Senate Committee on Banking, Trade and Commerce and the latter's report. Lest anyone charge that the Commons Committee was catering to the dictates of capital, one need only point to the Senate's report to show what the representatives of capital were really asking.

The government's tax reform legislation, Bill C-259, codified the concessions made during the White Paper debate, added the half-inclusion of capital gains in income and eliminated federal gift and estate taxes. Although the bill was not very different from the compromise position on the tax base advocated by the dissenting commissioners and many tax professionals, pressure from business critics and the co-operative movement and the Opposition parties persisted, extracting further concessions during parliamentary consideration of the bill. The final concessions during the legislative stages and the relevant features of the Bill as enacted are discussed in Chapter VIII, "The 1971 Tax Reform Legislation". Though the story for our purposes ends at the parliamentary approval of the bill, part of the price of its speedy passage through the Senate was the promise of further concessions favourable to

investors. Erosion of the partial reform began with the following budget and continued during the years following the proclamation of the new Act.[41]

Participation, Pluralism and the Structure of Power

In the sense that institutions were available for people to register their opinions, that information on a range of policy options was placed in the public domain, and that large numbers of people took advantage of these opportunities, public participation was a real element of the tax reform process. However, the process was less real in substance than in form, in terms of openness to the views and interests of the majority of adult Canadians. The interests which were heard at most stages were those representing privileged sectors of society, and who feared the loss of tax advantages through the adoption of any reform resembling the Carter comprehensive income concept. The voices speaking on behalf of the tax underdogs -- the lower income-earners, especially those earning wages and salaries, and also the poor and the unemployed -- were few and ineffective. Ironically, the interests of the lower-income earners were most effectively advanced when the scope of participation was most restricted: during the closed deliberations of the Commissioners and their senior staff, and (to a lesser degree) during the writing of the White Paper within the Department of Finance. The more open and "democratic" fora -- the public hearings of the Royal Commission, the media coverage at each stage, the public hearings of the parliamentary

committees, and the legislative debates -- served in general to reinforce the already overwhelming advantage of the economically powerful.

A close look at the "participatory" stages of tax reform shows the narrow class base of what might at first appear to be widespread public involvement. The opposition to the comprehensive income concept came from businesses of every description, big and small. It is quite remarkable that virtually all sectors of private capital would be so united on a political issue. Although the Carter recommendations would likely have benefited most manufacturing industries, most small and middle-sized entrepreneurs and investors, only organized labour, welfare groups, most academic professionals, the New Democratic Party, and the Communist Party spoke consistently in defence of the Report. In the light of this opposition to tax reform, and the weakness and marginal legitimacy of some of the forces defending the Carter Report, the timidity of the minority Liberal government of 1967, and even of the majority Trudeau government in 1968 during the tenure of Mitchell Sharp as Minister of Finance, is understandable. By contrast, the eagerness of Edgar Benson to get on with tax reform must have appeared naive and foolhardy to some of his Cabinet colleagues.

Although fitting generally within the pluralist genre in terms of its approach to the question of political power through studying the decision-making process, this study departs from pluralist conclusions regarding the distribution and exercise of political power. Over the

decade-long period of tax reform examined here, many political actors came and went and a large number of groups and interests had their say. However, all but a few came from, or represented a small spectrum of society -- investors, entrepreneurs, senior business executives and tax professionals -- people who had become tax-wise in the course of their personal and professional lives. Due to the past high progressive rate structure, they would have expected to pay marginal rates of income tax as high as 80 per cent, if it were not for the existence of avoidance devices.

The number of people in Canada at that time sufficiently knowledgeable about tax matters to speak with some confidence about the subject in an open forum would probably have been in the order of a few hundred individuals, depending upon the level of knowledge and confidence considered to be adequate. Most were tax professionals, usually lawyers, chartered accountants or economists, who had invested the considerable time and effort required to understand the tax system. Given the existing economic and tax environment, anyone in possession of such knowledge could command a high price in the market place for his services. The major consumers of tax advice were large corporations and wealthy individuals. Not surprisingly, many of the tax professionals had made productive use of their own good counsel, combined it with business acumen and some capital, and made themselves into substantial business owners and executives in their own right. The tax professionals outside the universities who were not themselves corporate executives looked to that sector for potential or actual clients, and as people moving in the same business world as

themselves, facing similar problems. The corporate business point of view on taxation was for most of them as familiar and axiomatic as their daily bread.

The tax professionals had provided the technical expertise which had enabled the owners of corporate wealth to minimize the bite taken by the state with each fiscal period and each generation, and helped them to spin the corporate webs which preserved their dominion over the family holdings. Ideally equipped to understand the needs of the major corporate executives and shareholders and to represent their interests in matters of tax planning, tax administration and tax policy, the chartered accountants and tax lawyers constituted a vital link between corporate wealth and political power.

When this symbiotic relationship of tax professionals with business is considered along with the central importance (with the partial and qualified exception of the internal Commission deliberations) of tax professionals at all stages of the tax reform process, then the overall tax reform process bears little resemblance to pluralist formulations. Although advice and pressure on the central political machinery came from a large number of individuals and organizations, the few dissenting opinions were drowned out by the dominant voice of investment capital. The "small business" lobby was part of this monopoly of political influence, as it simply reinforced the demands of investment capital at the expense of labour. The form was pluralist, the content monopolist.

However, the analysis cannot stop at simply counting heads, gauging the strength of voices, and tracing relationships among the partisans on each side of the issue. The concluding chapter recalls the logic of the arguments brought against the proponents of tax reform and of the Carter income concept. These were essentially structural arguments, pointing to the economic imperative to provide for sufficient employment opportunities for Canadians by offering capital a reward attractive enough to ensure future investment. Even the authors of the Carter Report had to acknowledge the force of this argument, though they drew the balance much closer to the side of progressive reform. Such arguments do not depend for their effect upon the number of tax professionals in or close to the corporate elite, although numbers and access ensure that the argument is heard clearly and often. The same arguments concerning the imperative of rewarding capital investment could in principle be made by, and in fact, were directed to, employed and unemployed workers. The discussion of the reactions to the Carter Report in Chapter 6, and of the White Paper debate in Chapter 7, suggests that such arguments are very persuasive, especially when couched in the form of rumoured or announced investment deferments and plant closings.

Among the people putting forward such arguments were those in control of substantial investment funds, and therefore, in a very practical sense, they knew what they were talking about. The losers of the Great Tax Reform Debate -- wage-earners and most salaried workers, the poor and marginalized, and all who spoke on their behalf -- were, in the final analysis, defeated by a structural phenomenon

over which they had very little control. Carter had seen milder forms of the same contradiction during his European tax excursion -- senior tax administrators in most of the countries he visited repeatedly referred to the same dilemma: "How do you make investment capital pay its fair share of the tax burden when it can easily leave for greener pastures abroad?" Given the constitutional and political framework of government in Canada, the level of political consciousness among Canadian workers during the 1960's and 1970's, and the world dominance of the multinational corporations in directing investment flows, the conclusion of the debate could not have been in substantial doubt.

Finally, the study explores the implications of these findings for the structure of power in Canada. The assumptions and constraints contained in the Carter Report are recalled and compared to the reforms enacted in 1971. The very sizeable gap between the two is attributed to factors relating to both the Report itself and to the Canadian political economy. The Report was based largely upon an economic analysis of what was required to ensure acceptable levels of economic performance -- what profit-seeking investors and entrepreneurs operating in Canadian and world markets would likely tolerate in terms of a tax regime. Investment capital was looked upon as a market phenomenon, as a fluid flowing toward the most favourable rate of return, not as a social and political force. Little attention was given to the political impact of economic activity; whether the particular industrial structure existing in Canada would put tighter constraints on possible tax reform than those allowed for in the Report. Much of the opposition to the Report related to the toll it

proposed to exact from the inter-generational transfer of wealth and the implications which this might have for the control of corporations by Canadian families. Family business in Canada means more than the neighbourhood variety store; many of the largest Canadian corporations are controlled by families and small groups of individuals, often with minority ownership and through chains of holding companies. The effective rate of taxation for these wealthy families does not simply affect the net rate of return on investment, but, if the real burden were increased substantially, it might endanger their control over their corporate empires.

A second characteristic of the Canadian economy was the regional concentration of the production activities of large resource-based corporations. Most were subsidiaries of American or other foreign corporations, and most (as their spokesmen took pains to point out) had other centres of operation in other countries. Other sectors in the economy looked to them as customers, suppliers and outlets for investment capital. They were therefore in a position to, and did, threaten withdrawal of investment capital or suspension of planned investments. Thus, a transmission belt existed between corporate wealth and political power, one discernible only when the belt was under tension: as the drive wheels turned in the corporate head offices, the belt tightened, and the pulleys in various provincial capitals, municipalities and federal constituencies began to move.

Notes Ch. 1

1. Report of The Royal Commission on Taxation, Vol. I (Ottawa: Queen's Printer, 1966), p. 6.
2. See the special issue of Canadian Public Administration, "Governing under Pressure", Vol. 25, No. 2 (Summer, 1982), esp. K.Z. Paltiel, "The changing environment and role of special interest groups.
3. Budget Speech, delivered in the House of Commons, June 18, 1971.
4. Ibid.
5. Edgar Benson, Minister of Finance, Proposals For Tax Reform, (Ottawa: Queen's Printer, 1969), henceforth referred to as the White Paper.
6. Leo Eisenstein, Ideologies of Taxation (New York: Ronald Press Co., 1961), pp. 156-157.
7. C.B. Macpherson, The Life and Times of Liberal Democracy, (London/New York: Oxford, 1977), p. 77.
8. "Pressure Groups: Adaptive Instruments of Political Communication", in Pross, ed., Pressure Group Behaviour in Canadian Politics", (McGraw-Hill Ryerson Ltd., 1975), pp. 1-24.
9. Frederick Engelmann and Mildred Schwartz, Political Parties and the Canadian Social Structure (Scarborough: Prentice-Hall, 1967), pp. 96 and 113.
10. The Canadian Political System, Environment, Structure and Process (Toronto: McGraw-Hill, 1971), particularly Ch. 13, "Interest Groups in Canadian Politics", pp. 297-321.
11. Robert Presthus, Elite Accommodation in Canadian Politics (Toronto: Macmillan, 1973).
12. Pross, p. 18.
13. (Toronto: University of Toronto Press, 1965).
14. Porter, pp. 556-557.
15. Porter, pp. 522-523.
16. Porter, pp. 532, 20-28.
17. Porter, p. 25.
18. See, for example, Pross, op. cit., p. 7. A more recent discussion of interest group politics in Canada, see the proceedings of a seminar sponsored by the Institute of Public Administration of Canada, the papers for which were published in Canadian Public Administration, Vol. 25, No. 2 (Summer, 1982). The contributions of A.P. Pross "Governing under pressure: the special interest groups -- summary of discussions" and K.Z. Paltiel, "The changing environment and role of special interest groups" discuss pluralist and opposing theories.
19. An Economic Theory of Democracy (New York: Harper and Row, 1957).
20. The Logic of Collective Action: Public Goods and the Theory of Groups (Cambridge, Mass.: Harvard University Press, 1965).
21. The Politics of the Expenditure Budget (Toronto and Buffalo: Ontario Economic Council, 1976); The Revenue Budget Process of the Government of Canada: Description, Appraisal, and Proposal (Toronto: Canadian Tax Foundation, 1982); and, in collaboration with M.J. Trebilcock, R.S. Prichard and D.N. Dewees) The Choice of Governing Instruments (Ottawa: Department of Supply and

Services, 1982).

22. Federal-Provincial Diplomacy: The Making of Recent Policy in Canada (Toronto: University of Toronto Press, 1972).
23. The Politics and Management of Canadian Economic Policy (Toronto: Macmillan, 1978).
24. How Ottawa Decides: Planning and Industrial Policy-Making 1968-1980 (Toronto: James Lorimer & Co., 1980).
25. The Politics of Anticipation (Ottawa: Carleton University School of Public Administration, 1980).
26. Simeon, p. 307.
27. Ibid., p. 309.
28. French, pp. 152-154.
29. Among the more frequently cited works are the collection edited by Leo Panitch, The Canadian State (Toronto: University of Toronto Press, 1977) and Wallace Clement, The Canadian Corporate Elite, (Toronto: McClelland and Stewart, Carleton Library No. 89, 1975).
30. The Redistribution of Income in Canada (Toronto: McClelland and Stewart, Carleton Library, No. 124, 1980), pp. 165-167; and John Bossons, "Economic Overview of the Tax Reform Legislation", Proceedings of the Twenty-third Tax Conference, (Toronto: Canadian Tax Foundation, 1972), pp. 45-67.
31. R.M. Haig, "The Concept of Income", in The Federal Income Tax, ed., R.M. Haig, (New York, 1921), Henry Simons, Personal Income Taxation: The Definition of Income as a Problem of Fiscal Policy (New York, 1938), and Simons, Federal Tax Reform (1950).
32. New Haven: Yale University Press, 1961). See also, Dahl, "A Critique of the Ruling Elite Model", American Political Science Review, Vol. LII, No. 2 (June, 1958) pp. 463-469, Pluralist Democracy in the United States: Conflict and Consent (Chicago: Rand McNally, 1967), and Nelson Polsby, Community Power and Political Theory, (New Haven: Yale University Press, 1963).
33. Community Power Structure (Chapel Hill: University of North Carolina Press, 1953).
34. The Power Elite (New York: Oxford University Press, 1956).
35. Who Rules America? (Englewood Cliffs, N.J.: Prentice Hall, 1967), The Higher Circles: the governing class in America (New York: Random House, 1970), Powers that be: processes of ruling -- domination in America (New York: Random House, 1978), and Who Really Rules? (Santa Monica: Goodyear, 1978). Ralph Miliband, The State in Capitalist Society (London: Redwood Press Ltd., 1969) summarizes analogous studies for Britain, France, Germany and Japan as well as the United States. Miliband's chief purpose was to show that these countries do not fit the pluralist model.
36. Bachrach and Baratz, "Two Faces of Power", American Political Science Review, Vol. LVI (Dec., 1962), pp. 947-952, reprinted in Charles A. McCoy and John Playford, eds., Apolitical Politics: A Critique of Behavioralism (New York: Thomas Y. Crowell co., 1967), "Decisions and Non-decisions; An Analytical Framework", American Political Science Review, Vol. LVII (Sept., 1963), pp. 632-642; and Power and Poverty: Theory and Practice (New York: Oxford, 1970).
37. The Semi-sovereign People, (New York: 1960), p. 71. The debate

over pluralist theories of politics continues. See John F. Manley, "Neo-Pluralism: A Class Analysis of Pluralism I and Pluralism II", and rejoinders by Charles Lindblom and Robert Dahl, in American Political Science Review, Vol. 77, No. 2 (June, 1983), pp. 368-389; and Colin Crouch, "New Thinking on Pluralism", The Political Quarterly, Vol. 54, No. 4 (Oct.-Dec., 1983), pp. 363-374.

38. As we are talking about the essence of conscious activity, the literature touching on this subject is practically limitless. In the context of organizational decision-making some of the basic references are Herbert A. Simon Administrative Behavior (New York: Macmillan, 1947, 1957, 1961), and The New Science of Management Decision (New York: Harper and Row, 1960), and James March and Herbert Simon, Organizations (New York: John Wiley and Sons, 1958). Among the important writings on public sector decision-making are Charles E. Lindblom The Intelligence of Democracy; Decision Making Through Mutual Adjustment (New York: Free Press, 1965), and The Policy-Making Process (Englewood Cliffs, N.J.: Prentice-Hall Inc., 1968), David Braybrooke and Charles E. Lindblom, A Strategy of Decision: Policy Evaluation as a Social Process (New York and London: The Free Press, 1963, 1970), Geoffrey Vickers, The Art of Judgement: A Study of Policy-Making (London: Chapman and Hall, 1965), Yehezkel Dror, Public Policy Making Reexamined (San Francisco: Chandler, 1968), Design For Policy Sciences (New York: American Elsevier Publishing Co., 1971), and Amitai Etzioni, The Active Society: A Theory of Societal and Political Processes, (New York: The Free Press, 1965), and a "Governmental Decision Making" symposium, including contributions of Dror, Lindblom and M. Heydebrand, in Public Administration Review, Vol. 24, No. 3 (Sept., 1964). I am indebted to Professor V. Subramaniam of the Department of Political Science at Carleton University for introducing me to this literature.

39. Most of the information pertaining to the Carter Commission was obtained from its records in the Public Archives of Canada, Record Group 33/65, comprising 157 volumes, access to most of which is restricted until 1993. Thanks to the cooperation of Mr. Jim Whelan of the Federal Archives and of Professor Douglas Hartle of the Institute for Policy Analysis of the University of Toronto, who had been the Commission's Director of Research, I was able to secure access to these records. Henceforth they will be cited as: PAC, RG 33/65, followed by the Volume number, the title of the document or the addressee and sender of the communication, followed by the date.

40. My requests to obtain access to the documents pertaining to the production of the White Paper did not receive a response. As the materials come under the heading of cabinet documents, the Freedom of Information Act cannot be invoked.

41. Colin Campbell, The Canadian Senate: A Lobby from Within (Toronto: Macmillan, 1978), pp. 16-17; Douglas G. Hartle, pp. 21-22, 33-34.

Chapter II: Origins of the Income Tax System

The political apparatus of any society can be activated to process only a very limited number of issues at any given time. While that machinery is thus occupied, all other issues must wait their turn, being detectable as "non-political" phenomena which place loads on various social institutions. Problems are not promoted to the status of political issues in a naive fashion. Just which subjects become political issues, how the problems requiring authoritative resolution are defined, and the characteristics of the political apparatus itself, are indicative of the relative power of different classes and groups within that society.

With these relationships more-or-less established, the various contending interests try to impose their will through the political process. The result of the struggle is then legitimized in some way so that the losers will live with their disappointment. The problem, having been "solved", at least in a political sense, is submerged once again amid other social phenomena. If the problem has not been solved in a substantive or technical sense, or if social change undermines the effectiveness of the political solution, then pressures will mount to place the issue on the political agenda once again.

The most fundamental tax controversy is a potentially explosive one: who, or which part of society will support the economic burden of the state? It is in the interests of those who have managed to

shift the burden onto others to keep the question away from the hazards of politics. Only the widespread perception among the powerful of some crisis justifies, in their eyes, resort to re-negotiation of this key provision of the social compact. Five critical periods can be detected in Canadian history when the general character of the tax system was placed on the national policy agenda: the financial and constitutional disarray leading to Confederation; the failure of indirect taxation to cope with the combined costs of railway construction and World War I; the failure of financial and constitutional arrangements during the Great Depression; the sudden expansion of state activities and imposition of very high taxes during World War II; and finally, the tension resulting from the growing revenue needs of all levels of government combined with structural weakness in the post-War tax system. From the settlement of the first four of these taxation debates emerged the institutions, practices, expectations, power relationships, and the problems leading to the appointment of the Royal Commission on Taxation in 1962.

Financing Development: the Colonial Period

The problem of government finance has always been a factor of great importance in Canadian political history. It has long been recognized that heavy colonial debt burdens, arising largely from government financing of the transportation infrastructure, provided an effective stimulus toward Confederation. The inability of the debt-ridden and virtually defenceless British North American colonies

to float long-term loans on the London bond market in 1866 provided a compelling financial signal to colonial politicians that they should consolidate the debt under the responsibility of a single authority with a significant revenue-raising capacity.[1] Key elements in the Confederation agreement were the assumption of colonial debts by the Dominion government and payment of subsidies to the provincial governments.

The colonial governments had customarily relied upon "indirect taxes", that is, taxes which were intended to be paid by economic intermediaries of those who were expected to bear the actual burden of the tax. These usually took the form of customs duties paid by the importers of goods, the burden being passed on to colonial consumers. The Confederation agreement made the field of indirect taxation the exclusive domain of the Dominion government, while the provinces were to be restricted to direct taxes and licences. As direct taxes were not popular with colonial electorates, it is likely that their allocation to the provinces was an indication that the Fathers of Confederation expected the provincial revenue needs would be very modest, or at least that restriction of their taxing powers would limit their spending.[2]

The Confederation settlement gave the Dominion government the financial burden, the functional responsibilities, and the taxing powers associated with the project of national economic development. While this consolidation of tasks and means was achieved only on the threshold of a decade of economic depression, it nevertheless

confirmed the pre-Confederation pattern of state subsidization of private entrepreneurship, especially in transportation infrastructure, for most of the next century. Subsidies often took the form of government guarantees for private stock and bond issues, with the government assuming the debt in the event of the default of the company.[3] This infrastructure was therefore financed by a combination of user charges on shippers using the railways and canals, and also by tax revenues which went to pay the subsidies and the interest on debts assumed by the government. Since most of the tax revenues were from customs duties and as the shipping charges on imports were added to the cost of goods purchased in British North America, the major costs of economic development were financed by levies on consumption. This was a highly regressive pattern of taxation, as those wealthy enough to have surplus income beyond that required for personal consumption were free of tax on the balance available for saving. Beyond local property taxes, which in some cases included modest (and probably poorly enforced) taxes on personal property, there were few fiscal restrictions on the private accumulation of wealth. Much of this private capital found its way into railways and other transportation investments which, as we have seen, also enjoyed more direct forms of state subsidy.

Private entrepreneurship was therefore twice blessed: first, in the form of tax-free income available for private investment, and second, (to the extent that the funds were invested in favoured sectors) in the form of government guarantees and subsidies. The relatively more important role of the state in Canadian economic

development compared to that of the United States has often been noted. What is sometimes overlooked is the fact that the state's function was not simply that of aiding economic development, but also of ensuring through regressive consumption taxes that the majority of people who possessed little personal wealth paid a disproportionately large share of the costs. The flip-side of the coin of the state as the driving force of economic development is that of the state as an engine of private capital accumulation through compulsory transfers from the less well-to-do, chiefly the family farmers. The Canadian state has, from the beginning, been a partner with private capital in the integrated business of income redistribution and private capital accumulation.

This would have been less true had the colonial governments, and later, the Dominion government, relied on direct, progressive taxation. Direct taxation, however, was not on the political agenda, and this remained so throughout the depression of the 1870's, the economic doldrums of the 1880's and early '90's, and the long period of prosperity around the turn of the century. While we are accustomed now to think of the tariff as a device for protection of domestic industries against foreign imports, before the introduction of the National Policy tariff of 1878 the tariff was considered chiefly as a revenue raising device, that is, a tax. The National Policy does not appear to have reduced the effectiveness of the tariff in raising revenue: between 1868 and 1913, customs revenues accounted for more than half of Dominion revenues in almost every year.[4]

Although two provinces and some municipalities at times levied taxes on personal property, certain incomes and on real property, they were not very successful revenue producers, apparently due in part to the ease of concealing property and income arising from ownership of financial securities.[5] Generally however, the regressive pattern of public finance set during the colonial period and consolidated at Confederation persisted until the second fiscal crisis, which ushered in the era of the income tax in Canada.

Financing the Great War

Depression in 1912 caused a sharp drop in imports and a parallel decline in customs revenue, the chief source of financial support for the Dominion government. This situation continued on into the First World War, when Dominion expenses increased rapidly, not only with the expenses of the War, but also with the added burden of assuming the funded debt of two bankrupt transcontinental railways.[6] The failure of the tariff as a revenue source, combined with the great increase in expenditures, forced the Dominion government to choose between tapping new revenue sources (such as a direct tax on incomes), or borrowing and causing inflation. The prospect of a direct tax on incomes was sufficiently disagreeable that, at first, the government chose borrowing and inflation. The Minister of Finance of the time, Thomas White, specifically rejected a tax on incomes as requiring new administrative and enforcement machinery, yet raising comparatively little revenue, and infringing on the tax fields of the provinces.[7]

However, the inflation resulting from the war production boom and government borrowing led to public pressure for a tax on scandalously large war profits. The Borden government responded with the imposition of a Business Profits Tax of 25 per cent on annual profits in excess of 7 per cent of capital employed in corporations, and in excess of 10 per cent of capital employed for other businesses.[8] Worsening inflation, continued high profits, soaring war casualties, and a bleak military outlook pressed the Union government, in the budget of April, 1917, to increase the Business Profits Tax. The issue became tied in to the conscription crisis, with the slogan "conscription of wealth" (as well as men) being widely repeated, especially among western farmers.[9] Finally bowing to what he called "manifest public necessity", White announced his intention to levy a tax on personal incomes.[10]

The Income War Tax Act of 1917 allowed an exemption of $1,500 for single persons, $3,000 for married persons, with the result that the tax hit only the middle and upper classes. The marginal rates started at a modest level of 2 per cent, climbing to 29 per cent on incomes over $100,000.[11] During the final two years of the War, the Income War Tax Act did not raise much revenue: when combined with the revenues from the Business War Profits Tax, direct taxes on income accounted for only $42 million of $802 million in tax revenue raised during the War years.[12] Direct taxes on income, therefore, although introduced as a war measure, did not contribute substantially toward financing the war effort during the period of hostilities. The War

was paid for largely through regressive indirect taxes on consumption and through inflation. Although the War saw the introduction of a nominally progressive tax on incomes, the pre-War pattern of financing expenditures by regressive taxes on consumption continued.

War expenditures did not end in 1919. Aside from demobilization expenditures, including pensions, there was interest to pay on the national debt. These payments, which reached a peak of $139.6 million in 1921, went largely to pay tax-free interest to the holders of war bonds. After its introduction in 1917, the rates of personal income tax were raised in 1918 and again in 1919, so that marginal rates went from 5 per cent on $1,500 of income for single persons, to about 65 per cent at the $200,000 income level. Judging only from the rate structure, it would appear that the Dominion Government was making a transition from a pattern of regressive taxation to a more progressive system. However, when one takes into account the fact that bond interest (which likely went mostly to high-income taxpayers who had purchased war bonds out of their inflated war profits) and most capital gains escaped taxation, then the only conclusion that one could draw with any confidence, was that the income tax was becoming an important element of the tax system, and that the nominal rate structure was, in itself, decidedly progressive. The increasing importance of income tax revenues combined with the heavy debt burden of the post-War years explains the long survival of the Income War Tax Act.

Income Tax, Tax Avoidance and Tax Consciousness:

The progressive rate structure and high top marginal rates gave rise to persistent efforts on the part of high-income taxpayers, both individually and collectively, to avoid its impact. Individually, the effort took the form of tax avoidance: the manipulation of transactions in order to escape the application of the letter of the Act. This in turn gave birth to a tax avoidance industry as professional tax advisors mobilized to collect their share of the tax savings.

While there was some reduction in tariffs in 1919-20, the immediate post-War trend was towards more taxes and higher rates. In addition to the higher rates and greater variety of taxes, the mode of collection of the new taxes -- the income tax from middle- and upper-income individuals and from corporations, and a sales tax from manufacturers and wholesalers -- contributed to an increasing tax consciousness in business circles. Indicative of this new tax consciousness is the founding of the Citizens' Research Institute of Canada in the early 'twenties. The Institute sponsored an annual Canadian Tax Conference, beginning in 1923 which "provided a public forum for the annual discussion of tax problems", and was used by business interests to propagate lessons on the evils caused by high and ill-conceived taxes.[13] Most of the complaints voiced at these conferences were directed against the income tax, particularly the high personal rates, which were said to encourage emigration to the U.S.[14] While applying political pressure, both directly on

politicians and through organizations such as the Citizens' Research Institute, individual taxpayer skirmishes with the Income Tax continued. Successful tax avoidance depended chiefly on arranging one's economic gain in such a manner as to have it fall outside the legal definition of income.

Income and Capital Gains:

The Income War Tax Act levied a tax on income defined in a broad fashion:

> ..the annual net profit or gain or gratuity, whether ascertained and capable of computation as being wages, salary, or emoluments, or as being profits from a trade or commercial or financial or other business or calling, directly or indirectly received by a person from any office or employment, or from any profession or calling, or from any trade, manufacture or business, as the case may be whether derived from sources within Canada or elsewhere; and shall include the interest, dividends or profits directly or indirectly received from money at interest upon any security or without security, or from stocks, or from any other investment, and, whether such gains or profits are divided or distributed or not, and also the annual profit or gain from any other source...[15]

This was followed by a list of eight classes of receipts to be treated as income, though the introductory phrase "and also the annual profit or gain from any other source including" clearly implied that the list consisted only of specific examples of income, not a definitive list. While this section would appear to include everything resembling the common-sense notion of income, this was not the way the learned judges of the

Canadian courts (and until 1949, the Judicial Committee of the Privy Council) perceived the matter. Although much of the language of the Canadian law was borrowed from American statutes, the judicial interpretation of the Canadian Act generally followed United Kingdom jurisprudence. Hence, while the wording of Canadian and American income tax legislation was similar, judicial interpretation of the latter was broad enough to include capital gains in income.[16]

In the United Kingdom, a long history of estate law and (since the nineteenth century) of income tax law, had made a careful distinction between "income" and "capital". The legal concepts of income and capital were formed in a society where, until the nineteenth century, practically all income was agricultural: it was seasonal, recurring annually, and could be harvested and disposed of without impinging on the land, or source, from which it grew. The land and improvements of an estate, commonly enjoying legal protection, were not generally thought of as commodities to be bought and sold. The value of an estate was usually discussed in terms of the annual income which it yielded rather than in terms of its market value, and hence the familiar judicial analogy of income as the fruit and capital as the tree. English legal tradition distinguished the income of an estate, which might be placed in the possession of a "life tenant", who, while enjoying the income, could not legally encroach upon the corpus, or capital, of the estate, the latter being the right of the "remainderman". The idea that capital,

and increases in capital, were separate from income, developed through judicial interpretation of estate law, was carried over to income tax law in the nineteenth and twentieth centuries.[17]

Income and capital were therefore established legal concepts in Great Britain even before the first income tax was levied there in 1799. Since the non-taxable status of capital gains was not a matter of legal controversy during the 19th century, the statutes of the period made no reference to capital gains and no attempt was made in the statutes to define income.[18] Instead, the categories of income subject to tax were enumerated in a schedular form, one of which was designed to contain residual types of income with the wording: "the annual profits or gains arising from any kind of property whatever". However, the courts, following the traditional legal concept of income and the English judicial rule of construction that interpretation of taxing statutes must be based on the strict wording of the statute rather than the "spirit" of the law, gave the statute a narrow interpretation, allowing most capital gains to escape tax.[19]

In spite of the significant differences in the United Kingdom and Canadian statutes, the strict law of construction and the traditional concept of income were generally applied in the judicial interpretation of the Canadian statutes.[20] The legal definition of income was therefore largely derived from British custom and jurisprudence and tended to have the following

characteristics.

(a) It was of a recurring nature;

(b) was realized periodically (usually in each year);

(c) flowed from a fixed and constant source;

(d) did not reduce the basic value of the source when separated from that source;

(e) was the result of pursuing a specific activity.[21]

These characteristics of "income" were not part of a strict definition, but more a set of typical descriptive categories normally applicable to income. Judicial decisions were sometimes based on one or another category without reference to the others, making for considerable variation in the effective meaning of "income" from one case to the next. Depending on whether a taxpayer was able to establish to the tax assessor's (or the court's) satisfaction that his economic gain did not fit this description, nor the phrase contained in the United Kingdom statute, "an adventure or concern in the nature of trade", he might pay either no tax at all, or a very substantial levy based on his usually high marginal rate of tax. The resulting incentive to turn taxable "income" into tax-free "capital gain" made alchemists out of lawyers and accountants knowledgable in the subtleties of tax law, business organization, and the workings of the administrative machinery of National Revenue.

Surplus-stripping:

There was opportunity for many a slip between the brimming cup of private gain and the thirsty lip of National Revenue. An important variant of the capital gains techniques of tax avoidance, was the deferral of the paying out profits in the form of dividends to corporate shareholders and allowing the market value of the shares to rise. Instead of having to pay income tax on their dividend earnings, the shareholders might realize a tax-free capital gain when they sold some or all of their shares. However, unless the owners were prepared to lose control of the corporation, this expedient was not available where corporations were owned by only a few shareholders and the shares not listed on a public stock exchange. This afforded opportunities for enterprising tax advisers to devise what became known as "surplus-stripping" schemes, involving corporate re-organizations and sales of shares in order to circumvent legislation designed to bring undistributed corporate earnings within the tax net.

Surplus-stripping techniques were as varied as the imaginations of the ingenious tax advisors who invented them. Most included some form of corporate reorganization, wind-up or sale involving the transfer of shares from one closely-held corporation to another, and the ultimate receipt of the surplus by the individual share-holder in the form of a non-taxable capital gain.

Under the original Income War Tax Act, shareholders had to include in taxable income their portion of retained corporate earnings unless the Minister decided that the purpose was not to evade tax, or that the amount of undistributed profits was "not in excess of reasonable business requirements".[22] Following a 1924 United Kingdom court decision which declared that receipts pertaining to reorganizing or winding up a business were capital in nature and therefore tax-free, the Canadian statute was amended to include a section declaring that the distribution of property in any form on discontinuance, winding-up, or reorganization would be deemed to be a dividend to the extent of any retained surplus on hand at that time.[23] This was the first in a long line of loop-hole plugging exercises engaged in by Canadian taxing authorities. No sooner had one loop-hole been plugged, however, than another was opened by enterprising tax practitioners.

Arising out of the combination of the poorly-defined legal boundary between capital gains and income, the separate taxation of corporate and personal income, and historically high marginal tax rates on personal income, surplus-stripping continued to drain the state revenues and the morale of many taxpayers. Along with other forms of tax avoidance, and in the context of declining corporate and personal incomes, it contributed to the fiscal crisis of the Depression.

Financing Relief: the Great Depression

The economic collapse which began in 1930 was accompanied by a decline in tax revenues to all levels of government, while demands for government expenditures for relief became more pressing. Public debt burdens became so heavy that several provinces and many municipalities were unable to honour their financial obligations, casualties of the third Canadian fiscal crisis since the 1860's. Governments responded in a doggedly perverse manner, raising tax rates and introducing new taxes in vain attempts to offset increasing government expenditures. By 1940 all provinces had entered the corporate income tax field and seven levied taxes on personal income; in the case of Ontario, pushing the municipalities out of the income tax field.[24] At the Dominion level, income exemptions were lowered and rates were raised, especially at the upper end of the scale.

The primary significance of the Depression, for our purpose of understanding the tax reform era of the 1960's, lies in the increased importance of direct taxation in the Canadian political economy, the exacerbation of taxation problems, and the forced re-thinking of tax policies which the crisis precipitated. While figures vary with the definitions of taxes and economic activity, those compiled by J. Harvey Perry and reproduced in Figure 2-1 below, comparing total tax revenue to gross national product illustrate this general point. Between 1926 and 1930, the proportion of total taxes to gross national product oscillated around 13 per cent. Between 1932 and 1939 it never went below 16.6 per cent, and went as high as 18.3 per cent in 1933,

It is also significant that the share of direct taxes, notably income taxes, increased relative to indirect taxes.[25]

TABLE 2-1
TAXES COMPARED TO GROSS NATIONAL PRODUCT AND PERSONAL INCOME

Year	Total taxes/GNP (%)	Personal direct taxes/Personal Income (%)
1926	13.2	1.3
1927	13.0	1.4
1928	12.9	1.3
1929	13.0	1.5
1930	12.8	1.6
1931	14.7	1.7
1932	17.0	2.1
1933	18.3	2.4
1934	17.3	2.0
1935	17.2	2.4
1936	18.1	2.7
1937	17.3	2.8
1938	17.2	2.8
1939	16.6	2.6

Source: J. Harvey Perry, Taxes, Tariffs and Subsidies, p. 275.)

On the face of it, one might be tempted to conclude that the Depression had firmly established progressive taxation, or at least progressive income taxation in Canada. However, as the tax rates began to climb, ingenious taxpayers and their advisors were, like Canada's national animal, industriously gnawing away at the base. As much of the income not taxed was not even reported (the Income War Tax Act did not require the reporting of capital gains), reliable measures of the extent of this erosion of the tax base are practically impossible to obtain. This is the case not only for outright tax evasion, where income legally subject to tax was not reported as required by law, but also for most capital gains, which for upper

income taxpayers could have been comparable to their combined income from all other sources. While the marginal rates on the schedule gave the appearance of progressivity, the effective rates were more likely to have been proportional or even regressive over the upper income range where capital gains were significant.[26]

The Depression and the renewed tax onslaught from all levels of government dashed the hopes of the wealthy that the income tax might eventually be abolished, and once more aroused demands from business interests for tax and financial reform. The tax increases at all levels of government also gave new impetus to tax avoidance efforts. As government attempts to close tax loopholes and amendments in response to successful tax lobbying made the statutes increasingly complex, the need for professional advice became correspondingly greater.

Even those taxpayers who could afford the most ingenious tax advisers were unable to avoid completely the progressive rates on personal income. Hence, parallel to individual tax avoidance activities, there were lobbying and propaganda efforts to reduce the tax burden. The Citizens' Research Institute was one institutional manifestation of this pressure. Through its Taxation Branch, the Institute published reports "dealing with increased governmental expenditure and debt" intended to bring "prominently to the attention of all the need for lightening the burden on the taxpayer."[27]

As all levels of government scrambled for a greater share of tax

revenue from a shrunken national income, the conflict between the provinces and the Dominion over revenue sources, present to some degree since Confederation, was made more acute. The entry of more provinces into the income tax field, combined with the financial incapacity of some provinces to discharge their constitutional obligations, moved business interests, some provincial governments and provincial bodies of enquiry into fiscal problems to demand a major reform of the Dominion-provincial financial arrangements.[28] By 1937, The Bank of Canada, in its Reports on the Financial Position of the Provinces of Manitoba, Saskatchewan, and Alberta added its voice to the demands for reform, calling for a Royal Commission to "provide a comprehensive enquiry into the financial powers and responsibilities of all our governing bodies."[29]

The Rowell-Sirois Commission:

While the terms of reference of the Commission included the examination of the entire Dominion and provincial systems of public finance and their respective legislative powers, taxation was the key issue of the inquiry. As a commission of enquiry into taxation, it made several notable recommendations that were to be repeated by the Carter Commission a quarter of a century later. Tax policy had traditionally been oriented toward balancing the government's expenditure budget and, since the era of the National Policy, also toward the protection of certain domestic industries. The Rowell-Sirois Commission's Report departed from this pattern in

advocating Keynesian fiscal policy, that is, the deliberate use of budget deficits during slack economic periods, and surpluses during times of high economic activity, to even-out extreme fluctuations of the business cycle. The Commission pointed out that only the Dominion possessed the broad powers over taxation, debt management and the money supply, as well as the diversified economic and population base, to enable it to carry out such a policy effectively, and therefore recommended the transfer to the Dominion of the taxes most suitable for this purpose: the personal income tax and the corporation income tax.[30]

The Commission viewed the personal income tax as the most equitable and the most effective tax, not only for revenue purposes, but for progressive government policies:

> It is the most effective method yet devised, within the framework of the capitalist economy, for achieving the social and humanitarian objectives of our civilization; for applying wealth which is made possible only by organized society for the benefit of society as a whole; for preserving the freedom of individual initiative and at the same time making possible the financing of those services which can be most economically provided by the community as a whole.[31]

However the income tax necessarily fell short of such impressive achievements in Canada due, in the Commission's judgement, to the existing divided jurisdiction. Instead it had produced "the inevitable friction and injustices which have arisen in the competitive scramble for revenues."[32] The regional concentration of wealth and income arising from the workings of the national economy meant comfortable income tax revenues in some provinces and very

little in others, and greatly unequal capacities of provincial governments to provide services for their residents. Provincial and local differences in income tax rates were inequitable, and as barriers to labour and capital, economically inefficient as well. Also, the inability of the Dominion government to guarantee provincial compliance with international taxation treaties might prevent the securing of equitable treatment of Canadians investing abroad and discourage foreign investment in Canada. In order to achieve its full potential as a sensitive fly-wheel for the capitalist economic system, the Commission therefore recommended that the income tax had to be under the control of a single authority, the Dominion government.[33]

With regard to corporation taxes, the Commission agreed with business complaints (including a brief from the Citizens' Research Institute) that business had "been made an object of taxation in itself" rather than "as an agent to collect taxes cheaply and simply from final recipients of wages, interest and dividends."[34] The economic inefficiencies of the existing form and administration of the corporation taxes were compounded by inequities and inefficiencies arising from divided jurisdiction.[35] The Commission recommended continuance of the corporate profits tax, but with the granting of a credit against personal income tax, the recognition of the obsolescence of business assets through capital cost allowances, and the averaging of corporate income over three years.[36]

The Commission also recommended that estate taxes and succession duties be transferred to the Dominion, as their revenue yields were

unpredictable, especially for provinces with small populations. It argued that wealth which was subject to tax in any one province had often been gathered from other provinces, and should rightly be distributed to them. Moreover, provincial administration of these taxes made avoidance possible by judicious selection of one's residence and location of investments, resulting in gross inequities, tax-induced barriers to mobility of capital, and pressures on provincial governments to reduce rates in order to attract wealthy residents and discourage their emigration.[37] The provinces were to be compensated for the loss of direct taxes by receiving undivided jurisdiction over taxes on named commodities, a refund of 10 per cent of the profits from mineral extraction, and annual "National Adjustment Grants" based on a formula to enable them to maintain accepted standards in their areas of spending responsibility without resort to higher provincial taxation.[38]

While the Report itself, submitted on May 3rd, 1940, was put to one side by the more immediate problems of promoting the war effort, the Dominion government, in responding to the challenges of controlling a war-time economy and of financing the war expenditures, found it expedient to use its war-time emergency powers to put into effect some of the Commission's recommendations. Some of the tax recommendations which were not implemented, or implemented only in part, would again surface after the War, first in the negative form of tax problems and controversies, and later as positive recommendations put forward by the Royal Commission on Taxation.

War-time Taxation

The Second World War, like the First, resulted in a discontinuity in the limits of acceptable change in tax policy by forcing a temporary acceptance by business interests of a strong interventionist state supported by a more efficient, and more burdensome, tax system.

The financing of the Second World War differed markedly from that of the First, in that approximately half the expenditures were paid for out of war-time taxation.[39] Although commodity taxes were increased substantially, greater reliance was placed on personal and corporate income taxes than on indirect taxes. The share of indirect taxes in Dominion revenue declined from about two-thirds before the War, to little more than one-third at its conclusion.[40] The Wartime Tax Agreements with the provinces empowered the Dominion government to monopolize the income tax field, and its dominance as an economic regulator was augmented in 1942 by an extensive system of controls on prices, wages and salaries, and the allocation of manpower and some materials.

Taxes on corporate income were increased, with the added imposition of a graduated surtax on business profits which exceeded a definition of pre-War profits by stipulated amounts. Between 1942 and 1945 marginal rates on "excess" profits, when combined with the "normal" tax, was 100 per cent, with 20 per cent refundable after the War.[41] Rates of tax on personal income were also sharply

increased: the marginal rate on taxable income exceeding $500,000 rose from 69.3 per cent to 98 per cent. At the lower end of the income scale, the marginal rate on the first thousand dollars of taxable income of single persons was increased from the pre-War rate of 3 per cent to 37 per cent in 1942-43.[42] One wartime innovation which has survived is the withholding of tax on employment income at source, effectively speeding-up tax payments and increasing revenues.

The Second World War also inaugurated the use of tax incentives. In response to increased concern for the potentially harmful consequences of high tax rates for economic activity and the effectiveness of the war effort, the government began to use selective reduction of direct taxes to encourage capital investment. Capital expenditures had not been deductible under the Income War Tax Act, but accelerated depreciation totaling more than $275 million was granted by the War Contracts Depreciation Board between 1940 and 1944, to encourage investment in plant which would "have no reasonable post-War value" or for "capital expenditures incurred under a war contract."[43] In order to alleviate the shortage of U.S. funds, the War Exchange Conservation Act authorized the Minister of Finance to grant accelerated depreciation on assets that would increase exports to the United States,[44] These incentives were broadened to non-war production industries in 1944.

In 1942, business losses became deductible against income earned in the following year. This was extended in 1944 to allow losses to be carried back one year, and forward three years.[45] With tax rates

going as high as 100 per cent, business expenses tended to become costs to the government rather than to the business, making necessary regulations to prevent abuse of deductions for such items as advertizing and charitable donations, and attempts to circumvent the operation of the tax on excess profits.[46]

Some corporation owners tried various surplus-stripping techniques to avoid the high personal income tax rates. Loop-holes had been plugged by legislative amendments in 1936, 1938 and 1943, but without lasting success.[47] In 1944, the Royal Commission on the Taxation of Annuities and Family Corporations (Ives Commission) was appointed to investigate what had, once again, become the "serious problem" of surplus-stripping.[48] Following presentation of its Report in 1946, the government introduced an amendment permitting distribution of pre-War profits after payment of a special tax ranging from 15 per cent to 33 per cent,[49] apparently in the hope that corporation owners would elect to pay a modest levy rather than try to to avoid tax completely.

One of the legacies of the War was the dominance of the central government in the field of direct taxes, including that of inheritance taxes which it had entered in 1941. For high-income taxpayers, the most keenly felt change was the high rate structure on the income tax, with very high marginal rates at the upper income end. Related to this was a growing acceptance by government officials that high taxes had important implications for economic activity, and that the tax system (as well as expenditures) could be used for economic incentive

and stabilization purposes.

The Post-War Tax Reform

The 1948-1949 reform to the Income War Tax Act, though less comprehensive in scope than that initiated by the Carter Commission nearly a quarter of a century later, was similar in being brought on by the demands of business and tax professionals, and in the dominance of those groups in the reform process. The reform, however failed to cure the structural flaws in the income tax system, flaws which became chronic irritants for business and tax professionals, and a source of significant revenue losses and compliance problems for the administration.

Context of the 1948 Tax Reform:

The salient tax features of the post-War period were high but declining personal income tax rates, more extensive adjustment of personal and corporate income taxes for economic incentives, and a reform of the income tax. These events were taking place within the international context of the "Cold War" dominated by American economic and military power, and in the federal-provincial context of the growth of provincial ambitions and the decline of the unified taxation system engineered by the Dominion government. With the beginning of the Korean War in 1950, a series of post-War declines in tax rates was

effectively halted at much higher levels than had been in effect before 1939. As the Korean War merged into a long Cold War, taxpayers faced the prospect of continuing high income tax rates to finance what appeared to be a permanent war-time establishment.

While the perception of a Communist threat from abroad provided the justification for renewed military spending, the anticipated electoral challenge at home posed by the CCF gave additional impetus to the King government to take some steps in the direction of accepting responsibility for social welfare. Thanks to the greatly strengthened Dominion taxation system built up during the Second World War, the required tax revenues could be mobilized for both military and social welfare expenditures.[50] Unemployment insurance had been introduced in 1941, after an amendment to the BNA Act. This was followed by Family Allowance payments in 1945, and, in 1952, by pensions under the Old Age Security Act. Such measures acted to further offset any decline in revenue needs following 1945.

When, as had been the case following the First World War, it again appeared that high taxes would be among the war survivors, pressures for tax reform were renewed. As Harvey Perry notes:

> One of the marked features of the immediate post-War period was the ground swell of discontent with the income tax. People had accepted a Spartan regime during wartime in fairly good heart; but with peace the income tax seemed to become the popular whipping boy. Everything was wrong with it. The rates were too high; the exemptions were too low; the calculations were too complicated; the law was uncertain; the statute was cumbersome; the administration was arbitrary; appeals were costly; there was "double taxation" of company

> earnings; some forms of income -- life annuities and undistributed profits -- paid too much tax while others -- income of mutuals and co-operatives -- paid too little. And so it went on. The income tax and its alleged deficiencies became front-page copy for newspapers, the Senate had an investigation, and an Income Taxpayers Association was formed, aimed primarily against co-operatives but carrying the crusade as well into other fields. Undoubtedly the formation of the Canadian Tax Foundation was an echo of this general public agitation, although the organization was in fact destined for longer-term purposes. Even the Minister of Finance, with unusual candour, admitted that all was not well. In 1946 he stated that "Our income tax is now unnecessarily cumbersome ...not only is the tax structure itself complex but as the House well knows its drafting leaves much to be desired.[51]

The government responded to some of this agitation by appointing the Royal Commission on the Taxation of Annuities and Family Corporations (Ives Commission) and the Royal Commission on Co-operatives in November, 1944.[52] While a host of revisions to the income tax were made during the years following the War in response to diverse taxpayer demands, the milestone of post-War tax reform was the rewriting of the Income War Tax Act, which was enacted in January 1949 as the Income Tax Act. To a great extent, the Act was a simplification and consolidation of the very complicated income tax structure emerging from the War. Just as the Income Tax Act of 1972 is the product of a decade-long political process, so its predecessor was the codification of a very similar process, with most of the events taking place between 1945 and 1949.

While the post-War tax reform process was not as extensive in scope or duration, or as fundamental in its questioning of the tax system as the reform process of the 1960's, it did have a number of

qualities which invite comparison with the later reform process:

1. It followed and was accompanied by widespread discontent among business and professional groups sensitive to high income tax rates and complexities and anomalies in the tax structure.

2. A Special Committee of the Senate was appointed in October, 1945 to examine the Income War Tax Act and the Excess Profits Tax Act, and to "formulate recommendations for the improvement, clarification and simplification of the methods of assessment and collection of taxes thereunder...".[53] The Committee held public hearings for several months, attended by representatives of the Canadian Manufacturers' Association, the Canadian Bar Association, the Dominion Association of Chartered Accountants, The Canadian Chamber of Commerce, "and about twenty other influential persons and organizations."[54]

   Among the Senate Committee's recommendations were the setting up of machinery, including a Tax Appeal Board, to hear appeals from decisions based on ministerial discretion; amending the drafting of the Act, including the definition of income, to bring it into "conformity with modern business practice" while clarifying certain provisions designed to prevent surplus-stripping; and allowing depreciation as a matter of right rather than of ministerial discretion.[55]

3. An inter-departmental committee, composed of officials from the

departments of Finance, Justice and National Revenue, worked for about two years, producing a bill, presented to Parliament in 1947.[56]

4. Introduced in the 1947 session as Bill 454, the legislation was subjected to public scrutiny. Representations were made by "scores of ...organizations and individuals" including the Canadian Tax Foundation, the Canadian Bar Association, and the Dominion Association of Chartered Accountants. In the 1948 session the government introduced Bill 338, a revised version of the earlier bill, and which was referred to the Commons Standing Committee on Banking and Commerce. After hearing testimony from the Minister of Finance, the Hon. D.C. Abbott and some of the members of the interdepartmental committee which had drafted the bill, it was finally approved by the House and Senate to become effective on January 1st, 1949 as the The Income Tax Act.[57]

This tax reform process differed significantly from the amendments which were a part of the annual budgetary process in the degree to which the government's intentions, in the form of a bill, were revealed to Parliament and the public well in advance of the date of their application. J. Harvey Perry, who was a senior tax official in the Department of Finance at that time, notes that the process of allowing the bill to stand over from one parliamentary session to the next, and the referral of the revised bill to the Commons Committee on Banking and Commerce, were unprecedented measures, taken "to assure

the fullest examination of its provisions by members of Parliament, lawyers, accountants, and the public at large."[58]

The most significant of the reforms involved the removal of discretionary provisions and their replacement by codified rules, such as the introduction of specified capital cost allowance schedules, until then ruled out except by Ministerial permission. What discretionary provisions remained could be appealed to the new Tax Appeal Board, and those decisions, to the Exchequer Court of Canada. While appeals on non-discretionary provisions of the Income War Tax Act had been possible before, the new Act greatly widened the scope and ease of the appeal procedure. Although the Tax Appeal Board was not formally a court of law and the taxpayer was not required to be represented by counsel, most appellants who were not themselves lawyers or accountants were so represented. Hence, among the by-products of the simplified appeal procedure was an increase in tax litigation and in the demand for legal services, as illustrated in Table 2-2, below, which shows the number of cases listed in the indices of Dominion Tax Cases. Rather than reducing the load on the Exchequer Court, the Tax Appeal Board served more as a court of first instance, as many of the cases heard by the Board were eventually heard on appeal in the Exchequer Court or more recently, the Federal Court. The growth in tax litigation can be taken as a rough index of the growth in the numbers of tax professionals.

TABLE 2-2
TAX CASES BEFORE THE COURTS

5-YEAR PERIOD	ALL CASES*	EXCLUDING TAX APPEAL BOARD CASES
1920-24	18	
1925-29	33	
1930-34	32	
1935-39	57	
1940-44	45	
1945-49	135	100
1950-54	1176	214
1955-59	1298	247
1960-64	1578	392
1965-69	1524	501

Source: Dominion Tax Cases.
* Totals in this column include cases heard by the Tax Appeal Board, which did not begin hearing cases until 1949.

The swing toward greater codification of income tax law and administration was destined to continue until the early 1960's, when new discretionary provisions were enacted in a desperate effort to curb tax avoidance schemes. During the interval, the Income Tax Act gradually became longer and more complicated under the weight of accumulated amendments until the complexity of the law itself became an issue.

While the post-War tax reform did clean up the drafting of the statute and paid greater respect to the rule of law by reducing the scope of administrative discretion, it did little to remove one of the more fundamental weakness of the Income War Tax Act and of its enforcement: that of the definition of income subject to tax. The fact that certain receipts could escape income tax, or be subject to a reduced tax if the transactions were properly manipulated, was no less true under the new Act than under the old. Canadian income tax statutes had never defined capital gains, and the statutory provisions

relating to the meaning of "income" did not provide adequate guidance for the courts. The persistence of this situation even after the post-War tax reform suggests that the Liberal government of the time preferred to leave this controversy to be settled by the courts.[59] However, the old politicians' adage that problems, when ignored long enough, often go away, proved not to be the case with the definition of taxable income.

The Canadian Tax Foundation:

One of the products of taxpayer dissatisfaction with high post-War tax rates was the Canadian Tax Foundation. Founded in 1945 as a joint project of the Canadian Bar Association and the Dominion Association of Chartered Accountants,[60] it was among the participants in the 1948 tax reform process. The Foundation was created in anticipation of the continuing importance of tax matters in post-War Canada and was intended to perform a role similar to that the Canadian Tax Conference between the wars, of providing a forum and a platform for the communication and dissemination of research on taxation and the views of tax professionals.[61] The purpose of the Foundation was printed on the back cover of most of its publications:

> ...to provide the tax-paying public and the governments of Canada with the benefit of expert, impartial research into current problems of taxation and government finance. This work is carried on by a well-qualified, permanent staff and by outside experts commissioned for special studies. The Foundation publishes the Canadian Tax Journal and other books and pamphlets, and its activities include holding

> conferences, providing speakers, and making submissions to government.

The Foundation's Board of Governors consisted of 16 lawyers nominated by the Canadian Bar Association and an equal number of chartered accountants, nominated by the Canadian Institute of Chartered Accountants.

The Foundation had both individual members, (usually members of either of the two founding professions, plus some economists) and corporate members, the latter being expected to "make contributions proportionate to the size of the company".[62] From only 98 members in 1947, it grew rapidly, reflecting the increased interest in tax matters as hopes of major tax reductions faded.[63] By 1953, corporate membership had more than doubled over the previous year, individual memberships stood at 1,000 and Foundation publications were being mailed to 2,000 subscribers.[64] The Foundation's report of that year emphasized the importance of building the individual and corporate membership and the organization's reliance on professional contacts to gain corporate support:

> Apart from the financial resources so received, which are needed, this increase is gratifying evidence of favourable recognition of the Foundation's past record and plans for the future. We take this opportunity of repeating that applications for individual membership from members of the professions are always particularly welcome. The Foundation has built up its membership primarily from these quarters and relies on their valued help in securing wider corporate support.[65]

In fact, the Foundation was almost entirely dependent on corporate

support: in 1954, 90 per cent of its revenue of $100,000 came from this source.[66]

The Annual Tax Conference, probably the high point of the year for the Foundation, was devoted to discussion of current developments and problems in Canadian taxation, with panel or workshop sessions with specialist practitioners, administrators and researchers in specified problem areas, and also plenary sessions on topics of general interest to the tax professionals. These annual conferences allowed the tax practitioners to renew their knowledge of tax developments and to meet colleagues in business, private practice and government. Officials from the Departments of Finance and National Revenue served as speakers, panelists and conference participants, and it was not unusual for the keynote speaker at the Conference banquet to be the Minister or a senior official of either Department.

In addition to these network-building roles of the Annual Conference, the Journal editor remarked on the more specific function of the Conference as an annual scrutiny of the budget:

> ...a procedure and device of annual review, eliciting the experience of tax practitioners and businessmen across the country and operating at a sufficient interval after each year's crop of new legislation to allow the difficulties to come to the surface, and long enough ahead of the next year's crop to allow them to be considered and corrected....
>
> The open session on Current Tax Highlights, introduced as a regular feature last year [1952], provides a forum where attention is focussed on troublesome provisions which can be noted in the published proceedings and taken into the agenda of the Joint Taxation Committee

> [of the two parent associations] for consideration in the preparation of their annual tax brief.[67]

While co-operating with the Joint Taxation Committee and providing technical advice to other organizations for pre-budget submissions to the Minister of Finance,[68] the Foundation gradually came to see itself in a more neutral role, distinct from that of lobbyist or pressure group. This position was stated emphatically by J. Harvey Perry on his retirement as Director of the Foundation in 1961:

> 1. That the purpose of the Foundation should be to establish facts and verify theories in every possible aspect of taxation in Canada;
>
> 2. That in carrying out this vital function it must at all times maintain an impartial, unbiased and independent point of view. Impartially [sic] is the difference between research and propaganda.
>
> 3. That the Foundation should neither act as a pressure group nor come under the influence of pressure groups. Such activities have their proper and accepted role in formation of public policy but are inconsistent with the function of research.[69]

As a result of this policy of neutrality, Perry pointed out, the Foundation's publications had gained widespread acceptance as "forums for the free exchange of views on subjects inherently controversial", and even the Government of Canada, like all governments, "inordinately suspicious of taxpayers and their representatives..." had accepted Foundation publications at their face value. Having come to the Foundation from the Taxation Division of the Department of Finance in 1952, Perry undoubtedly had a considerable influence in steering the Foundation away from a lobbying role, and toward a position of unchallenged legitimacy.

However, the Foundation's professed neutrality on controversial issues did not prevent it from expressing opinions to government and to the public on tax questions, especially during the early years. An editorial section in the Canadian Tax Journal, (which, over the years, became less and less editorial in nature) was a common vehicle for influencing opinion and policy. A 1953 editorial, advocated an increase in the exemption level of succession duties to $75,000, thus removing "a large proportion of ...people from this unhappy position (of brooding over succession duties instead of their golf scores) with an inconsiderable loss of revenue." While the consequences of this change for "vertical equity" and for the distribution of wealth were not discussed, the editorial took up a theme which was becoming commonplace among well-to-do taxpayers:

> The existing level of income tax rates has almost snuffed out the opportunity of property accumulation except through capital gains. To remove even this possibility by confiscatory gift and death taxes would be a serious matter at the present stage of our economic development.[70]

As professional dissatisfaction with the reformed Income Tax Act grew, the Foundation helped to focus opinion and to provide a forum and research resources for the discussion of policy alternatives.

The 1949 Act and Corporate Distributions:

The Income Tax reform of 1948 removed most of the ministerial

discretion provisions, as well as other sections dealing with inter-corporate dividends between companies under common control, and inter-corporate transmission of undistributed income on hand on winding-up, discontinuance or reorganization.[71] The provision from the Income War Tax Act giving the Minister discretion to prevent accumulation of undistributed income in excess of reasonable business requirements or for the purpose of avoiding tax was replaced in 1950 with the "designated surplus" legislation.[72] An attempt to curb surplus-stripping by preventing the abuse of tax-free inter-corporate dividends, it provided that, where one Canadian corporation acquired control of a second corporation when the latter had undistributed income on hand, that income would become "designated surplus", and be subject to income tax to the extent that it was paid out of the designated surplus.[73] Payment of a special 15 per cent tax on surplus accumulated by the end of the 1949 taxation year permitted the creation of "tax-paid undistributed income". For subsequent years, tax-paid undistributed income could be created on payment of a 15 per cent tax on an amount equal to dividends paid out in that year, and then distributed tax-free to shareholders by issuing a preferred stock dividend.[74]

These measures imposed a mild tax on surplus-stripping, which, compared with the alternative of high marginal rates of personal tax, should have been relatively attractive. However, tax sophisticates preferred to avoid tax completely by exploiting weaknesses in the statutory definitions of "designated surplus" and "control" through the use of non-voting shares to transfer most of the surplus, or the

sale of the shares of the surplus-bearing corporation to two or more persons who were "at arm's length", with no-one having control, or the use of a holding company to maintain control of the corporation prior to the accumulation of the surplus.[75] Since the designated surplus provisions tried to attack surplus-stripping by taxing otherwise tax-exempt inter-corporate dividends used to transfer retained earnings, they could also be circumvented by selling the shares to an entity that did not pay such a tax. This could be a non-resident corporation (which would pay only a small withholding tax), a tax-exempt entity, or a trader or dealer in securities, who could offset the dividend income with the loss on sale of the securities after stripping the surplus.[76]

An attempt to close these loopholes was made in 1955 when the designated surplus legislation was extended to cover situations where control of the corporation with the surplus was sold to non-resident corporations, tax-exempt entities other than personal corporations, or traders or dealers in securities.[77] In 1959, however, a new loophole was opened with the enactment of provisions which had the effect of removing the "designated surplus" status of retained earnings on statutory amalgamation of one corporation with another.[78]

The 1949 Act and the Definition of Income:

Since the Canadian statute declared that income "from all sources" was subject to tax, the only available legal defence for those seeking

to avoid the tax was to claim that the receipt in question was not "income", or was not actually "received", or at least not by the person claimed to have received it by the taxing authorities. Of all the litigation surrounding the meaning of the term "income", most cases related to the legal distinction between income, as provided for in the Act, and "capital gain", which was not mentioned in the Act, but which the courts had ruled to be the non-taxable return of an investment. This was the basic principle behind most of the "surplus-stripping" schemes and ingenious tax lawyers were able to find many other applications of subtle weaknesses in the statutory references to income.

In a special study for the Carter Commission, Douglas Sherbaniuk[79] summarized the legal history of a large number of problems with the definition of income. The following partial list of tax disputes derived from that study illustrates the many dimensions of the question:

1. Sale of business inventory on winding-up: whether gains arose from the sale of inventory or of capital assets;[80]
2. Gains different from the normal profit of a business, and which might be capital in nature: foreign exchange profits, insurance proceeds, damages and compensation, gifts and windfalls, forgiveness of indebtedness, lump-sum payments for imparting industrial "know-how;[81]
3. "Constructive profits" from non-cash transactions: the use of business inventory for personal enjoyment, gifts out of

inventory, sale of inventory below market value, constructive profits from business services, profits from illegal business, gambling profits;[82]

4. Rental income: whether payments were taxable rental income, or non-taxable capital receipts from sale of property;[83]
5. Royalty payments: whether payments were taxable royalties or non-taxable capital payments;[84]
6. Annuities: what portion, if any, constituted a non-taxable return of capital;[85]
7. Patents and copyrights: whether they produced taxable income or capital receipts;[86]
8. Income from "money": problems arose in separating the taxable interest element from the non-taxable return of capital or discount;[87]
9. Income from offices and employment: gifts and windfalls, not generally subject to tax, were a tempting avenue of tax avoidance for tax planners in the area of executive compensation;[88]
10. Income from "casual services", taxable under the Act, was sometimes confused with capital receipts;[89]
11. Time of "receipt": steep progressive rates on taxable income gave a powerful incentive to high-income taxpayers to minimize the tax by spreading it over a period of years, to reduce the burden by deferring the tax, or to allocate it to a year where it could be offset by business losses;[90]
12. Who received the income? Income could be received by an individual, an individual through a partnership, an estate, a

beneficiary of the estate, by an agent on behalf of the principal, by one taxpayer who directs payment to another, by a taxpayer indirectly by withholding at source, or payment on his behalf to a creditor, or it could be encumbered with further obligations or conditions;[91]

13. Non-cash benefits: taxing benefits was largely an attempt to outflank tax avoidance by eliminating cash or monetary transactions.[92] The 1965 consolidated index of Dominion Tax Cases lists about 159 references to cases since 1920 involving "benefits".[93]

Only four (numbers 3, 11, 12 and 13) of these items of contention are not directly related to the distinction between income and capital gains. All arose out of problems with the existing tax structure, which imposed steep progressive rates on an ill-defined income base.

The Tax Professionals and Agenda Formation

An important element in the exercise of political power is the determination of which problems shall be deemed to be sufficiently important to occupy the limited time of politicians and legislators. The 1948 reform left serious problems which the tax professionals managed to keep out of the political arena for about a decade. As the courts and the interaction between tax practitioners and tax officials failed to solve these problems, many practitioners became convinced that the risks of resorting to a political solution were outweighed by the

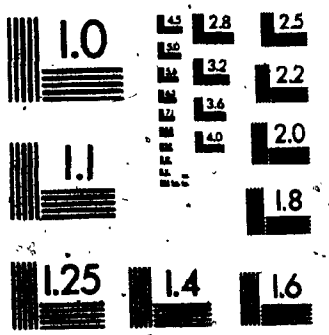
increasingly severe problems of the high progressive rates, the uncertainty in the definition of income, the troublesome area of corporate distributions, and the feeling that the tax system was strangling economic growth. Never far from the world of corporate business, the tax professionals were joined by business leaders in calling for a royal commission as a vehicle for a fundamental reform of the tax system.

Keeping Tax Reform Off the Political Agenda:

Having been born in time to participate in the post-War tax reform, the Canadian Tax Foundation became a forum for expressions of dissatisfaction with the new Act only a few years after it took effect. The failure of the new Act to clarify the boundary between taxable income and non-taxable capital receipts resulted in much lively discussion at the 1951 Tax Conference. Although diverse proposals were put forward, the discussion was inconclusive and the Foundation staff was asked to put the question on the agenda for the following year. A "data paper" prepared by the staff for use by 1953 Conference participants summarized the Conference discussions of the previous year and listed the following "main points" on which "members expressed concern":

> (a) The vagueness of the line between "capital gains" and ordinary income was conceded by all speakers. This of course is the essence of the problem.
>
> (b) The apparently increasing tendency of assessors to bring into tax as income occasional gains on

2



capital transactions was frequently mentioned.

(c) The emphasis on real estate transactions and the relative absence of assessments involving transactions in equities received comment.

(d) The absence of any organized method for the reporting of gains to the taxing authorities so that equitable treatment may be given in all cases was pointed out by some members.

(e) Certain aspects of the new Income Tax Act gave concern. The substitution of the expression "income for the year" in the Income Tax Act for the word "annual" used in the Income War Tax Act was felt to be a change of fundamental importance, implying that the test of the regular and periodic occurrence as a characteristic of income had been abandoned. The broad definition of "business" in the new act, particularly the inclusion of the words "an adventure or concern in the nature of trade" also seemed to many to be a fundamental change which increased the likelihood that gains not previously taxed would henceforth be regarded as income.

(f) Certain aspects of the decisions given by the Tax Appeal Board were commented on. In particular the emphasis on the presence or absence of "intention" disturbed many members.

(g) Some members felt that a fundamental contradiction was involved in applying British jurisprudence to a statute which bore no resemblance to the United Kingdom Act but had many marks of similarity to the American law.

(h) Another view expressed regarding the British jurisprudence was that it should not be applied at all in Canada since it had been developed under quite different circumstances than existed in Canada today. The Tax Appeal Board and the higher courts should develop a distinctive Canadian jurisprudence.

(i) The greatest diversity of views prevailed as to what action should be taken to dispel these problems. Many members favoured a statutory declaration that "capital gains" were not taxable, or else the adoption of a general definition of income that would clearly exclude such gains, failing this, the statutory exclusion of gains from transactions in specified types of capital--e.g,

> houses. Another group on the other hand felt that both clarity and equity would be served by the deliberate adoption of the American system of taxing all forms of gains, including those on property. A large and active minority urged a cautious approach to either of these solutions, arguing that the suggestion that Parliament legislate in this field was inviting trouble, and that the courts were quite competent to work out a satisfactory solution to the problem if given time. The point of law at issue is quite intricate, and such points have traditionally been left to the courts to settle.[94]

While the taxation of capital receipts in the same manner as other income might have suggested itself, as it did to the Royal Commission on Taxation fourteen years later, this option apparently was beyond the imagination of the 1952 Conference participants, who saw only three policy proposals worthy of debate:

> (1) legislate to specifically exclude capital gains;
>
> (2) follow the American system (with preferential rates for capital gains, subject to a specified holding period, and (presumably) without taxation of accrued gains on death;
>
> (3) leave this delicate and complicated question to the courts to straighten out.[95]

One tax professional was sufficiently bold to go beyond these limits to the debate. John G. McDonald, of the Toronto law firm of McDonald, Davies and Ward, writing in the November, 1951 issue of The Canadian Bar Review, recommended the taxation of all capital gains as income. He based his argument on the wide meaning given to "business" in the Act, not limited to "concern in the nature of trade" as interpreted by the courts, and concluded that, by this criterion, virtually all capital receipts were taxable income. He also argued

from the standpoint of equity and "ability to pay":

> In the law of income taxation, of all things, reality should govern. The income tax is designed to take a portion of the individual's economic advancement from year to year, in accordance with his ability to pay. It imposes no penalty upon his estate, but claims a share of his annual economic growth. Capital gains are a part of that growth, and if derived from business activity or from property, it is arguable that such gains are taxable under the present law.
>
> Lastly, if the taxpayer conducts his affairs in the same manner as he would were his "capital" dealings an integral part of his ordinary business, he should not be heard to claim exemption upon the basis of his amateur status. The whole idea is to levy a tax upon income -- equitably among all taxpayers -- and he enjoys no less "income" than the next man who buys and sells professionally.[96]

McDonald's position on capital gains, which was close to that adopted by the Carter Commission in 1967, drew the fire of Stuart Thom, of the Toronto law firm of Osler, Hoskin and Harcourt. In a letter to the editor of the Review printed in the January, 1952 issue, he charged that McDonald had "allowed his social and economic predilections for a tax on capital gains to cloud his legal comment on the new Income Tax Act." He argued that the new Act, like the old one, would be interpreted within the British system of jurisprudence, which considers capital receipts not to be taxable. The question of whether or not a gain is taxable, he said, was a question, not of policy, but of fact, to be decided by the courts, on the merits of each case, and from principles which were not in dispute.[97]

Although McDonald would eventually reverse his opinion on the taxation of capital gains by the time the Carter Report was

released,[98] his position was then at one extreme of the spectrum of debate, and Thom's (probably enjoying much more company than McDonald) near the other. Very few would have gone so far as to suggest that all capital gains be taxed at full rates, although most tax professionals probably would not have shared Thom's optimism regarding the course of judicial interpretation.

At least some were suggesting that the whole tax structure was in need of an overhall. Writing in the February, 1952 issue of the Canadian Chartered Accountant, W. F. Lougheed noted the lack of a definition of income in the new Act, the lack of consistency of administrative and judicial treatment of capital gains, the situation regarding the taxation of undistributed corporate profits, and the constraints imposed on the federal government by "rigidity" in a large portion of its expenditures. Questions of justice and equality aside, he concluded that the income tax system had failed the criterion of "certainty". Piecemeal changes and the addition of new taxes, in spite of growing revenue needs, would not provide the answer: "What is needed far more is a thorough revision of the tax structure...."[99]

Summarizing the situation in 1953, the Foundation staff pointed out that there had been no legislative attempt to extend the definition of income to include capital gains, nor had the Department of National Revenue tried to extend greatly the "scope of the accepted concept of income": the cases appealed by the Department were clearly marginal cases. Where the Department had tried to enforce (or broaden) the concept of income, it was in real estate transactions and

other forms of tangible property, and not "casual transactions in securities by individuals not professionally engaged in the brokerage business."[100]

Having already implied that there was no need for panic, the staff paper asked: "Do we resolve it by some drastic action, or is there reason to believe that it will work out in a satisfactory way if left to the courts?"[101] The paper proceeded to answer this by showing that in the American system, the problems of distinguishing capital gains (which, though subject to tax, were accorded preferential treatment) from ordinary income were very similar to those in the British and Canadian systems. The paper concluded:

> It can safely be said that little comfort can be derived from it that any greater certainty, simplicity or equity would be achieved by deliberately setting out to tax capital gains. Almost all the theoretical issues of distinguishing regular and casual gains are still present, but in addition there emerges a whole and completely unfamiliar range of complex practical problems involved simply in the <u>measurement</u> of capital gain, once identified.[102]

Having found as many complications and uncertainties in an existing system which taxed capital gains not at full rates, but at a preferential rate, the authors of the staff paper drew the conclusion that taxation of capital gains would not lead to greater certainty. However, the actual examples they provided were due to the preference accorded capital gains as defined by the U.S. law. The valid conclusion therefore ought to have been that taxing capital gains at preferential rates does not lead to substantially greater certainty,

While the evidence and the logic of the Foundation staff's argument did not support any conclusions regarding the taxation of capital gains at the same rates as ordinary income, they failed to make explicit this very significant qualification.

Believing that they had disposed of the alternative of taxing capital gains, the Foundation staff proposed five points as being "among the essentials of a Canadian solution:[103]

1. That we stop looking to the U.S. system for a solution, since it is neither better nor very different in its essentials;

2. That any legislative route to a solution be discarded, since that could not remove all uncertainties and "...it is useless to exhort Parliament to action when there is no agreement at all among a group as broad and as well qualified to advise on the matter as the members of the Foundation";

3. Take at face value "the government's official pronouncement that it does not intend to tax capital gains", and concentrate "on the formulation through the Courts of such principles as it is possible to develop for the identification of income as such";

4. Canadian, British and even American experience all lead to the conclusion that gains from "security trading carried on by individuals not professionally engaged in the brokerage business" will be considered as capital gains. Since this accounts for "80 or 90 per cent" of capital gains there is little cause for concern that they will become subject to tax;

5. Since the criterion of "intention" is important in distinguishing between income and capital gains, "we endeavour to define as clearly as possible the conditions upon which its existence is established, and its relative importance at the various stages of a transaction."[104]

These recommendations were followed by a number of generalizations drawn from the jurisprudence very similar to the indications of "the badges of trade" proposed by the United Kingdom Royal Commission on the Income Tax of 1920, and did not establish the distinction with any greater clarity. Essentially, the position taken by the Foundation staff was that the recent court cases should not cause holders of financial securities to panic and demand an overhaul of the tax system, to suggest the taxation of all capital gains on the reasoning that a certain (though presumably reduced) tax was better than the uncertainty, delay and expense of litigation which might ensue. They recommended instead a "stand pat" strategy of relying on the courts to sort the matter out, combined with the existing policy position of the government that "capital gains" were not taxable.

The course recommended in the Foundation staff paper in 52 was essentially what happened for the remainder of the decade. The main events in the history of "capital gains" occurred, not in the political arena, but in the courts, where most politicians were probably happy to leave them. When the courts failed to solve the problem, however, the issue found its way back to the Tax Foundation's annual conferences.

Judicial Decision-Making on Capital Gains:

Although the description of income in the 1949 Act could have been interpreted sufficiently broadly to include capital gains, it was less

detailed than the description of income contained in the Income War Tax Act, and had only limited influence on subsequent judicial interpretation. Lacking what they considered a specific statutory definition of income, the courts felt free to continue to follow United Kingdom precedents until a body of Canadian case law had been established. The central question at issue in most United Kingdom and Canadian litigation came to be whether increments arising from property transactions arose during the course of "an adventure or concern in the nature of trade", following the definition of trade in the United Kingdom statute, in which case the receipts in question were taxable.[105]

The 1955 United Kingdom Royal Commission on the Taxation of Profits and Income was divided on the question of taxing capital gains. A minority report argued strongly in favour, while the majority recommended continuation of the existing treatment, taxing only those gains arising from "an adventure or concern in the nature of trade". The majority, however, did find the jurisprudence to lack the desired uniformity of treatment of similar cases. To avoid the problem of determining directly the motives of the taxpayer, that is, whether he engaged in the transaction in question for the purpose of "an adventure or concern in the nature of trade", the British Commission put forward six "of the major relevant considerations that bear upon the identification of these 'badges of trade'":

(1) The subject matter of the realization;
(2) The length of the period of ownership.
(3) The frequency in number of similar transactions by the same person.

(4) Supplementary work on or in connection with the property realized.
(5) The circumstances that were responsible for the realization.
(6) Motive.

Following these "badges of trade", in order not to attract tax to one's transactions, one should buy and sell objects which were not common objects of trade and from which one might derive personal enjoyment; hold the assets as long as possible; buy and sell infrequently and in small quantities; do not make any systematic effort to make the assets more marketable; make it appear that the property was sold for reasons beyond one's control; and generally give the impression that one's gain was an unexpected windfall rather than a planned attempt to make a profit.

These rules or guides which the Commission majority distilled from United Kingdom jurisprudence since 1920 were, as they stated, simply a list of considerations, and more indicative of the inherent uncertainties in the concepts of income and capital gain than the clarification which the Commissioners intended. However, these same considerations, chiefly in their undistilled form as case law, provided much of the guidance in judicial interpretation of the Canadian income tax statutes.[106]

Canadian courts appeared to have paid little attention to the specific content of the Canadian statute, or to the differences between it and the United Kingdom legislation. In the case of the United Kingdom, the problem of judicial interpretation was essentially

to determine whether, in a specific case, the revenue from a transaction fitted within one of the enumerated categories of income in the schedules of the statute. The (Canadian) Income War Tax Act, however, contained the phrases "and also the annual profit or gain from any other source including...", followed by a list, which included: "undertaking of any kind whatsoever", a phrase repeated in the 1949 Act. This would appear to imply a much broader meaning of income than the oft-quoted words of the United Kingdom statute, "adventure or concern in the nature of trade." However, Canadian courts referred to the latter, more restrictive, phrase even before it appeared in the 1949 Act.[107]

The courts usually approached the problem by trying to distinguish between income, which was taxable, and capital gain, which was not. Neither concept, in the opinion of the courts, was defined in the legislation, and therefore recourse was made to the traditional metaphor of the fruit and the tree. The "fruit" or stock-in-trade was income, and liable to tax. The "tree" or source of income was not itself income but an investment. Disposition of an investment was therefore not income, but an increment in capital. However, the analogy broke down when one encountered dealings in "trees" rather than "fruit": when was the gain from the disposition of an asset simply the realization of an "investment", and when was it more a turn-over of inventory? The solution to this riddle was supposed to lie in the determination of whether or not the person who executed the transaction was engaged in a trade or "an adventure in the nature of trade", or, on the other hand, whether he had initially bought the

asset as an investment for the purposes of either personal enjoyment or receipt of income, and had, in disposing of that asset, simply realized his investment.

Having thereby substituted one riddle for another, the courts applied the "badges of trade" considerations to find a solution. As a result, judicial interpretation of income tax legislation tended to be inconsistent and unpredictable, as a decision in any one case often hung on which of several considerations the judge or majority of judges decided was paramount. A few extreme cases based on the 1949 statute will illustrate how judicial interpretation of the reformed Act failed to solve the problem of distinguishing income from capital gains. Had the courts consistently interpreted the phrase in the 1949 Act, "undertaking of any kind whatsoever"[108] to be more encompassing than the words of the United Kingdom statute, "adventure or concern in the nature of trade", as they had done in the cases of Drumheller v. M.N.R.[109] and Regal Heights v. M.N.R.,[110] then all realized gains would have been subject to tax in Canada.

The latter decision of the Exchequer Court was appealed in 1960 to the Supreme Court of Canada, which dismissed the appeal in a majority decision.[111] The basis of the decision (which came to be known as the "Regal Heights Principle") held that, even though the primary original intention had been one of investment, and therefore, in the absence of further considerations, the disposal of the asset would have been considered a non-taxable capital receipt, the existence of a secondary intention to dispose of the asset at a profit should the

opportunity arise, made the transaction subject to tax. This principle accepted the applicability of United Kingdom case law based on the distinction between capital receipts arising from investment, and income from "an adventure or concern in the nature of trade", and therefore differs from the cases referred to previously. In the Regal Heights case, where land was purchased and a corporation formed for the purpose of developing a shopping center, and the land subsequently sold at a profit when the shopping center plans fell through, the majority decided that the appellants did have a secondary intention of selling the land at a profit.

Had the full implications of this decision been followed in subsequent cases, gains on disposal of assets would have become as fully subject to tax as they might have had the decisions in the Drumheller case and the original Regal Heights case cited above been followed. It would have been rather difficult in most cases to show that, in purchasing an asset that was subsequently sold at a profit, one did not have at least a secondary intention of doing so if the opportunity arose. Canadian courts might then have, by faithful observance of United Kingdom case law, wound up at the same point where they could have started by examining carefully the wording of the Canadian statute.

It appeared that this might indeed happen with the decision in Smith v. M.N.R., where land sold for a profit after having been farmed for a number of years was deemed to have been also an adventure or concern in the nature of trade.[112] When the full implications of

this principle became apparent, however, the learned judges hesitated in its application. It is possible that the judge expressing the minority opinion in the Regal Heights case perceived the potentially far-reaching implications of the principle of secondary intention, and preferred to rely on the characteristics of the assets suggesting either the return of capital or the turn-over of inventory. In his dissenting judgment in that case, Cartwright J., while accepting the "inference" of the trial judge that "reasonable and experienced businessmen, such as the promoters were, must have envisaged the possibility of being unable to carry out the scheme of developing the shopping centre and have hoped in that event to dispose of the lands at a profit", refused to draw the conclusion of the majority, that the appellant was engaged in speculation in vacant land:

> ...it appears to me that the sales of the lands made by the appellant were a realization of its capital assets when the purpose for which they had been acquired was defeated by the decision of the department store mentioned in the evidence to build on a nearby site. To put the matter colloquially, the lands were acquired and disposed of not as the stock-in-trade or inventory of a dealer in land but as capital assets of a developer of a shopping centre which, owing to circumstances beyond the control of the appellant, it became impossible to develop...[113]

The fact that the Supreme Court judges could agree on the facts of the case but not on the test that should be applied was symptomatic of the entire history of the capital gains jurisprudence. The minority judgement in Regal Heights at least had the merit of avoiding the implication of potentially taxing all property gains, and the apparent absurdities implied in the test of secondary intention.

In the well-publicized 1962 Supreme Court case, Irrigation Industries v. M.N.R., Martland, J., writing the decision for the majority (with two dissenting), specifically rejected the secondary intention test after considering its implications. In the Exchequer Court,[114] Cameron J. had ruled the gains from disposal of mining company treasury shares by Irrigation Industries to be the result of an adventure or concern in the nature of trade on the grounds that the shares had been purchased with borrowed funds and, being the shares of a new mining company, presumably could not be expected to produce dividends for a number of years. Also, the appellant had disposed of the shares after only a short period of time. Martland J. however, rejected the factors of borrowed funds and the likelihood of no early dividends as being of any significance, then went on:

> However, assuming that the conclusion was correct that this purchase was speculative in that it was made with the intention of disposing of the shares at a profit as soon as reasonably possible, does this, in itself, lead to the conclusion that it was an adventure in the nature of trade?
>
> It is difficult to conceive of any case, in which securities are purchased, in which the purchaser does not have at least some intention of disposing of them if their value appreciates to the point where their sale appears to be financially desirable. If this is so, then any purchase and sale of securities must constitute an adventure in the nature of trade, unless it is attempted to ascertain whether the primary intention at the time of purchase is to retain the security or to sell it. This, however, leads to the difficulty mentioned by my brother Cartwright that the question of taxability is to be determined by seeking to ascertain the primary subjective intention of the purchaser at the time of purchase.
>
> I cannot agree that the question as to whether or not an

> isolated transaction in securities is to constitute an adventure in the nature of trade can be determined solely upon that basis. In my opinion, a person who puts money into a business enterprise by the purchase of the shares of a company on an isolated occasion, and not as a part of his regular business, cannot be said to have engaged in an adventure in the nature of trade merely because the purchase was speculative in that, at that time, he did not intend to hold the shares indefinitely, but intended, if possible, to sell them at a profit as soon as he reasonably could. I think that there must be clearer indications of "trade" than this before it can be said that there has been an adventure in the nature of trade....[115]

It is interesting to note that Cartwright, J., the writer of the dissenting opinion in this case (with Judson J., who had written the majority judgment in the Regal Heights case, concurring) had also expressed a dissenting opinion in the Regal Heights case. On the case of Regal Heights he had dissented from a judgment based on the test of secondary intention in favour of distinguishing between inventory and a capital asset. Yet in Irrigation Industries, where the majority had in fact made such a distinction, he dissented on the grounds that the precedent set in Regal Heights should be respected. This minority opinion, that the precedent set in the Regal Heights was relevant, served to underline the discrepancy between the results of the two decisions: isolated speculation in land produced taxable income, but similar speculation in shares of an unproven mine resulted in non-taxable capital gains.

Consternation among tax professionals had been growing for some time on the whole question of capital gains versus taxable income. Even before the Supreme Court decision in the Irrigation

Industries case, it was becoming increasingly difficult to give clients reliable advice. At the the 1961 Tax Conference of the Canadian Tax Foundation, O.J. Hall, of Sutton, Braidwood & Co. of Vancouver, while reviewing a number of recent capital gains cases, pointed to the lack of certainty arising from apparently inconsistent judgments and likened the process to a game of chance, with the odds currently in favour of the Minister.[116]

The judgment of the Supreme Court on the Irrigation Industries appeal was handed down on March 26, 1962, hitting the Canadian tax community like a bombshell. In the May-June issue of the Canadian Tax Journal, Gwenneth McGregor, editor of the regular feature, "Around the Courts", opened her discussion with the following comment:

> The effect of this Supreme Court decision on the tax world has been in the nature of a hundred-megaton bomb, since it appears to widen the capital gains area beyond anything previously done by the courts, and moreover to call in question many of the basic principles that have been established by jurisprudence over many years. If applied indiscriminately as a precedent, this judgment could well render valueless most of this jurisprudence and also lead to the result that profits arising from speculative transactions would not be considered taxable income.[117]

Speculating on the likely "fallout" from this judicial blast, McGregor thought that the effect of the decision could possibly be contained by future court decisions giving it a vary restricted interpretation, rather than establishing a general principle applicable to future cases, or that it could lead the taxing authorities to seek a legislative solution in the form of a tax of

some sort on capital gains.[118]

As the Tax Foundation staff paper of 1952 had recommended, policy on taxation of capital gains was being made, not in the political and legislative arenas, but in the courts, and (to the increasing chagrin of the tax professionals) in the offices of National Revenue. When the courts conspicuously failed to solve the problem, the issue found its way back to the Tax Foundation's annual conferences. This happened first with respect to the question of surplus-stripping which was beginning to take on scandalous proportions.

Surplus-stripping Enters the Political Agenda:

The surplus-stripping issue was of sufficiently widespread interest in 1960 for a general session to be devoted to it at the annual tax conference. The Minister of Finance, Donald Fleming, had just appointed a "Committee of Four" tax professionals: Emile Beauvais, George Tamaki, Lancelot J. Smith and R. Bredin Stappells to study the problem of corporate distributions and to make recommendations for a solution.

All three speakers assigned to the topic placed the problem within the context of "double taxation" of corporate income: that is, the fact that, after the payment of approximately 50 per cent tax on corporate profits, the shareholders still had to pay personal income tax on the portion distributed. The rate of personal tax was in

excess of 80 per cent in some cases, amounting to virtual "confiscation" of the corporate income, especially when the distribution was a forced one in order to pay death duties. Hence, the on-going "chess game" of surplus-stripping between tax advisers and the Minister, as one conference participant described it.[119] Although the non-taxability of capital gains was also central to the surplus-stripping issue -- since it usually provided both the incentive and the means for surplus-stripping, and also allowed the distribution of profits from widely-held corporations tax free -- this did not figure in the discussions of either the "problem" or the possible "solutions".

One of the speakers, W.R. Jacket, General Counsel for Canadian Pacific Railway, who, as a civil servant, had worked on the provisions of the Act dealing with corporate distributions, put the issue into the following perspective:

> 1. Since 1917, our income tax acts have taxed corporations on their corporate profits and individual shareholders on their dividends -- this is what has been known as "double taxation".
>
> 2. Any device or hole in the tax law whereby some individual shareholders would be permitted to obtain corporate earnings without paying the equivalent of a tax on dividends would involve a grave inequity as among different classes of shareholders -- and, unless skilfully concealed, it might also arouse strong political disfavour as constituting an exemption of dividends (the income of the well-to-do) as Prime Minister Bennett apparently found out to his surprise.)
>
> 3. Any suggested solution to the grave problems arising under the present law -- to which my friends will refer -- should be tested by asking: (a) Is it being proposed, in effect, to abolish the

> tax on corporation profits in whole or in part and, if so, is it practical politics to suggest that?
>
> (b) Is it being proposed, in effect, to abolish the tax payable by individuals on dividends, in whole or in part, and if so, is it practical politics to suggest that?[120]

The following speaker, D.J. Kelsey, after a review of the problem in the context of the tension between the principle of progressive taxation, and the political attractiveness of taxing corporations, rejected any piece-meal amendments to the existing law, and proposed a variant of Jackett's second "solution":

> I find myself being drawn more and more, granted against the current of belief of many that it would not be politically acceptable, to this simplest solution of all -- tax corporation income heavily as it flows into the corporation; thereafter let the residue of earnings pass freely among residents with neither tax nor hindrance from tax law.[121]

The final speaker of the session, Stanley E. Edwards, of the Toronto law firm Fraser, Beatty and Co., spoke favourably of Kelsey's suggestion, but doubted whether the government would have the "considerable political courage" necessary to limit tax on corporate income to 50 per cent and logically extend this upper limit to all individual incomes. This transparent exemption of dividends would be too "easily understood", whereas the existing system, which produced very little revenue from corporate distributions, was too complicated to be understood by "the general public". As a more politically acceptable alternative, he proposed scrapping the existing anti-surplus-stripping provisions and substituting a rather elaborate method of imposing a maximum 15 per cent tax on the sale of shares by

those with controlling or substantial interest to an entity which was eligible to receive dividends tax free or at a low rate. To the extent that complete avoidance could be prevented -- and he acknowledged that difficult problems of draftsmanship were involved -- the alternative meant that a tax of 15 per cent or less would be imposed on corporate distributions, at least for those astute enough to take advantage of the provisions.[122]

All solutions discussed at the 1960 Conference were meant to eliminate, or alleviate the "double taxation" of corporate-source income, and in some cases, to disguise the fact that dividends were no longer subject to progressive rates of income tax. While the individual progressive income tax rates were seen as part of the problem, (and their elimination or circumvention, part of the solution) the tax-free status of capital gains was not.

These avoidance techniques were available only to controlling shareholders in closely-held corporations, and were therefore viewed by some as a blatant violation of the principle of "horizontal equity", that is, treating those in similar circumstances in a similar manner. The pressure on tax advisers from clients anxious to reduce their tax burden to the same extent as their competitors, the resentment among tax professionals at what many regarded as only marginally ethical practices by their professional colleagues and competitors, and the resentment among investors in widely-held corporate shares who could not (but also need not) make use of surplus-stripping devices themselves, began to demand, in the name of

"equity" an investigation into the practice, or into the entire tax system.[123]

Tax Reform Enters the Political Agenda:

Tax reform was in the air at the 1961 Tax Conference, held at the Queen Elizabeth Hotel in Montreal. Most of the sessions highlighted serious shortcomings in the existing tax system and pointed toward the need for a thorough re-structuring of at least the Income Tax. In addition to the discussion of the capital gains problem, there was a panel on "Surplus Computations Under the Income Tax", and a general session devoted to personal corporations, which had become one of the devices for surplus stripping and other methods of tax avoidance. A renewed attack on progressive taxation was the feature of the opening General Session. Another issue which was warming up, the taxation of co-operatives in comparison to their private enterprise competitors, was the topic of another panel session. Perhaps it was the effect of the recent downturn in the economy, combined with the growing severity of problems arising with the tax structure, that made the 1961 Conference much less complacent than its immediate predecessors.

There was also the nearby example of President Kennedy's tax reform project, explained by the guest of honour at the Conference Banquet, Assistant Secretary of the Treasury Department, Stanley S. Surrey.[124] Surrey outlined the rationale behind President Kennedy's new tax program which the latter had introduced in his Message to

Congress soon after taking office. The central theme was equity, that equal incomes should bear an equal tax burden.[125] The tax loophole singled out by Surrey (and Kennedy, whom he quoted) was the abuse of business expenses by "expense account living". Other priority areas for reform would be simplifying the system, preventing the substantial amount of non-compliance, and using the income tax system to encourage economic growth. This last objective would be approached through the widening of the tax base, and using the revenue thus gained to lower the rates, thus reducing the adverse effects on economic growth. He pointed out that the removal of "special provisions" would contribute toward economic growth directly by reducing economic distortions and improving the efficiency of the allocation of resources, as well as allowing for a general reduction of the rates of tax. In addition, he argued, it would contribute toward the goal of equity, by removing special advantages for certain classes of taxpayers, and of simplicity, by removing complicated language in the statute defining the special provisions.[126]

At this point in his address, Surrey might perhaps have noticed his listeners shifting uneasily in their chairs. Which "special preferences", besides "expense account living" (and most of the tickets to the Foundation banquet were likely purchased with before-tax income) did Surrey think were incompatible with an "equitable" tax system? Surrey's concluding remarks quickly put their digestion at ease: a reformed tax system, besides removing the "obstacles" to economic growth, should also "contribute in an affirmative way ...through promoting increased investment by business

in machinery and equipment."[127] The President's program included more generous capital cost allowances and an 8 per cent investment tax credit.

Surrey did not discuss the possibility of conflicts among the various goals. His listeners were left with the impression that the goals of the U.S. tax reform programme, "fairness, simplicity, and contribution to economic growth", would be mutually reinforcing and emerge from a moderate reform of a tax system which was already "fundamentally sound".[128] Probably the emphasis on broadening the tax base in the U.S. reform plans did not appeal to his Canadian listeners: no one at that Conference was calling for a broadening of the Canadian tax base. Capital gains were already a part of the American tax base (though accorded reduced rates) and Canadian tax professionals could imagine what might be added to the Canadian tax base. The lesson they took from Surrey was probably the one they could best use: Kennedy had begun the reform of the American system to encourage economic growth, and it was time to think of tax reform in Canada.[129]

The record of the opening general session of the 1961 Tax Conference provides the best distillation of the growing uneasiness of the tax professionals with the income tax. A.J. Little, Chairman of the Foundation, referred to the withdrawal by the Government the previous June, of its proposed amendments to Income Tax Act regarding personal corporations. After suggesting some of the perverse effects the proposed amendments would have on Canadian-owned family

businesses, he commented on what he regarded as the inadequate capacity and resources of the tax policy apparatus of the Government and legislative system:

> Therefore it seems to me that the ranks of our legislative tax planners should be strengthened to permit more time for thoughtful consideration and forward planning when legislation such as this is in contemplation. In addition to this I think such a tax planning group should seriously consider devising ways and means of permitting major changes to be examined by taxpayers and their advisers who are apt to be most knowledgeable in respect of the practical problems which may be created, before such changes are adopted. I think the nature of the proposed personal corporation amendments and the undoubtedly unexpected effect which could have resulted, point up the need for forward thinking of this type.[130]

There followed a general session devoted to the "ability to pay" doctrine, a principle which was usually used to defend the progressive rates of personal income tax. None of the three speakers had anything favourable to say about the idea that taxes should be levied in accordance with ability to pay, or about its corollary, that rates of tax should increase at something more than in direct proportion to income.

Dr. A.K. Eaton, recently retired as Director of the Taxation Division of the Department of Finance, started his attack on progressive taxation by quoting from Karl Marx to imply an ideological kinship of the ability-to-pay principle. He claimed that it was only under the duress of his government employment that he had not spoken out earlier against progressive taxation. Taxes levied according to ability to pay should be, not progressive, but proportional, he said,

and a flat-rate income tax of 16 per cent would raise the same revenue as the existing progressive income tax. The reasons for progressive income tax, and increasing welfare programmes, he concluded, were political: there were more low-income voters than high-income voters, and political parties could not resist out-bidding each other.[131]

The second speaker, Trevor F. Moore, Vice-President of Imperial Oil Limited, was equally unsympathetic to progressive taxation.[132] He pointed to economic reasons why tax reform was needed: the current slow growth in the economy, which, in spite of a recent up-swing, would still leave about 5 per cent of the labour force unemployed in the coming winter; the increasing trade competition from the European Common Market, which Great Britain was expected to join; and the large proportion of the national income paid in taxes, which made the economic effects of taxation as important as the revenue effects. From this he concluded that tax policies should be integrated with government economic planning, including greater inter-governmental co-ordination to end the "tax jungle". Central to his idea of economic planning were tax incentives to encourage investment. He complained, however, that political parties running for election preferred to offer "expensive handouts to the electorate".[133]

The final speaker of the general session was H. Hewert Stikeman, senior partner in Stikeman and Elliott of Montreal, a former Deputy Minister of National Revenue, Taxation during the War, former Counsel to the Special Senate Committee examining the Income War Tax Act, and one of the most successful tax lawyers in Canada.[134] Stikeman

explained how the high rates of progressive income tax, when combined with the tax on corporate profits and, eventually, the estate tax and succession duties, forced entrepreneurs who had rescued or built up substantial businesses to choose between leaving the country, selling out (frequently to foreign interests) or, increasingly, to adopting sophisticated methods of tax avoidance. Like the previous speakers, he believed that the economic effects of the tax system were serious impediments to economic growth:

> In my opinion the tax structure and the progressive rate of Canadian taxation today are perhaps the two largest factors militating against capital formation in Canada.[135]

It was possible, however, to avoid the effects of high tax rates. Stikeman cited judicial opinions to show that the courts did not frown upon the activity, so long as it was squarely within the letter of the law,[136] then discussed the following general types of avoidance:

1. distribution of surpluses at less than the normal rates of personal or corporate taxation (including "surplus-stripping");

2. disassociating associated companies (in order to achieve maximum advantage from the low rate of tax on the first $35,000 of corporate profits);

3. estate planning (usually to minimize estate tax and succession duty liabilities, but sometimes to minimize income tax through a surplus-stripping device);

4. depersonalizing personal corporations: some tax avoidance devices made use of the personal corporation, some, of the process of disqualification of that status;

5. inter-corporate avoidance (frequently a part of surplus-stripping schemes, or to prevent surplus earnings from building up in a corporation).[137]

Stikeman said that the Government was faced with two alternatives: either to include provisions in the Act specifically forbidding the avoidance activities, or, preferably, to rearrange the tax burden in such a way that avoidance would not be necessary, so that even the uninitiated would know how to arrange their affairs to minimize their tax burden. Stikeman credited the Tax Foundation with publishing a number of studies which would contribute toward the latter objective, which could be achieved, not by redrafting sections of the Act, but by changing "the tax structure itself as a concept. A revolutionary approach is what Canada needs in the fiscal scene today."[138]

Stikeman had a strategy for accomplishing this revolution:

> We have learned that governments cannot be counted upon to take the sole initiative in these matters. The government's interest in the fiscal system is primarily one of raising revenue without stultifying the economy too much in the process. However, taxpayers as a group are a headless body. Business men are organized into segments, Boards of Trade, Chambers of Commerce and various other groupings. They all see their own problems, but few of them see the whole problem or their own problem in relation to the whole. This Foundation, however, does. It is equipped and experienced enough to undertake the necessary surveys and to make the necessary recommendations. Perhaps this is the real reason for which we were created. When I look back on the day in 1948 when Molyneaux Gordon, Grant Glassco and John Forsyth and I had lunch in the Chateau Laurier and heard Molyneaux Gordon expound the possibilities of a Tax Foundation for Canada he had exactly this in mind. "Some day," he said "this country is going to get itself so hopelessly enmeshed in its own fiscal system that somebody is going to have to cut a few ropes." ... He went on to say the person who is going to be listened to when the rope-cutting time comes could be the Tax Foundation.

> I therefore commend it to all of you, which means all of us, that we should now creatively attempt with the intellectual resources at our disposal and the mechanical means at our command within this Foundation to embark upon a constructive study with a view to making concrete constructive suggestions to the government of the day as to how to deal with avoidance, not by trying to drive it underground, but by removing the causes and introducing a tax system which does not unduly stultify initiative.[139]

Stikeman expressed his enthusiasm for the Foundation's plans (announced at that Conference) to sponsor a comprehensive study of the economic effects of taxation, to be undertaken by economists at Queen's University, and urged his audience to inform the Government of the various methods of tax avoidance and of the serious implications the existing tax structure had for the economy: ".. the fact that avoidance ... exists and must exist if the economy is to go forward under the present system is an indictment of the system."[140] It was also, he said, a serious challenge to the Government itself, one which placed the Foundation in a unique and strategic position:

> The government is largely in the position it is today because it is faced not only with this problem, but has far more serious things to think about and it is not composed of many persons who can readily grasp the problems in this complicated and narrow area without a great deal of study which they have not time to give. It is therefore up to us -- to this Foundation -- to those of us here today, to all of us to work together with all the experience and means at our disposal -- to bring to the government a plan. This plan could be accepted by any government without danger because it would be sponsored by this Foundation in keeping with its great tradition of objectivity which has kept it free from special pleading or the importuning of pressure groups. At the same time the government would also know that any such plan had been produced by persons skilled in this sphere with actual experience to draw upon who are doing it for one reason only -- that they wish to see Canada go forward.

Three things must be our goal--

(1) That no tax structure should be erected which will prevent business incentive from fulfilling its proper role in the economy: to develop it, to build capital and to remain Canadian.

(2) That every taxpayer shall know with certainty the measure of his burden and the consequences of his actions before hand.

(3) That consistency be adhered to and that the rules be not changed without adequate warning and regard for the psychological effect of such change upon Canadian and non-Canadian investors.[141]

While tax reform was not specifically on the agenda of the 1961 Tax Conference, the need for a thorough reform of at least the income tax was on the minds of several speakers, and of many of those attending as well, at least after the conference had got underway. It was probably no coincidence, that, shortly after the November conference, business interests began to demand a reform of the tax system.

Meanwhile, the courts had been busy applying the "badges of trade" to disputed instances under the Income Tax Act. With the Supreme Court judgement in the Irrigation Industries case, pressures were building for some sort of definitive solution. Many businessmen and tax professionals urged the Government to completely overhaul the Income Tax Act, a few going so far as to suggest following the recent British lead by taxing capital gains.

The 1962 Conference of the Canadian Tax Foundation devoted a special panel discussion to "Capital Gains - U.K. and the Irrigation

Industries Case". The chairman of the panel, Stuart D. Thom, following a subtle analysis of the implications of the Supreme Court decision, concluded by referring to remarks by the Foundation's former Chairman, A.J. Little, before the Canadian Club on October 26th of that year. Little had called for courageous and imaginative changes in tax laws, but, while emphasizing the importance of equitable taxation, spoke in opposition to any tax on capital gains. Said Thom:

> It occurs to me that a system of taxation that does not attempt to tax gains or profits of every kind is inequitable to start with. Moreover, not only is the tax inequitable in its hit-and-miss application, but it introduces a degree of uncertainty which, as today's discussions I think will show, had become almost intolerable. The uncertainty that characterizes the Canadian tax is being compounded by the defensive type of legislation which the Department favours, but does not use in open combat but rather in the course of negotiations. I refer to such sections as 8, 16, and 137, among others. These statements of taxing policy are in a sense simple to read, but they are capable of unlimited extension and many people feel that, if the Department sought to exercise the power which it has given to itself, the capital gain would be as dead as a dodo in no time and its death would be brought about in a manner which would be highly undesirable. It may be it is merely our good fortune that the administration to date has not tested its strength. The equitable and certain taxation which all of us agree is such a desirable goal might better be achieved by grappling with the undoubted difficulties of capital gains tax rather than by leaving the matter to the long drawn out and frequently puzzling processes of judicial legislation or to the threat of action under the club and pistol sections of the Act.[142]

This was a sharp reversal of his views on the taxation of capital gains from 1952, when he had taken John G. McDonald to task in the Canadian Bar Review for taking a similar stand.[143]

In the January-February, 1962, issue of the Canadian Tax Journal,

the editor noted that "...several leaders of Canada's financial and business communities... [had] recommended that a Royal Commission enquiry be conducted into the ramifications of Canada's tax structure.[144] While the editor reacted somewhat cautiously to the proposal, he did support the idea:

> If a Royal Commission of men learned in the ways of finance and various phases of business, economics, law and accounting would undertake to design a practical measure for ranking desireable objectives of tax policy, the value to Canada would be inestimable....[145]

When the Diefenbaker Government announced in August, 1962, the appointment of the Royal Commission on Taxation, the Foundation offered its full co-operation to the Commission and suggested the provinces follow the lead of Ontario and appoint similar provincial commissions to work with the federal Commission, perhaps even appointing individuals from the Carter Commission to the provincial commissions.[146] The editor of the Canadian Tax Journal reminded the business community of the special role that it could play, by demonstrating the effect of taxation on business and financial decision-making. Business alone was "in a position to give expert testimony ...in connection with tax incentives."[147]

Conclusion

From its origin in the fiscal systems of the British North American colonies, the Canadian tax system had complemented state expenditures on transportation infrastructure in encouraging the accumulation and concentration of private capital. Regressive indirect taxes and state subsidies for canals and railways funnelled wealth from small agricultural producers into private investments in transportation, trade, finance, and the processing of natural resources and agricultural products.

The first step toward direct, progressive taxation, The Income War Tax Act, was the last resort of a reluctant government to wartime emergency, and was never accepted as a permanent and legitimate institution by wealthy Canadians who were expected to bear the greatest burden. Like air under pressure, private wealth sought out escape routes through the clauses of the Act, building up in the process an industry of professionals dedicated to the minimization of tax and the lobbying for tax concessions. Reflecting the activities of this growing tax avoidance industry, the legislation became longer and more complex as it incorporated both concessions extracted from successive governments and attempts by tax officials to plug loopholes drilled by enterprising tax practitioners.

The tension between urgent spending needs and inadequate revenues forced governments to limit concessions to business and professional pressures for tax relief. This contradiction became acute during

periods of war and economic depression, provoking major shifts in tax policy in attempts to bolster revenues. The post-World War II period saw the emergence of a chronic fiscal squeeze resulting from growing government expenditures at all levels, sharpened inter-governmental competition for tax revenues, increasingly sophisticated and widespread tax avoidance, and mounting pressure from business and the tax professions against the income tax and government spending. The 1948 tax reform had been placed on the political agenda by the same groups who then played a leading role in re-shaping the statute.

Serious structural problems remained in the 1949 Act, chiefly the failure to distinguish between taxable income and tax-free capital gain. Tax professionals, through the vehicle of the Canadian Tax Foundation, successfully withheld the problem of capital gains from the political agenda throughout the 1950's, despite the apparent inability of the courts to deal with it. By the beginning of the 1960's, however, the increasingly obvious structural flaws in the income tax system combined with high personal tax rates and a sluggish economy persuaded tax professionals and influential businessmen that a political solution was unavoidable. Although the economy was recovering from recession, many businessmen and tax practitioners believed that only lower taxes could assure prosperity. While these voices were being heard in most business fora and in the mass media, the Canadian Tax Foundation gave them a legitimate platform. Rather than the self-pleading of privileged minorities, they spoke in the name of national economic progress, if not of national salvation.

No one among the tax professionals spoke about the lack of adequate progressivity in the existing Canadian tax system, or the greatly unequal distribution of income and wealth. On the contrary, they complained of too much progressivity and too much re-distribution of income. Taxes were too high for those whose talent and efforts, they said, provided economic well-being for the others. With the tax practitioners and businessmen taking the initiative, the issue of tax reform was placed on the political agenda and formulated in the language and image of business.

Notes to Chapter II

1. Perry, J. Harvey. Taxes, Tariffs and Subsidies, Vol. I (Toronto: University of Toronto Press, 1955), pp. 37-39; A. Milton Moore, J. Harvey Perry, and Donald I. Beach, The Financing of Canadian Federation: the First Hundred Years, Canadian Tax Paper, No. 43, (Toronto: Canadian Tax Foundation, 1966), pp. 1-2; Donald G. Creighton, British North America at Confederation: a study prepared for the Royal Commission on Dominion-Provincial Relations, (Ottawa: Queen's Printer, c. 1940), pp. 10-60; Report of the Royal Commission on Dominion-Provincial Relations Vol. I (Ottawa: King's Printer, 1940); H.A. Innis, "Factors in Canadian Economic Development", in Mary Q. Innis, ed., Essays in Canadian Economic History (Toronto: University of Toronto Press, 1956), pp. 206-207; W.A. MacKintosh, The Economic Background of Dominion-Provincial Relations (Toronto: McClelland and Stewart Carleton Library, No. 5, 1963), pp. 13-26. I have used Perry's work as the chief source for most of this chapter because of its concentration on taxation, and because Perry's knowledge of the historical background to Canada's taxation problems were, as a result of his appointment to the Royal Commission, effectively at the Commission's disposal.
2. As the Minister of Finance of the Province of Canada, the Hon. Alexander Tilloch Galt, put it in the Legislative Assembly on February 7, 1865: "If the men in power [in the provinces] find that they are required, by means of direct taxation, to procure the funds necessary to administer the local affairs, for which abundant provision is made in the scheme, they will pause before they enter upon any career of extravagance." The Confederation Debates in the Province of Canada, 1865, ed. P.B. Waite (Toronto: McClellnd an Stewart, Carleton Library, 1963), p. 54.
3. Perry (Vol. 1, p. 38) cites the situation preceding Confederation, of loans advanced to railways, including the Grand Trunk by the Province of Canada, on which little or no interest was being paid. For a detailed account of the avenues through which public funds were channeled into railroad construction and into the pockets of railroad promoters, see Gustavus Myers, A History of Canadian Wealth, 2nd edition, (Toronto: James Lewis & Samuel, 1972), pp. 168-340.
4. Perry, pp. 72, 106.
5. Ibid., pp. 78-88, 121-122.
6. Ibid., p. 144.
7. Ibid., pp. 145-146.
8. Ibid., pp. 152-154.
9. Ibid., pp. 154-155.
10. Ibid., pp. 156-157.
11. For residents of British Columbia, the total Dominion and provincial marginal rates would have ranged from 5 per cent, to 39 per cent over the same income range. The Act also imposed a 4 per cent tax on corporate profits, but only to the extent that it exceeded that imposed under the Business Profits War Tax. Perry, p. 158.

12. Perry, p. 159.
13. Ibid., pp. 196, 211.
14. Ibid., p. 211.
15. S.C. 1917, ch. 28, later R.S.C. 1927, Ch. 97 and amendments thereto. Quoted by Geoffrey R. Conway and John G. Smith, The Law Concerning Capital Gains, p. 88, and by Douglas J. Sherbaniuk, The Concept of Income: The Receipts Side, Royal Commission on Taxation, Study No. 20, (Ottawa: Queen's Printer, 1968), p. 2.
16. A number of sources deal with the different concepts of income in the U.S. and the U.K., including J. Harvey Perry, Taxation In Canada, 3rd edition, (Toronto: University of Toronto Press, 1961), pp. 40-46; Perry, "Capital Gains: The British Point of View", Canadian Tax Journal, Vol. 1, No. 4, (Nov.-Dec., 1953), pp. 548-561; Douglas G. Sherbaniuk, The Concept of Income: The Receipts Side, Royal Commission on Taxation, Study No. 20, (Ottawa: The Queen's Printer, 1968), pp. 1-3, 30-40; and Geoffrey R. Conway and John G. Smith, The Law Concerning Capital Gains, Royal Commission on Taxation, Study No. 19B, (Ottawa: The Queen's Printer, 1967) pp. 1-67. Further references to judicial interpretation of income tax law concerning capital gains will be to Conway and Smith, which summarizes some of the earlier writings.
17. Conway and Smith, pp. 2-5; 91-92.
18. Ibid., p. 3.
19. Ibid., pp. 6-10, 95.
20. Ibid., pp. 95-96.
21. Ibid., p. 91.
22. Stripping of Corporate Surplus, Royal Commission on Taxation, Study No. 15. (Ottawa: Queen's Printer, 1967), p. 14. This discussion of surplus-stripping is based largely on the Royal Commission study, as it summarizes the relevant literature published to that date.
23. Ibid., p. 14. The Royal Commission study cites J. Richards Petrie, The Taxation of Corporate Income in Canada, (Toronto: University of Toronto Press, 1952), p. 54.
24. Perry, pp. 256-264. The tax increases were perverse from a Keynesian standpoint, though the provinces at least had little choice but to attempt to increase revenues to balance expenditures.
25. Ibid. Actual tax liabilities depended upon a large number of factors, including whether one lived in a city which imposed an income tax, and the rate of provincial income tax, if any.
26. This is the conclusion, based on U.S. data, of the study published by the Royal Commission on Taxation, Geoffrey R. Conway, The Taxation of Capital Gains, (Ottawa: 1968), pp. 96, 115).
27. Report of the Director (Toronto: Citizens' Research Institute of Canada, 1932), pp. 3-4.
28. Perry notes the suggestions made at Dominion-provincial conferences, especially that of 1935, the Nova Scotia Royal Commission of Economic Enquiry, in its 1934 publication, A Submission on Dominion-Provincial Relations and the Fiscal Disabilities of Nova Scotia within the Canadian Federation, the

1935 Report of the Alberta Taxation Inquiry Board on Provincial and Municipal Taxation, and the 1936 Report of the Saskatchewan Commission of Inquiry into Provincial and Municipal Taxation. Ibid., p. 305,

29. P. 26; quoted by Perry, p. 306.
30. Report of the Royal Commission on Dominion-Provincial Relations, (Ottawa: King's Printer, 1940), pp. 111-115; Perry, 316-319.
31. Report, Bk. II, p. 111; quoted in Perry, p. 316.
32. Report, Bk. II, p. 111.
33. Report, pp 111-112; noted in Perry, p. 317.
34. Report, Bk. II, p. 113; quoted by Perry, p. 318.
35. Ibid.
36. Report, Bk. II, pp. 153-160.
37. Report, Bk. II, pp. 117-120; Perry, pp. 319-322.
38. Report, Bk. II, pp. 81-86, 121, 125-130, 162; Perry, pp. 323.
39. Perry, Vol. II, p. 328.
40. Perry, Vol. II, p. 372.
41. Perry, Vol. II, pp. 344-346.
42. Perry, Vol. II, table, p. 368.
43. Quoted in Perry, Vol. II, p. 355.
44. Perry, Vol. II, p. 355.
45. Perry, Vol. II, pp. 357-358.
46. Perry, Vol. II, p. 358.
47. Report on Surplus-Stripping, pp. 16-17.
48. Ibid., p. 17.
49. Ibid., p.17.
50. Interview with Robert Bryce, Jan. 14, 1983. See Granatstein, The Ottawa Men: the civil service mandarins, 1935-1972, (Toronto: Oxford University Press, 1982), p. 165-168, for a discussion of the social reformist influences within the Dominion bureaucracy on post-War social policy and public finance. While it is true that progressive "mandarins" proposed and drafted the measures, they were put forward in response to political challenges to the Liberal Party from the CCF.
51. Perry, Vol. II, p. 395.
52. Some of the recommendations of the Ives Commission, which reported in March, 1945 are discussed below.
53. Quoted by Perry, p. 416.
54. Ibid., pp. 416-417.
55. Ibid., p. 418.
56. Ibid., p. 419.
57. Ibid., pp. 419-420.
58. Perry, pp. 419-420.
59. House of Commons Debates, Mar. 28, 1950; quoted in Conway and Smith, The Law Concerning Capital Gains, Royal Commission on Taxation, Study No. 19b (Ottawa: Queen's Printer, 1967), pp. 96-97.
60. The Association later changed its name to the Canadian Institute of Chartered Accountants.
61. An item in the Canadian Tax Journal, Vol. 10, No. 1 (Jan.-Feb., 1962) notes that the charter members of the Foundation were Gordon Peter Campbell, John Grant Glassco, Harrison Cooley Hayes, and Molyneaux Lockhart Gordon.

62. Membership application form, Report of the Proceedings of the Twentieth Tax Conference, (Toronto: CTF, 1968), last page.
63. Canadian Tax Journal, Vol. 15, No. 5, (1967), p. 433.
64. "5th Report to the Parent Associations", Canadian Tax Journal, Vol. 1, No. 5, (Sept.-Oct., 1953), pp. 518-524.
65. Ibid., p. 524.
66. Canadian Tax Journal, Vol. 2, No. 2 (May-June, 1954), p. 135.
67. Vol. 1, No. 3 (May-June, 1953), p. 236.
68. The Canadian Tax Journal, Vol 1, No. 6 (Nov.-Dec., 1953), p. 3. "The Most Unusual Idea in Canada", Canadian Tax Journal, Vol. 9, No. 1 (Jan.-Feb., 1961), p. 5.
70. Canadian Tax Journal, Vol. 1, No. 6 (Nov.-Dec., 1953).
71. Stripping of Corporate Surplus, pp. 18-19. The Royal Commission study refers to sections 32A(3), 14, and 19(2).
72. Ibid., p. 18.
73. Ibid., p. 19.
74. Ibid., p. 22.
75. Ibid., pp. 19-20.
76. Ibid., p. 21.
77. Ibid., pp. 19, 21. This was Part IIB (section 105B) of the Act.
78. Part IIC (section 105C, Ibid., p. 21.
79. The Concept of Income - The Receipts Side, Royal Commission on Taxation, Study No. 20, (Ottawa: The Queen's Printer, 1968).
80. Ibid., pp. 62-63.
81. Ibid., pp. 63-85.
82. Ibid., pp. 87-102.
83. Ibid., pp. 105-107.
84. Ibid., pp. 108-109.
85. Ibid., pp. 116-122.
86. Ibid., pp. 122-125.
87. Ibid., pp. 125-127.
88. Ibid., pp. 132-139.
89. Ibid., pp. 138-139.
90. Ibid., pp. 160-162, 173-180, 187-194.
91. Ibid., pp. 194-196.
92. Ibid., pp. 197-201.
93. Don Mills: CCH Canadian Limited, 1965. The references are not mutually exclusive, as one case may be referenced under two or more topic headings.
94. "Identifying Income", etc, Data Papers, Sixth Tax Conference (Toronto: Canadian Tax Foundation, 1953), pp. 1-2.
95. Ibid., p.2.
96. Ibid. Quoted from The Canadian Bar Review (Nov., 1951), p. 927.
97. Ibid.
98. See Report of the Nineteenth Tax Conference, pp. 353-357.
99. Canadian Chartered Accountant, (Feb., 1952), p. 55; Quoted in "Identifying Income", pp. 10-11.
100. Ibid., p. 14.
101. Ibid., p. 15.
102. Ibid., p. 20.
103. Ibid., pp. 21-22.
104. Ibid., p. 22.
105. Conway and Smith, p. 8.

106. J. Harvey Perry, Taxation in Canada, 3rd edition, (Toronto; University of Toronto Press, 1961.), p. 46.
107. Conway and Smith, pp. 90-91. The authors quoted J. Harvey Perry, Taxation in Canada, p. 45.
108. Conway and Smith, p. 107, cite sections 3, 4 and 139(1)(e).
109. [1959] CTC 275; 59 DTC 1177.
110. [1960] CTC 46; 60 DTC 1041; cited in Conway and Smith, p. 107.
111. [1960] CTC 390; 60 DTC 1272; quoted in part by Conway and Smith, p. 110.112. Conway and Smith, pp. 118-119.
113. 60 DTC 1270, at p. 1271.
114. 60 DTC 1232.
115. 62 DTC 1131, at p. 1133. Quoted in part in Conway and Smith, pp. 117-118.
116. Report of the 1961 Tax Conference, (Toronto: Canadian Tax Foundation, 1962.) pp. 345-349.
117. McGregor, Canadian Tax Journal, Vol. 10, No. 3 (May-June, 1962), p. 166; quoted by Stuart D. Thom, Q.C., Osler, Hoskin & Harcourt, Toronto, Report of the 1962 Tax Conference, (Toronto: Canadian Tax Foundation, 1962.), pp. 71-72.
118. McGregor, Canadian Tax Journal, Vol. 10, No. 3 (May-June, 1962), p. 166; noted by Thom, Report of the 1962 Tax Conference, p.72.
119. D.J. Kelsey, of Helliwell, Maclachlan & Co., Vancouver, 1960 Conference Report, p. 296.
120. 1960 Conference Report, p. 291.
121. Ibid., p. 298.
122. Ibid., pp. 306-307.
123. Kenneth Lem. Carter, "Canadian Tax Reform and Henry Simons", The Journal of Law and Economics, Vol. XI, p. 231; Hartle interview.
124. 1961 Conference Report, pp. 264-270.
125. Ibid., p. 266.
126. Ibid., pp. 268-269.
127. Ibid., p. 269.
128. Ibid., p. 270.
129. Of course, the Conference participants would have already have been aware of Kennedy's tax reform plans from press reports. Surrey's banquet address, however served as a reminder, and, along with a number of problem sessions, helped to set the tax reform tone of the Conference.
130. 1961 Conference Report, p. 6.
131. Ibid., pp. 9-16.
132. Ibid., pp. 16-23.
133. Ibid., p. 23.
134. 1961 Conference Report, pp. 23-41. The Financial Post, (April, 13, 1963) in a report of an address by Stikeman to the Montreal Institute of Investment Analysts, predicting a capital gains tax for Canada, referred to Stikeman as "widely regarded as one of Canada's top tax experts."
135. Ibid., p. 26.
136. Ibid., p. 27.
137. Ibid., pp. 28-32.
138. Ibid., p. 40.
139. Ibid.
140. Ibid., p.41.

141. Ibid.
142. 1961 Conference Report, p. 75.
143. See above, pp. 86-88.
144. Vol. 10, No. 1, p. 3.
145. Ibid., p. 4.
146. Canadian Tax Journal, Vol. 10, No. 5 (Sept.-Oct., 1962), p. 303.
147. Ibid., p. 302. . end of notes

Chapter III: The Royal Commission on Taxation

Introduction

Once raised to the level of a political problem, the specific institutional processes used to deal with it are commonly subject to some degree of manipulation. As the outcome of the political process is not independent of the institutional route through which it is channelled, the selection of the institutions to deal with the problem and the specific individuals occupying the command-posts of these institutions become, themselves, objects of contention.

Influential tax professionals and business elites had come to the conclusion by 1962 that a fundamental reform of the income tax system was required in order to remove what they believed were tax-induced impediments to entrepreneurial activity and economic growth in Canada. Although business was well-represented in the established political institutions, it was expected that the customary budgetary route for tax changes would simply produce more of the same, patch-work repairs. A royal commission composed of the "right people" would (so it was hoped) be insulated from the popular pressures which had led vote-conscious governments toward expensive welfare-type spending programmes and steeply progressive income tax rates.

The following account of the appointment and formation of the

Royal Commission shows how the tax professionals and business elites succeeded in having the Diefenbaker government adopt their project of a royal commission on taxation and how the media propagated the views of the same groups on which aspects of the tax system needed reforming and what the goals of the reform ought to be. While the membership of the Commission was reassuring to the tax professionals and business, events were taking place within the senior staff of the Commission which would profoundly alter the trajectory of tax reform.

Appointment of the Commission

It is a commonplace observation among Ottawa civil servants of the period that Prime Minister Diefenbaker had little interest in, or aptitude for economic policy. He was interested in re-election, however, and as the Conservative mandate from 1958 was approaching the end of its normal lifespan, he was forced to pay more than the customary attention to the Party's declining level of popular support. The April 1962 Gallup poll had shown the Liberals ahead in a national sample, 43 to 38 per cent for the Tories. The proportion of "undecided" had increased from 22 to 30 per cent near the end of 1960, and in Ontario, the "undecided" had reached 34 per cent.[1] This clearly spelled trouble for the Tories. Toronto's eighteen ridings, seventeen of which were then held by the Conservatives, were expected to play an important role in the coming election.[2]

Speculation about an election was reinforced by Mr. Diefenbaker's

remarks to the National Young Progressive Conservatives' Convention, in Ottawa on April 8th, 1962 that the voters would show their trust in his Government.[3] One of the resolutions put before that convention was that "a Royal Commission be appointed to consider the need for a new and more feasible Canadian tax structure."[4]

Oakley Dalgleish, editor of the the Toronto Globe and Mail had for some years been urging successive federal governments to appoint a Royal Commission to study the taxation system. Any Globe editorial dealing with economic or fiscal questions was likely to wind up with a call for an enquiry into the tax system, such as the two Dalgleish had written commenting favourably on the Minister of Finance, Donald Fleming's budget speech of April 10th, 1962. The first, published the morning after the budget, complimented Fleming for not presenting the usual pre-election budget full of vote-getting gimmicks, and praised it as a "business Budget", with its incentives for business research and tax incentives for increased sales by corporations. The aim of these incentives, said Dalgleish, was to "help business -- and the country -- help itself."[5] Yet this laudatory use of tax incentives pointed to the poor state of knowledge in this area:

> The new measures, meanwhile emphasize all the more the need for a thorough review of Canada's entire tax structure. Tax incentives, to be as effective as possible, require a detailed knowledge of the effects of taxation generally. It is to be hoped that Mr. Fleming's limited use of new incentives in this Budget is a promise that such a study is soon to be made. It is urgently needed.[6]

Dalgleish expanded on this theme ten days later in an editorial

entitled "Levels of Taxation",[7] referring to "recent statements" by E.G. Burton, Chairman and President of Simpson's Ltd. that "taxation in this country is far too heavy with the result that business enterprise is discouraged and promising young people move to the United States...."[8] Dalgleish repeated his contention:

> ...frequently expressed by this newspaper and by other business leaders: Canadians are grievously overtaxed without realizing it. Every businessman can see in his own field some of the evil effects of crushing taxation, but few if any can see the whole picture and appreciate the damage to the national economy.
>
> This is the reason that we, and others, have advocated the appointment of a Royal Commission to examine the tax structure in Canada. Once a Commission had established the facts about Canadian taxation, as compared with taxation in other countries, Mr. Burton might find public support for his demand that taxes should be reduced and the nation should learn to live within its resources.[9]

Leslie Frost, the former Premier of Ontario, and a close friend of Dalgleish, had also recommended such a course to Diefenbaker, putting the Government of Ontario on record favouring a Royal Commission on Taxation.[10] On June 10, 1958, not long after the federal Conservatives sweeping electoral victory, Dalgleish had accompanied Frost, Diefenbaker and Donald Fleming on a fishing trip, during which the conversation turned to Dominion-provincial fiscal relations. The next day, at Frost's request, Dalgleish put his thoughts down on paper, recommending to the Prime Minister that he announce a "committee or commission, to examine the tax structure of this

country, with special attention to the full and varied impact of the different forms of taxation..."[11] Dalgleish, and Frost in a supporting letter enclosed with Dalgleish's note, placed this within the context of the need of the provinces and municipalities for a greater share of tax revenues and for a Dominion-provincial conference on the issue. Dalgleish, perhaps remembering the strained relations between the Rowell-Sirois Commission and several of the provinces, stressed the importance of full provincial co-operation, and suggested that Mr. Diefenbaker go so far as to ask the premiers for their suggestions regarding the composition of the commission.[12]

Frost had strongly backed Diefenbaker during the 1958 election, in the course of which the Tories had secured an overwhelming victory in Ontario, including all the Toronto ridings. While Frost, having resigned as the Premier the previous August, was no longer in a position to give him the same support in 1962, the Prime Minister hoped that John Robarts, who had succeeded Frost as Premier in November, would also lend his support to the federal Party in Ontario. Robarts had also publicly urged the federal Government to undertake a thorough enquiry into the tax system.[13]

It may be significant that Mr. Diefenbaker chose to announce the election date of June 18th at a "Hail-to-the-Chief" banquet at Queen's Park, with Leslie Frost and Robarts in attendance.[14] Federal-Provincial financial relations was reportedly among the topics of conversation, as were plans for the general election.[15]

Whatever the prospects were for Robarts' active participation in the campaign, it is very likely that Diefenbaker's hope for the support of the Globe and Mail, and business, during the coming election was the decisive factor in his decision to promise a Royal Commission on Taxation. While Dalgleish had commented favourably on Fleming's pre-election budget, he had also called for an in-depth study of tax incentives, and was severely critical of the Government's fulfilment of its previous election promises to increase welfare benefits "at a time when the country could not afford them".[16] While it was most unlikely that the Globe and Mail would support the Liberals, the solid backing of this influential newspaper could not be taken for granted. Diefenbaker probably reasoned that the Royal Commission would provide that assurance.[17]

Assurances of some kind toward the financial community appeared to be needed at that point. Speculative pressures on the Canadian dollar had led to a sharp drop in the Government's foreign exchange reserves, forcing Donald Fleming to announce on the evening of May 2nd, 1962 that the dollar had been devalued from 95 cents to 92.5 cents in terms of the American dollar.[18] The Globe and Mail quoted "one of Toronto's largest investment dealers" that there had been "a considerable reduction in confidence in the Canadian fiscal policies and a steady withdrawal of money from investment as a result."[19] The front page story then quoted "another broker" who wondered whether the Government could prevent a further slide, suggesting that the situation was "out of control."[20]

Dalgleish's editorial the following day traced the devaluation to Canada's declining exports, "Canadians living beyond their means" and to high government spending. While "the world" was demanding that Canadians put their "economic house in order", he stressed that this would not happen until the Government set the example "by putting its fiscal house in order".[21] Clearly, the mere promise of a Royal Commission could scarcely be calculated to stem a run on the dollar. However, if the downward pressure on the dollar was an indication of a want of investor confidence in the Government's fiscal policies, as the previous day's Globe and Mail story had reported, then Diefenbaker must have hoped that the Government's announced intention to undertake a serious study of the taxation system might be interpreted as one positive long-term measure.

There did not appear to be any strong political arguments against including a Royal Commission on Taxation in the Tory election platform. It was being urged on the Government by businessmen, by the editor of the Globe and Mail, and it would cost very little compared to most election promises. It would also be difficult for anyone to strongly oppose, since the tax professionals appeared to favour an enquiry. Moreover, it had the advantage of freeing the Government from taking any controversial position on tax structure matters: one would not want to prejudge the outcome of the study. It must have appeared like a very safe and inexpensive way to secure what could turn out to be the necessary margin of votes in a crucial region of the country.

Mr. Fleming was only lukewarm to the idea, nor did it receive any support from his Departmental advisors.[22] Claude Isbister, the Assistant Deputy Minister for Taxation, was skeptical of the whole idea, preferring small-scale revisions, usually within the annual budgetary process.[23] However, Fleming did not actively oppose Diefenbaker's plan, and the Prime Minister put little faith in the advice of most senior civil servants.[24] The large number of Royal Commissions appointed during the Diefenbaker years has often been attributed to his deep distrust of the federal bureaucracy, and was almost certainly a contributing factor in this case.

On May 6th, 1962, in his opening campaign speech in London, Ontario, Mr. Diefenbaker announced his intention to appoint the Royal Commission. Not surprisingly, the event made front page news in the following morning's Globe and Mail. Next to the headline, "PROBE WOULD SEEK FAIRNESS, PM PROMISES REVIEW ON CANADIAN TAX LAWS" and "5,000 hear Diefenbaker Plans", was a quarter-page photograph of Mr. Diefenbaker at the lectern, with Premier Robarts, Donald Fleming, Leslie and Mrs. Frost clearly shown in the background. The news featured a number of favourable comments on the promise from businessmen, including Karl E. Scott, President of Ford Motor Company of Canada, W. Harold Rea, President of Canadian Oil Companies, W.O. Twaits, President of Imperial Oil (whose Vice-President, Trevor F. Moore had advocated a commission on taxation at the Canadian Tax Conference the previous November), and Leonard F. Wills, Vice-President of Honeywell Controls.

Dalgleish's editorial in the same issue, "The Vital Pledge" was predictably enthusiastic:

> The announcement is of great satisfaction to this newspaper which had been calling for 17 years -- since February, 1945 -- for a thorough and impartial inquiry into the tax jungle that has grown up and come close to strangling our economy. It will be of equal satisfaction to the many business and provincial leaders who have joined with us in the demand. We have suffered many disappointments through the long campaign from politicians who have hinted and not delivered; now is our time to rejoice that at last we have a Prime Minister who has given a specific understanding he can be relied upon to honour.
>
> Mr. Diefenbaker clearly appreciates that action to investigate and reform our tax system is the essential foundation for all other pledges he may make in this campaign -- to stimulate economic growth, expand job opportunities, improve social welfare, and carry through great projects for national development. He is realistic enough to know that business is the only source of wealth and security; that business must be enabled to earn the money the politicians want to spend.
>
> The importance of taxation policy in the business climate does not need to be established in this day and age. Everybody should know by now that high and ill-designed taxes cripple business, slow down growth, and reduce the revenues available to government. That is the ailment Canada has been suffering from for years, and the ailment that a Royal Commission can go far to cure.[25]

The Globe and Mail, was read by, and tended to reflect the opinions of Canadian businessmen, especially those in the Toronto region. Dalgleish's editorials calling for "tax reform", in the sense of lower taxes on business and high-income individuals, articulated a widespread sentiment in business circles.

Businessmen were also using other channels to make politicians aware of their views on tax policy. Wallace McCutcheon pressed the

idea on Diefenbaker, reputedly going so far as to make that a condition of his entering the Cabinet.[26] On August 9, 1962, the Prime Minister appointed McCutcheon to the Senate and brought him into the Cabinet in order to strengthen the Government's contacts with and support from the business world.[27] As one of the controlling shareholders of the Argus group of companies, along with E.P. Taylor (who also spoke in favour of a critical study of the tax system)[28] and J.A. McDougald, McCutcheon was well-endowed with business contacts: Chairman of St. Lawrence Corporation, The National Life Assurance Company of Canada; Vice-Chairman of Canadian Breweries Limited, Canadian Equity and Developments Company; Chairman of the Executive Committee of British Columbia Forest Products; and a Director of another 18 corporations, including The Canadian Bank of Commerce, Avco of Canada, Carling Brewing Company, Dominion Stores, Dominion Tar and Chemical Company, Dow Brewery and Massey Ferguson.[29] He also had a number of philanthropic and public service directorships, such as the Board of Governors of the University of Toronto and was a member of the Rideau Club and other elite clubs in Toronto, Montreal and Nassau. McCutcheon's position on the Board of Governors of the University of Toronto would have brought him into contact with fellow board member and taxation commission booster, Oakley Dalgleish.

Although the promise of a Royal Commission on Taxation did not play a major role in the election campaign, it was received favourably by business and did not do the Conservatives any harm. The campaign was fought on other issues, chiefly the poor Canadian economic

performance during the life of the Diefenbaker Government. Diefenbaker later described the speculative run on the dollar and its devaluation as the the most important cause of the Conservatives' loss of their commanding majority in the House of Commons.[30]

The new Diefenbaker Government, with only minority support in the House after June 18th, 1962 continued to face economic difficulties during the summer. On June 22, in response to a continued drain on the foreign exchange reserves, the Government suddenly imposed an "Austerity Programme", featuring exchange controls, a temporary import surcharge, cuts in government expenditures, and a freeze on civil service salaries.

Newspaper editorial reaction to the Austerity Programme was generally favourable, though the Penticton Herald probably expressed a widespread view, certainly in business circles, that economic recovery was the key to the solution, and that this required tax incentives and tax reform:

> Prime Minister John Diefenbaker, during the election campaign, announced his intention to appoint a Royal Commission to study reform of Canada's crippling tax structure. The sooner he is able to announce the establishment of this commission, the sooner businessmen will feel a new confidence in the future. The last budget in Ottawa offered valuable tax incentives to businessmen, particularly in the field of research. The next budget -- and we hope it will be introduced soon after Parliament reassembles -- should offer further incentives.[31]

The series of unhappy accidents which the Tory Government experienced with regard to economic and monetary policy -- slow

economic growth before 1962, high levels of unemployment, the Coyne affair, the run on the dollar, the apparent necessity of "Austerity" measures -- probably contributed to the Government's decision to announce the Royal Commission on Taxation.[32] Carter himself suggested to the press that the Austerity Programme may have been one reason for the enquiry, noting that a reformed taxation system might stimulate the economy and increase tax revenues.[33]

The Prime Minister's announced the creation of the Royal Commission on August 27th. Its Chairman was to be Kenneth LeM. Carter, of Toronto, a senior partner in the accounting firm of McDonald, Currie & Company. Although George Nowlan had been appointed Minister of Finance by this time, the Chairman of the new Commission was a personal friend of Fleming, and the latter's preferred choice.[34] If Carter had any political party affiliations they were not well known, though the fact of his appointment to head the Commission led others to assume that he was linked in some way to the Conservative Party.[35]

Carter had all the right qualifications and business contacts for the job. He had been Chairman of the "Carter Committee" on the Federal Sales Tax, appointed by the Liberal government in 1955. Like most tax specialists, he was a member of the Canadian Tax Foundation, and a former Chairman of its Board of Governors. The official announcement credited Carter with "a unique knowledge of the Canadian tax structure", which was probably only a mild overstatement.[36] He had further suitable qualifications, being a past President of the

Institute of Chartered Accountants of Ontario, and was then serving his third term as President of the Canadian Welfare Council. One item which received no press coverage was his membership on the Board of Directors of the Southam Company Limited, one of the largest newspaper publishers in Canada.[37] He was reputed to be hard-working and on the conservative side in philosophical approach, but without any partisan political ties. It would have been difficult for anyone to criticize this appointment, and apparently no one did.

The other five Commissioners were not named until September 17th, after consultation with Nowlan, McCutcheon, Fleming and, as was customary, with the newly-appointed Chairman.

J. Harvey Perry, who was "everybody's choice" for the Commission[38] was Executive Director of the Canadian Bankers' Association and had been Director of the Canadian Tax Foundation from 1952 to 1961. His service with the Foundation brought him into close contact and friendship with Carter, who later insisted on having him on the Commission.[39] A graduate of the University of Toronto in Economics and Political Science, he served as an official in what became the Taxation Division of the Department of Finance from 1936 to 1951. An authority on the federal Income Tax, he had written two major works and numerous published articles on the Canadian taxation system.[40] Perry was not appointed to chair the Commission because it was felt that his long career in Finance might undermine the image of an independent inquiry,[41] but it was widely understood that Perry was expected to be "the tax expert" on the Commission.

The remaining Commissioners were appointed primarily for reasons of regional and social representation. A. Emile Beauvais, chartered accountant and senior counsel for the Quebec City accounting firm, Samson, Belair, Coté, Lacroix et Associés, in addition to "representing" Quebec, was a specialist in tax matters on the accounting side, and also brought a business viewpoint to the Commission, being Executive Vice-President and Director of Donohue Brothers, and a Director of Dominion Corset and Quebec Savings Bank. He had graduated from Laval with a doctorate in Financial Sciences and began practicing as a chartered accountant in 1925. He was a Past President of the Canadian Institute of Chartered Accountants, and international member of the American Institute of Accountants. Beauvais had also been one of the "Committee of Four" appointed by Donald Fleming in October, 1961 to study and report on the problem of the taxation of corporate distributions or "surplus-stripping".[42] Like Perry and Carter, his general views on tax matters were not unknown to the Government and the Department and were no cause for alarm.

Mrs. S.M. (Eleanor) Milne, of Winnipeg, considered to represent women and the prairie provinces, was Treasurer of the National Council of Women and also assisted her husband in his accounting practice.[43]

Representing the Maritime region was Donald G. Grant, a Halifax lawyer, Director and General Manager of the Nova Scotia Trust Co. He was also Vice-President and Manager of the Yarmouth Building and Loan

Society, and a Director of Maritime Steel and Foundries, and Pictou County Bus Services. He received his Bachelor of Arts and Bachelor of Laws from Dalhousie University and was called to the Nova Scotia Bar in 1932. He was Past-President of the Trust Companies Association of Canada and a member of the Nova Scotia Barristers Society and the Canadian Bar Association. While not a tax expert, he was well-informed in tax matters.[44]

Charles E.S. Walls, of Victoria, was intended to represent the West and agriculture, and to add some balance to the otherwise overwhelming business representation on the Commission. Educated at the Edinburgh College of Arts, he farmed for four years in Canada, then studied business at Alberta College in Edmonton, and joined a western wholesale house as Buyer and Departmental Manager. During the mid 'thirties he became Provincial Manager for Manitoba for an insurance company. Leaving the army as a Lieutenant-Colonel following the War, he took up farming in British Columbia and later became a Director, and then Manager of the B.C. Federation of Agriculture. Since 1951 he had been an Executive Director of the Canadian Federation of Agriculture and a member of its National Policy Committee. In 1959 he was named by the Diefenbaker Government to the Advisory Committee of the Farm Credit Corporation.

It was a Commission with three recognized tax specialists complemented by tax-wise professionals. With the qualified exceptions of Walls and Milne, all brought with them a business viewpoint. Labour was conspicuously without representation, and the Commission's

voluminous press clippings contain no indication of any complaint about this.

Terms of Reference for the Commission

The Commission's terms of reference were set out in Order-in-Council P.C. 1962-1334, dated September 25th, 1962. As their considerable breadth came to be of great import for the way the Commission perceived and carried out its task, the relevant section of that document is reproduced below. The six Commissioners were named, and directed to:

> ...enquire into and report upon the incidence and effects of taxation imposed by Parliament, including any changes made during the currency of the inquiry, upon the operation of the national economy, the conduct of business, the organization of industry and the positions of individuals; and to make recommendations for improvements in the tax laws and their administration that may be consistent with the maintenance of a sufficient flow of revenue; and without restricting the generality of the foregoing, the Commission shall consider and report upon:
>
> (a) the distribution of burdens among taxpayers resulting from existing rates, exemptions, reliefs and allowances provided in the personal and corporation income taxes, estate taxes and sales and excise taxes, taking into account also the jurisdiction and practices of the provinces and municipalities;
>
> (b) the effects of the tax system on employment, living standards, savings and investment, industrial productivity, and economic stability and growth;
>
> (c) provisions in existing laws which may have given rise over the years to anomalies or inequities or which may require action to close loopholes which

permit the use of devices to avoid fair taxation;

(d) the effects of the income, sales and excise taxes and estate duties on income and investment flows which affect the balance of international payments and economic relations with other countries;

(e) the means whereby the tax laws can best be formulated to encourage Canadian ownership of Canadian industry without discouraging the flow of investment funds into Canada;

(f) the changes that may be made to achieve greater clarity, simplicity and effectiveness in the tax laws or their administration; and

(g) such other related matters as the Commissioners consider pertinent or relevant to the specific or general scope of the inquiry.[45]

These terms of reference were drafted by Claude Isbister, the Assistant Deputy Minister for Taxation in the Department of Finance with the assistance of the Taxation Division,[46] and also of Gear McIntyre, Deputy Minister of National Revenue, Taxation, and Robert Bryce, who was Clerk of the Privy Council at the time. The draft was discussed with both George Nowlan, Fleming's successor as Minister of Finance, and with the new Minister of Trade and Commerce, Senator Wallace McCutcheon.[47] Nowlan, a booster for the idea of a royal commission on taxation was appointed to the Finance portfolio on August 9, the same day as his friend, McCutcheon, was appointed to the Cabinet and Senate.

Just about every tax controversy was included with the exception of the federal-provincial division of taxing powers, the tariff structure, and the question of using the tax system for transfer payments to those without any taxable income (negative taxation). The

terms of reference had been made deliberately very broad.[48] Bryce had felt that wide-ranging remedies were needed to cure the surplus-stripping problem and other abuses than had been recommended by the Committee of Four.[49]

There was a considerable amount of press criticism regarding the omission of federal-provincial fiscal relations, since it was not clear how one could recommend changes to federal taxes without affecting sources or amounts of revenue going to the provinces. Department of Finance officials, however, felt that the Commission had enough work to do without the massive addition of the constitutional question of the division of taxing powers.[50] No doubt, they also remembered the difficulties which the Rowell-Sirois Commission had with provincial governments. In addition, a five-year tax-collection agreement had just come into effect and the provincial governments would have been against putting the whole matter before a Royal Commission.[51]

With the exception of Premier Robert Stanfield of Nova Scotia,[52] no one questioned the omission of the tariff from the terms of reference. It was the opinion of the Government, and the new Royal Commission, that the tariff was more a question of commercial policy rather than tax policy, and therefore properly outside the scope of its terms of reference. An additional consideration was that the margin for reform in this area was limited by international agreements.

Consideration of a negative income tax was omitted from the terms

of reference because no one in Finance or Cabinet had thought about it. Like tariffs, income redistribution through cash payments to those in need was not perceived to come under the heading of tax policy. Even if they had thought of it, the people who were complaining loudly about the existing tax system, and had pressed for a royal commission, were complaining about too much re-distribution of income from the "rich" to the "poor". The last thing they had in mind when they talked of tax reform was a negative income tax for more effective income re-distribution.

Harvey Perry, in his retrospective on tax reform, does not mention the tariff as a significant omission from the terms of reference, but considered federal-provincial fiscal relations and the distributional aspects of transfer payments to persons as "important exclusions in a general review."[53] He acknowledged, however, that the Commission had enough to occupy itself without any additional burdens.[54]

Interpretation of the Terms of Reference by the Press

Canadians learned of the appointment of the Commission through the print and electronic media. For most, this was their only source of information about the Commission: its terms of reference, the testimony at the public hearings, its research findings, and its recommendations for reforming the tax system. Being vitally interested in what the press had to say about it, the Commission subscribed to the Canadian Press Clipping Service, and thus a

systematic compilation of press reports from all parts of Canada is available.

Appointment of the Commission was welcomed by practically all newspaper editors, and nearly all opinion reported in the press agreed that a thorough study and reform of the tax system was long overdue and would be of great significance for the economic future of the country. The August 27th edition of The Evening Times-Globe of St. John reprinted the previous day's editorial of the Montreal Gazette, headed "Present System Handicaps Canada -- The Urgency of Tax Reform":

> The awareness grows that what Canada lacks, and what Canada needs, is a philosophy of taxation. The country has plenty of taxes. But they are not imposed on any comprehensive principle, or even with much thorough concern for the results....
> Prime Minister Diefenbaker promised that he would appoint a Royal Commission to review Canada's tax structure. Despite the fact that there have been many royal commissions, here is one that Canada cannot do without. It might for the first time, seriously turn Canadians to realizing what a confusion their tax system is, and how seriously it may be thwarting their aims.[55]

All the opposition parties could say was that it was overdue, or that appointing a Royal Commission would take too long to implement reforms which were urgently needed. Liberal leader Lester Pearson issued a statement saying that his party had been advocating such a study for five years and that he hoped that the Royal Commission would "not prove a further evasion of responsibility by this government".[56] NDP leader, Tommy Douglas pointed out that the Commission could bring improvements only in the long run, and that short-term relief for winter unemployment was needed right away.

Social Credit leader Robert Thompson also criticized the slowness of the Royal Commission route when immediate action was required.[57] While the Prime Minister said that he wanted the Commission to "scientifically examine the Federal Tax Structure... eliminate the inequities and anomalies and streamline it, modernizing the whole system", he conceded to his critics that reform must not be postponed. As the Ottawa Journal reported:

> Speed was of the essence, suggested the Prime Minister, and the Commission would be asked to get down to work at the earliest possible moment.
> It would be one of those "efficient, fast-working commissions, too" he said, parrying the suggestion that this type of investigation was one that could "drag on for two or three years."
> "We want a report and recommendations as soon as they can properly be prepared", he said.[58]

Most editorial opinion, and opinion reported in news items stressed the patchwork nature of the existing tax system, the result of decades of lobbying and ad hoc application "band-aid" solutions. Some rational pattern was required. The most urgent problem was considered to be the presumed drag which the tax system put on economic growth. The tax rates were too high, discouraging individual incentive and forcing talented people to leave the country. The corporate income tax was a barrier to Canadian exports and capital investment. The estate tax was destructive of small Canadian-owned businesses. Finally, the complexity of the system was itself an economic disincentive.

Newspapers gave prominent coverage to business spokesman supporting the appointment of the Commission and calling attention to

the effects of taxes on economic growth. The Toronto Star of August 28, and many other Canadian papers, printed a United Press International story from Montreal, reporting the remarks of William S. Kirkpatrick, President of the Canadian Chamber of Commerce. The Chamber, he said, had urged such a study for several years, and he asked that particular attention be paid to the effect of taxation on individual and business incentives:

> No single reform would do more to restore the sense of the worth of enterprise and effort than to relieve the discouraging effect of tax rates which absorb a third or a half or more of the fruits of every venture.... It is important that taxation be designed as a stimulant to economic growth.[59]

Kirkpatrick's words, and similar statements by other businessmen, were quoted approvingly in many newspaper editorials. The Toronto Telegram had a major feature entitled, "Give Us Tools To Do Job: Tax Plea", with the photographs and comments of Edgar G. Burton, Chairman and President of Simpsons, J.R. Bradfield, President of Noranda Mines, H.E. Landford, President of Chartered Trust Co., and Trevor F. Moore, Vice-President of Imperial Oil. All contributed to different aspects of the common theme that business needed some form of tax relief in order to grow. Two anonymous executives thought the Commission should look at the high tax rates paid by people in the upper income brackets: "I'm not a wealthy man, said one, but I might be misunderstood." All welcomed the choice for Chairman: said Moore, "He's an expert and will do a first class job."[60]

With taxes and tax reform in the news, the statements and

publications of the Canadian Tax Foundation were frequently quoted and cited. It was pointed out that the Foundation had already made a monumental contribution to the development of knowledge of our tax system and of highly qualified people to assist the Royal Commission. The Foundation-supported study of the economic effects of taxation at Queen's University was often mentioned, as was Irving J. Goffman's study, The Burden of Canadian Taxation, published by the Foundation a month earlier. Most reports of the latter study discussed what it had to say regarding the total magnitude of the tax burden rather than its distribution by income class, although Fraser Robertson's analysis in the Globe and Mail[61] did reveal Goffman's finding that the burden of the tax system was heavier on low income earners. Kenneth Eaton's attack on the progressive income tax, aired at the 1961 Tax Conference and published in the Foundation's Conference Report, were occasionally referred to, as were the Foundation's Director Ronald Robertson's remarks in the Canadian Tax Journal about the importance of continued economic growth in order to prevent the effective tax burden from getting any heavier,[62] and about the need for simplifying the tax laws.[63]

A slightly less pervasive theme in newspaper editorials was the apparent failure of the Government to launch the Commission as a co-operative venture with the provincial governments. The August 30th editorial in the Montreal Star was typical:

> If... the national tax structure is to be changed radically, the political decisions will need to be taken by Ottawa and the provinces acting together. In other words, Ottawa and the provinces will need to agree on a

> redistribution of taxing powers, for the federal tax structure cannot be considered in isolation.
>
> Even though the [preliminary] terms of reference do not mention provincial taxes, the two are so interwoven that one cannot be considered without the other. So that, whether the provinces like it or not, they will want to submit briefs to the tax commission in order to protect their own constitutional interest.[64]

A third theme which was expressed in a few large metropolitan dailies and which found an echo in many small-town papers was the complaint that taxes were simply too high, the result of too much government. The Montreal Gazette likened the new mood favouring tax reform in Canada to a similar climate in the U.S., and attributed both to "a growing awareness that this continent has overburdened the mainspring of effort..." The editorial charged that high taxes had curbed the work incentive, reduced economic activity and thereby cut its own government revenues, producing "awesome deficits year after year. It is becoming evident that progressive theory of taxation is becoming the author of its own defeat."[65] The editorial concluded by quoting a newsletter from the National City Bank that government spending must be reduced in order to balance the budget and reduce the tax burden. A more moderate variant of this theme was that the relative emphasis on the income tax should be reduced in favour of sales taxes.

Interpretation of the Terms of Reference by the Commission

The Commission began to interpret its terms of reference even

before their official publication. Only a week after his appointment as Chairman, two weeks before the appointment of the other commissioners, and three weeks before the official announcement of the terms of reference, Carter drew up an initial research agenda for the Commission.[66] Fifteen groups of studies were listed under three headings. "Economic Studies" would include historical studies of Canadian taxation, comparative studies with the United States and Europe, yield of Canadian taxes by various categories of taxpayers, and the relative weight of taxes on exports as compared to those of other countries. Under "Professional Staff Studies", Carter included the incidence of the corporation tax, "said to be already underway" by the Queen's University group with the support of the Tax Foundation, the taxation of corporate income, including "double taxation" and "surplus-stripping", income tax concessions and incentives, "loopholes and abuses" (including living and entertainment expenses and surplus-stripping), transferability of losses between taxpayers, and costs of collection and compliance. The third class of studies "by Economic and Professional Staff" included "Taxation of capital gains" and four studies on sales taxes.[67]

Shortly afterward, Carter and Perry got together for two days to consider the basic strategy of the Commission. They discussed the possibility of a "quick patch-up job", which would simply examine the specific complaints which appeared to be justified and sufficiently serious, and propose solutions for each. While attracted by this option, they eventually rejected it in favour of a broad and more thorough investigation of all relevant aspects of the federal tax

system.[68] It was agreed that Perry would draw up a "research outline that would direct the thinking of the commission and its staff to the underlying principles of taxation and provide more permanent answers to issues then current."[69] This set the Commission on its way to becoming one of the great research-oriented commissions, like the Rowell-Sirois Commission. Academic tax specialists would therefore tend to be as influential as tax practitioners and business interests, which would not have been the case had the Commission confined itself to public hearings and briefs.

As the Royal Commission on Government Organization (Glassco Commission) was winding down its operations, its Secretary, Michael Pitfield was assigned to the Commission on at least a temporary basis, as were some of the administrative staff. One of the initial tasks of the staff was to prepare for the first meeting of the Commission, October 10th to 12th, during which the Commissioners met privately with senior Government officials to discuss their terms of reference.

Before meeting with these officials, however, the Commissioners took advantage of the presence among their number of a former taxation official from the Department of Finance, J. Harvey Perry. He suggested that the most important economic areas to be researched by the Commission were the total burden of taxation by all levels of government and the effect of taxation on economic growth. Among the tax structure questions requiring the research services of chartered accountants and lawyers, he mentioned the problem of corporate distributions (surplus-stripping), the dividend tax credit, the

taxation of co-operatives, and "the desirability of capital gains taxes."[70] In the field of international taxation, in addition to the economic question of the influence of taxation on the balance of payments, there were the problems relating to withholding taxes, the role of foreign subsidiaries, the tax burden on export industries, the possible remission of sales taxes on exports, and foreign experience regarding estate taxes and real estate taxes.

Perry gave his fellow Commissioners a more detailed list of over sixty "Suggested Studies" for the Commission, which he had drawn up at Carter's request.[71] It touched on most of the current controversial subjects in Canadian taxation and many others as well. Under "General Income Tax Studies", Perry had listed:

- basic principles governing progressive tax rates
- double taxation - or not; methods of integration
- capital gains
- price level changes
- time period problems (arbitrary annual division of flow of receipts and related outlays; "one time" expenditures)
- deductibility of expenses (T.F.)[72]

The "T.F." after the final item meant that that the study had either been completed or was under way with the support of the Canadian Tax Foundation. Several of the studies in Perry's list were so marked, and it was understood at the time that the Foundation studies would resolve all or most of the "big" issues.[73] Under "Personal Income Tax", of eight items, the first two dealt with the "scope of the tax" and the "rate of progression of [the] schedule.[74]

Meeting informally with the Commissioners on October 11th, Gear McEntyre, Deputy Minister of National Revenue, Taxation, emphasized the importance to his Department of the self-assessment system. This depended on the use of clear, concise forms, understandable to the taxpayers, which, in turn depended on "simple and clear tax laws".[75]

The Commissioners then met with Claude Isbister, Associate Deputy Minister of Finance (Taxation),[76] In recommending "how best to tax", Isbister said that the Commission should take into account all levels of government, but make recommendations only for the Federal authorities. He agreed with Carter, that all economic relations with the provinces would have to be examined, and recommended that the Commission consult first with the provincial Vice-Treasurers and then with their respective Ministers. The possibility of obtaining advice from foreign specialists was discussed and Isbister suggested some sources and procedures to facilitate the process.

The discussion then turned to the use of incentives and tax cuts to stimulate economic growth and as tools of stabilization policy. Isbister explained that any increase in government expenditures or increase in the deficit was "impossible" at that time, and that any easing in monetary policy would provoke another dollar crisis. The Government was therefore limited to economic policies which did not involve an increase in expenditures. By a process of elimination therefore, "tax rearrangements" were considered to be "the most desireable" alternative. Isbister referred specifically to the graduated rates of personal income tax, which the Department would

like to lower. The high progressive rates, had, at one time been regarded as "the alternative to Communism", and more recently as a built-in stabilizer to moderate swings in the business cycle. He believed, however, that it was no longer effective in serving the latter purpose. He also pointed to the "natural arguments" that high progressive rates inhibit work incentives.[77]

Meeting with the Commissioners on October 12th, D.S. Thorson, the Deputy Minister of Justice, asked the Commission to look into the problem of Ministerial discretion versus elaborate codification of taxing statutes. The 1948 Income Tax Act had removed most of the discretionary clauses, but had resulted in an "endless process of definition and redefinition" and the proliferation of specific sections resulting from pressures put on the Minister of Finance. He complained that there was no philosophy behind this conglomeration of provisions:

> It is merely a series of set rules with a number of disadvantages: seeking to provide for detailed individual fact situations, preventing the courts from enunciating a series of principles, leading to the development of innumerable schemes and gimmicks, developing a general philosophy ...[among] the taxpayers that there is a way out for everyone. These are very unhappy developments and the complexities that they have introduced into the law may be graphically illustrated by the fact that the Act has, in less than 15 years, tripled in size. Another example, would be section 12 (1)a. of the Income Tax Act concerning disallowance of

> capital expenditures, which has itself become nothing but a series of exceptions. The erosive effects of this tendency on the revenue can be imagined. The result is that a restatement of the law is drastically required.[78]

Mr. Thorson also thought the Commission should look into the process of budget-making and presentation. The tradition of budget secrecy was especially open to question. He urged the Commission to look into ways in which "the public could be given a greater voice" and the time allowed for pre-budget submissions increased. However reforms of the process should not include "wide-open public hearings", since they would likely be dominated by pressure groups, preventing a truly fair hearing.[79]

The first public indication that the Commissioners had given a broad interpretation to their terms of reference was given in November by Perry, speaking on behalf of Carter, who was prevented by illness from addressing the Annual Conference of the Canadian Tax Foundation. Said Commissioner Perry:

> Briefly, the Commission considers that it has been enjoined to study the economic effects and the structural deficiencies of the whole of the federal tax structure and make recommendations for changes designed to remedy these faults. We interpret the federal tax structure to include all levies imposed under the Income Tax Act and the Estate Tax Act, the Excise Tax Act and the Excise Act. For obvious reasons we consider the tariff as being of concern to us only as it is of relevance to a tax coming directly within our terms of reference. For reasons equally obvious we do not feel that we have been authorized to make recommendations on provincial and municipal taxes. We have also concluded that federal-provincial tax arrangements as such do not

> come within our ambit. Notwithstanding these limitations it is self-apparent that a study of federal taxation cannot be carried on in a vacuum isolated from the taxes levied by the other governments in Canada, and we will be taking them into account as a conditioning factor in several connections. These few limitations are almost the only vaguely defined horizons we can detect in our terms of reference. Otherwise the field appears to be wide open for any aspects of any federal tax.[80]

As Perry clearly implied, the accent was going to be on study, one of unprecedented scope and considerable depth.

In an effort to secure provincial co-operation, Carter met with representatives of the provincial governments and invited each to set up commissions analagous to the federal Royal Commission. In a January, 1963, meeting in Toronto between senior representatives of the federal Commission and what was to officially become the Ontario Committee on Taxation, Carter presented the provincial representatives an aide memoire briefly outlining his Commission's interpretation of its terms of reference, and concluded with a statement of how the Commission perceived its mandate in relation to the provinces:

> When considering the burden upon taxpayers, we are instructed to take into account the jurisdictions and practices of the provinces and municipalities. We are gravely concerned with the burden of this charge and must take steps towards co-operation with the provinces.
>
> Canadian taxes fall under three groupings: ...[those based on income, on business transactions, and on non-business transactions].
>
> Provinces are interested in all three groups of taxes both as to effects and tax structure. It is of the greatest importance to seek agreement from provincial committees in those (recommendations) which have common

application.[81]

This interpretation of the terms of reference committed the federal Commission to attempt some form of co-ordination with provincial bodies in order to achieve harmony in areas of "common application", and in which the aide memoire explicitly included all three types of taxation. Had the federal Commission proceeded in this fashion, it would have accepted significant constraints on its freedom to make recommendations.

Three days after the meeting with the Ontario Committee, the memorandum proposing inter-Commission co-operation was revised to avoid any reference to co-ordination in terms of recommendations. Henceforth the emphasis would be on basic research:

> The Federal Commission would be happy to extend its fullest co-operation to Provincial Committees or Commissions to be set up and to make available to them a substantial amount of statistical information as well as some of the basic research studies which it is going to undertake.[82]

The Ontario Committee was quite eager to co-operate with the federal Commission, and, if possible, to make use of some of the latter's research. Carter was receptive to this idea, while emphasizing that the information would have to be kept strictly confidential and not be made available to governments. As with the federal commissioners and staff, the oath of secrecy would have to be taken, and even then, material received in confidence by one Commission could not be turned over to another. Also, the federal Commission could not assure its provincial counterparts that they

could necessarily exchange information concerning recommendations.[83]

The fear that confidential information shared with provincial authorities might be passed on to politicians or leaked to the press, thereby fueling federal-provincial controversy, was a major constraint on co-operation with the provinces. It was primarily for this reason that Carter tried to persuade the provincial governments to set up truly independent commissions which could co-operate with the federal Commission without representing the views of, or prematurely providing information to their respective governments.[84]

By the spring of 1963, following Carter's tour of provincial capitals with Marc Lalonde, who had been retained by the Commission, most provinces had either set up bodies of some description to co-operate to varying degrees with the federal Commission, or indicated their intentions to do so. In most cases, the commissions were to study and recommend reforms in their respective provincial tax systems. However, the response ranged from that of eager co-operation from Ontario and Saskatchewan, the latter setting up a commission for the sole purpose of assisting the federal Commission, to outright refusal of Nova Scotia and British Columbia to set up any special body to study provincial taxation and co-operate with the federal Commission. Newfoundland did not even reply to the Commission's correspondence.[85]

The heterogeneous nature of the provincial response made organized co-operation difficult, though a number of joint meetings of

sub-committees of Commissioners did take place, and basic data and some economic research was exchanged. From the point of view of the development of the comprehensive income concept of the Carter Report, this poorly-developed state of co-operation with the provinces was a fortunate occurrence, though it did not bode well for the eventual acceptance of recommendations based on the concept.

The Organization of the Commission

A research project of the size envisaged by Perry's list of sixty suggested studies required skilful management to ensure that the research was organized in such a way as to avoid duplication while taking full advantage of existing knowledge. The questions to be investigated had to be defined so that researchers competent in their respective fields could complete the various tasks effectively and on time. To get the job done the Commission would have to locate and attract people with the appropriate knowledge and experience to conduct this research. Organizing the task, assembling the staff, and directing their work would demand someone with knowledge in at least some of the areas to be investigated, ideas and contacts sufficient to attract the skilled people to do the research, and managerial abilities adequate to the task of orchestrating a large research organization toward a common purpose. This would be the job of the Director of Research.

Among the candidates surveyed by Carter and Perry was Douglas G.

Hartle, a member of the Department of Political Economy at the University of Toronto. Hartle had done his under-graduate work at Carleton University in Economics, Political Science and History. He then went to Duke University for his M.A., studying under the supervision of Joseph J. Spengler, known for his work on the history of economic thought and demography. He returned to Canada to work for the Department of Labour, while continuing to work on his doctorate, then went to the Department of Political Economy at the University of Toronto, first as a research assistant to Professor William Hood, then as a lecturer. He came to the attention of Carter when Professor Vincent Bladen, the head of the Department, recommended him for the post of Director of Research.[86]

The Commissioners appointed John K. Stewart, a successful corporate tax lawyer and senior partner of the Toronto firm of Fraser, Beatty, Stewart, as their Legal Advisor. Stewart and Carter were personal friends and had often collaborated professionally.[87] Had it not been for the need to restrict the proportion of Toronto people on the Commission, Carter would have insisted that Stewart be appointed as a Commissioner.[88]

In order to assist the Director of Research in recruiting staff, and in co-ordinating work among the three major disciplines and professions, Carter hired William F. Martin, C.A., of Vancouver.[89] Carter had met Martin while doing some accounting work for the British Columbia Power Corporation, Martin's previous employer.

As interim Secretary to the Royal Commission, Michael Pitfield was initially its senior official, reporting directly to Carter. He was responsible for carrying out the Commissioners' first decisions, including their plans and announcements regarding briefs and public hearings, establishing a rudimentary plan of organization, submitting requests to Privy Council and Treasury Board for budgetary allocations and authority to hire staff, the hiring of administrative staff, and supervising all the initial housekeeping chores involved in setting up the Commission.

Pitfield set about his duties with eager efficiency. Even before the Research Director had reported to work, Pitfield had already addressed three memoranda to him, containing suggestions regarding organization and procedures of the research side of the Commission's staff.[90] Pitfield's plan for the Commission, on the basis of which he had submitted a proposed budget to Privy Council and Treasury Board a week earlier, envisaged a lean permanent research staff under the Director of Research, aided by a number of project officers at various levels of responsibility, hired on a per diem contract basis. The latter contract researchers would collectively make up the "External research programme", working as self-contained project teams on separate, well-defined projects determined by the Director of Research. Horizontal communication would be provided by "research teams" of appropriate individuals from the relevant projects.

The "internal" staff would consist of the Director of Research, an Assistant for administrative and research purposes, and five "Research

Supervisors", each supervising three to five of the projects in the External research programme, and working under a single "Research Co-ordinator". Pitfield saw the latter position, which should be filled by a French Canadian, "as a sort of Assistant Research Director" and proposed Pierre Trudeau, who would "unlock all sorts of avenues in French Canada if we can get him..." and of whom he had already spoken with the Chairman, as a possible candidate.[91]

Hartle, however, preferred to organize the research programme around full-time staff researchers rather than rely on the "external" orientation recommended by Pitfield. Both Carter's and Perry's list of suggested studies had implied an integration with, or reliance upon the studies then under way by the Queen's Tax Study Group which was funded by the Canadian Tax Foundation, and also on other Foundation studies. While acknowledging the direct relevance of the Queen's studies for the Commission's work, Hartle recommended that, since the Commission would have no control over their content or dates of completion, it should therefore undertake separate studies using its own staff.[92]

Hartle proposed that all of the Commission's research "be under the direction and control of the Director of Research" who would "be responsible to the Chairman of the Commission".[93] These studies would be grouped into five divisions, each with a supervisor and staff:

A. Studies of the control of the aggregate level of economic activity through fiscal policy and related measures.

B. Studies of the effects of government revenues and expenditures on the allocation of resources ...

C. Studies of the effects of government revenues and expenditures on the distribution of income, and on welfare generally.

D. Studies of the constitutional and administrative problems of the tax system.

E. Studies of the legal and accounting problems of the tax system (excluding constitutional problems).[94]

To relate the work of these divisions to the major types of taxes, Hartle proposed five committees to collect and organize the research pertaining to each type of tax and report on the respective alternatives and their implications.

Hartle also told Carter that he would prepare a working paper setting out the objectives of the tax system to guide the work of the Commission, and eventually to "provide a basis for chapter or chapters in the final report".[95] Hartle saw the initial task as one of comprehending those objectives and analyzing how the tax system satisfied them, therefore indicating "...the crucial areas in the tax system which require appraisal".

Carter accepted, at least in principle, Hartle's ideas on the research programme.[96] Having failed to convince Hartle of the advantages of the "external" research organization, Pitfield wrote to Carter two days later, outlining his own ideas concerning the organization and responsibilities of the offices of Secretary and Director of Research.[97] He pointed out, that Gordon Bennett, a high-ranking civil servant at the "Senior Officer 2" level, was being

considered for the post. If one was to judge from the Research Director's Program of Studies, Pitfield argued, there would be little responsibility for a person of this seniority, beyond "a vicarious representation of the Research Director in procedural and non-substantive or formal relationships with participants..." and other administrative matters.[98]

Pitfield suggested that the problem related to the conception of the Program of Studies outlined by the Director of Research:

> If you examine the excellent Program of Studies suggested by the Research Director, you will notice that it covers every aspect of the inquiry, both practical (viz.: technical) and theoretical (viz.: economic). The question is whether or not this broad and extensive - indeed, massive - programme is to be directed by one person, as seems to be implied by the Research Director, or by two persons - one concerned with the technical and the other with the economic.[99]

He placed the Commission within the historical context of earlier Royal Commissions, in which the emphasis on research, and with it the role of the research director, had tended to grow. With Hartle's proposed mode of operation, the evolution would take the "...final step, where the inquiry is the Research programme and the Research programme is the Research Director."[100]

Pitfield proposed two alternative modes of organization of the offices of Secretary and Research Director. The first, put forth as the logical consequence of accepting Hartle's conception of the Programme of Studies, was that the two offices be combined. An Assistant Secretary, responsible to the Research Director, would take

care of administrative matters, leaving the Program of Studies unchanged. If this alternative were selected, however, there would have to be "a substantial reallocation of duties", in order to free the Research Director from any research activities, the better to handle his supervisory responsibilities.

Pitfield's second alternative divided the research tasks between the Research Director and Secretary:

> Accepting the suggested Programme of studies, the areas designated as A, B and C - being substantially economic - can be allocated to the supervision of the Research Director, and the areas designated as D and E - being substantially technical - can be allocated to the Secretary. The cross-fertilization by horizontal research teams would continue as suggested, but the Research Director and Secretary would each be responsible for the direction of the inquiry, the briefing of participants, the analysis of submissions, the preparation of project reports, their discussion with the Commissioners, and the preparation of chapter drafts insofar as his area is concerned. In this concept, the Research Director would, in fact, be doing research within the Commission, with a largely permanent staff, and the Secretary would be taking account of those technical areas in which it is considered that by far the larger proportion of the participants will be interested and which, at the moment, it is intended to examine largely outside of the Commission through the co-operation of participants, in external projects and public hearings. The Secretary would, of course, remain in charge of the administration of the Commission so that it may be said that the purpose of the division is to leave the Research Director in charge of the economic expertise, while the Secretary is left with the direction of practical aspects of the inquiry.[101]

The effect of Pitfield's second proposal would have been to give the Secretary control of the research on tax structure and administrative law, as well as the overall administration of the

Commission, while the Research Director would be more or less restricted to supervision of the economic studies.

Pitfield then provided a capsule assessment of each alternative. The first, while assuring a clear and unified line of responsibility for all activities of the Commission, would be, in effect, returning to the traditional system of a single secretary, in an era when modern research techniques made the task too large for one person. The second, while dividing the Commission staff in two and leaving the Chairman to function as "co-ordinator and general manager", was Pitfield's preferred alternative:

> It does reduce the responsibilities of each to workable limits, however, and at the same time ensures that, by giving place to both points of view, the technical and economic aspects of the inquiry are brought before the Commissioners without the one submerging the other beforehand. In addition, to the degree that the Research Director and the Secretary function as a partnership, the burden of managerial responsibility is reduced.[102]

Hartle responded by defending his conception of a larger role for the Director of Research than that envisaged by Pitfield.[103] Arguing against the latter's proposed splitting of the research programme, Hartle wrote to the Chairman that this did not correspond to his own recollection of his initial conversation with Carter and Perry in Toronto. Hartle had understood that he would be responsible for all research while the Secretary would handle administration, and his "Suggested Programme of Studies" had reflected this understanding.[104] Examining Pitfield's two alternative modes of

organization, Hartle immediately rejected the combination of the two offices of Secretary and Research Director: "The job is too big for one man if the research position is going to have any research content at all."[105] Nor was the second alternative a wise choice in his view. Splitting the research programme along the lines suggested by Pitfield would prevent the close integration of the economic and tax structure aspects, which was essential if the research programme were to "...make a substantial contribution to the work of the Commission".[106]

Hartle suggested making the Secretary primarily responsible for administration and the Research Director responsible for research. In dealing with participants, the research staff would go through the Secretary, which would require that the former clearly and promptly define their needs for information, and the latter accurately communicate these to the participants. In hiring staff, the Research Director should confer with the Secretary on the particulars, and no appointments would be made to the research staff without prior consultation with the Research Director. The research group would prepare drafts of those chapters of the Report requested by the Commissioners, and the Secretary "could draft some chapters on the basis of data and information obtained in part from members of the research group."[107]

From the subsequent operation of the Commission, it is clear that Hartle's view prevailed. At the Second Meeting of the Commission Hartle presented his initial Report to the Commissioners, in which he

said that he had adopted a policy of encouraging internal rather than external research. This would, he explained, enable the Commission to control the research more effectively and ensure that the work was well integrated. External research would be considered only as a last resort. Carter supported Hartle's proposals, adding that, in addition to the advantages of greater control over the research, there would likely be substantial time and money savings. Without further discussion, this change in research policy was formally approved.[108]

Pitfield's status as Secretary had been, apparently by his choice, a provisional one from the beginning of the Commission. Hartle's full control over the research programme would have removed any doubts he may have had about leaving the Commission. To replace Pitfield as Secretary, Carter was able to have seconded Gordon L. Bennett, then Acting Assistant Deputy Minister of National Revenue, Customs and Excise. Bennett was duly appointed permanent Secretary at the Commission's January meeting.[109] At the same meeting, the Commission appointed Pitfield on a part-time basis as Assistant to the Chairman in order to assist in the hand-over of the duties of Secretary, and to provide for "a continuity in the development of inter-governmental relations."[110]

Pitfield's new office of "Supervisor, Area "E", included overseeing relations with the provincial governments and commissions and research in matters of administrative law, with Hartle exercising overall direction.[111] This consolidated Hartle's control over all research conducted by, or contracted for, the Commission, and allowed

him to keep sufficiently informed of developments relating to the provinces to ensure that no future commitments were undertaken without his knowledge. It was understood that communication with the provincial commissions and committees would be kept to a minimum consistent with the Chairman's commitments.[112]

Hartle's increased control over Commission-provincial relations had an indirect effect on the Commission's recommendations concerning income taxation, in that alternative outcomes arising from commitments which might have been undertaken with provincial bodies were avoided. The provinces, which competed with the federal government for tax revenues while sharing in the revenue from the same income tax base, would have wanted to participate in the re-definition of that base. Hartle's action to limit the federal Commission's formal ties with the provincial commissions removed one potential constraint on the decision-making processes of the Commission.

Practical considerations played an important part in Hartle's attitude toward the provincial commissions. He felt that the Commission had enough work to do without getting too closely involved with their provincial counterparts. More significantly, the latter tended to be interested in reforms of a limited and pragmatic nature, rather than the more rational and comprehensive review which Hartle envisaged for the Federal Commission. Also, had the provincial commissions been privy to such considerations during the formative stages there was a possibility of the Royal Commission "being scooped" before their Report was released.[113]

The implications of Hartle's firm control over all Commission research are less speculative. Had his role in directing the tax structure studies been restricted, it is likely that the Commission's Report would have been quite different. As the discussion in the following chapter will demonstrate, the Commission's adoption of the comprehensive income concept owed a great deal to the ideas, influence and tenacity of its Director of Research.

Formation of the Research Staff:

Well before the lines of authority within the Commission had been settled, Hartle had been elaborating his ideas on the role of the Research Staff. Early in November, Hartle proposed to Carter that a list be drawn up of "key participants", including those groups and individuals who would effectively articulate the opposing points of view and provide the most useful information. Such a list ought to include individuals representative of different geographic areas, sources and sizes of income, occupations, as well as provincial and municipal governments, government departments and organizations, trade and industry associations, professional organizations, foreign investors, and experts in fields relevant to the enquiry.[114] The research staff would prepare confidential memoranda to each, indicating what the Commission would like to see discussed in their submissions.[115]

When the submissions were received, the research staff would prepare memoranda for the Commissioners, pointing out areas of the submissions which required more information or clarification, and also bring to the Commissioners' attention points of contradiction, both within a particular submission, and with other submissions. The research staff could also brief the Commissioners prior to hearings with "expert" witnesses.[116]

These activities would be only one phase of the research staff's duties, the other being directed toward the special studies and production of the Commission's report. Hartle envisaged the research staff co-operating in the preparation of an outline of the Report, and later, in the writing of draft chapters specified by the Commissioners.[117] It would clearly be difficult to accomplish all these tasks without a sizeable "in-house" research staff,[118] and retaining suitably qualified researchers within the constraints imposed by Treasury Board proved to be a formidable challenge in itself.

The Commission's terms of reference allowed it to hire staff of its own choosing, subject to approval by Treasury Board. As an administrative matter this authority rested with Carter, the Commission's Chairman.[119] Carter delegated hiring of the research staff to Hartle, while the actual administrative procedures were handled by the Commission's secretary, who dealt with Treasury Board officials regarding resources and approval for specific appointments.

On the tax structure side, Hartle received a good deal of assistance in locating qualified researchers. Carter and Perry had extensive contacts among tax professionals and with the Canadian Tax Foundation.[120] In January, 1963, William Martin, Co-ordinator of the Tax Structure side of the Research Staff, visited the Tax Foundation's Director, Ronald Robertson, to discuss organization and staffing.[121] Carter also wrote to "a select group of lawyers, chartered accountants, and Deans of Graduate Schools in search of bright young professionals".[122] Commissioner Beauvais offered to assist in locating suitable French-Canadian candidates.[123] John Stewart also recommended a number of people to Carter and Hartle for the legal research.[124] While interim Secretary, Michael Pitfield recommended a number of candidates to both Carter and Hartle.[125]

Several members were recruited from government departments. Following Carter's initial conversations with the Deputy Ministers of Finance, Justice, and of the two branches of National Revenue, it was agreed that an officer from each would be seconded to the Commission.[126]

Hartle looked for candidates among university faculty members for economists. Unfortunately, the beginning of the life of the Commission was out of [illegible] with the annual rhythm of the universities and the faculty membe[illegible]ld not be free from their teaching responsibilities until [illegible].[127] An additional complication he faced was the relative scarcity of highly qualified economists in Canada, aggravated by competition from other Royal Commissions (notably the

Porter Commission on Banking), the prospect of a "National Planning Board" (which came into the world as the Economic Council of Canada), the rapid expansion of university enrolment, the increasing demand from international agencies, and "the growing enthusiasm of business for the services of economists".[128] The resulting delays in retaining staff meant that the Research Staff could not perform its advisory role to the Commission during the public hearings in the spring of 1963, and also that the Commission's schedule, calling for the final Report to be completed in two years, would be very difficult to keep.[129]

In spite of his efforts to find qualified Canadians for the economic research positions, Hartle had to report to the Commissioners in January of his intention to hire five or six non-Canadians out of a total of about 40 or 50 researchers. While describing the market for Canadian economists as "tight", he complained that the supply of French-Canadian economists was practically non-existent: of at least fifteen persons approached, only about four had shown any interest in working for the Commission.[130]

The salary levels allowed by Treasury Board made it difficult to attract experienced scholars.[131] The procedures were also discouraging: the Commission was not granted an authorized "Establishment" of a certain number of staff, but instead had to submit a request to Treasury Board to hire and pay each prospective staff member, making negotiation with candidates awkward and occasionally embarrassing.[132] In conversations with "Ministers and

senior officials" Carter had defended the Commission's right to make appointments on its own authority, and argued that Treasury Board was limited to questions of remuneration only, and "only for cause shown".[133] Consistent with Carter's assertions, the Commission adopted as policy its practice of making appointments to the Research Staff "independent of Treasury Board authority for their remuneration..." confident that "while Treasury Board approval of remuneration might be difficult to obtain, it would eventually be forthcoming."[134]

In January, Hartle asked Carter's approval to make an application to Treasury Board to hire six non-Canadian economists, specialists in areas for which Hartle had not been able to find or attract suitable Canadians. The list of their interests included the quantitative analysis of the behavior of business enterprise, industry tax incentives, public debt management, government expenditures and revenue requirements, the effects of taxation on work incentives, the problems of expenditure taxation, and the effects of taxation on personal saving. Of these six non-Canadians, four were British subjects, and four were then teaching at universities in the United States.[135]

Carter approved Hartle's request the following day, and Pitfield informed Carter that he would "take up the whole matter with Bryce on Friday."[136] Privy Council and Treasury Board approval was slow to come, however. By February, a number of appointments recommended to the Privy Council the previous month were causing the Commission some

embarrassment: all had been offered employment, but the Commission could not say when they should report for work, as it was not certain that they could actually be hired. In some cases, Canadians appointed to research positions had already reported for work, made arrangements to move their families, and incurred expenses, yet they could not receive any remuneration because their salary and allowances had not been approved by Treasury Board Minute, the latter requiring a recommendation from the Privy Council.[137] The Commission also intended to invite two distinguished tax specialists, Carl Shoup from the United States, and Mr. Van Hoorn of the Netherlands, to appear before the Commission in Ottawa, but approval for payment of their expenses was also being held up. This was also the case for the services of Pierre Trudeau and Marc Lalonde, the latter having already accompanied Carter on his visits to the provincial capitals.[138]

Trying to find out the reasons for the delay, Bennett concluded from his conversations with Bryce and David Watters, Assistant Secretary to the Treasury Board, that the two officials were not trying to obstruct the Commission's appointments, and that "there must therefore be a matter of high policy involved."[139] Bryce, while "fully conscious of the urgency" of the cases, "...had to discuss it with the Prime Minister." Watters said there was nothing more he could do to speed up approval of the appointments and that they were on the agenda for Cabinet consideration the following Wednesday morning.[140] Bennett recommended to Carter that the Commission get assurances that such delays would not plague future appointments, make sure that there was no "high policy reason" why non-residents could

not be hired when absolutely necessary, and secure Privy Council and Treasury Board approval of the Commission's programme, budget and establishment.[141]

However, there was little progress on these points. Early in March, Hartle received a telephone call from Robert Bryce, asking why the Commission wanted to hire an American economist to conduct one of the research projects. He was referring to one of the research staff appointees from the previous January which had not yet been approved by Privy Council and Treasury Board. Hartle's reply appeared to satisfy him, at least in that particular case. However, during the course of a tense conversation, Bryce offered some hints concerning the delays in getting approval of the appointments to the research staff:

> 1. The Commission is hiring far too large a staff. Why don't I [Hartle], together with Commissioner Perry, do the work.
>
> 2. Taking so many "outsiders" or "experts" on to the staff will discredit the Commissioner's [sic] report in his eyes, and in the eyes of other senior government men.
>
> 3. The technical subject matter in the terms of reference is not as great, or important, as I believe it to be.
>
> 4. There has never been a Commission like ours before - and never again![142]

Hartle reported the conversation to Carter, to make him aware "of the skepticism and hostility which the Commission faces in dealing with senior civil servants".[143] He suggested a meeting between the Commission, Privy Council and Treasury Board to settle the matter of appointments once and for all, or "the politicians should direct the

civil servants not to interfere."[144] Carter took over the altercation from this point and convinced Bryce and Treasury Board officials of the Commission's determination to hire expert staff.[145] By the time of the Commission's Third Meeting, in April, 1963, the delays in getting Treasury Board approval had finally been overcome.[146]

The salary levels permitted by Treasury Board were not nearly high enough to buy the services of the experienced and expensive tax professionals employed by business firms or in private practice. As it was, Hartle could not offer sufficient financial incentives to attract many senior people from the universities, let alone those from the lucrative private sector. The university scholars hired by the Commission were usually junior faculty members, many recently out of graduate school, some having interrupted work on their dissertations to join the Commission. Unable to attract the "big names" of the academic world to the research staff, the Commission nevertheless managed to benefit from their advice through their publications and by inviting specialists to testify at special hearings of the Commission and to provide confidential appraisals of some of the special studies and draft chapters.

By May, the Commission's research establishment numbered about 87 persons, including part-time advisers and consultants, as well as staff hired only for the summer.[147] Of these, 21 made up the staff of the Tax Structure Studies, including its Co-ordinator, William Martin, and four supervisors: D.B. Fields, Personal Income Tax; W.E.

Goodlet, Business Income Taxes; H.D. McGurran, Taxation in Other Countries; and Howard Perrigo, Commodity Taxes.[148] There were 35 persons working on the Economic Studies, including its Co-ordinator, Duncan McDougall, and five part-time advisors. Within this division, there were six supervisors: W. Irwin Gillespie, Distribution Studies; Stephan F. Kaliski, Foreign Sector; Yehuda Kotowitz, Business Sector; William Peters, Personal Sector; Robert M. Will, Stability Studies; and Thomas A. Wilson, Econometric Analysis. "Intergovernmental Relations and Legal Problems" was listed as a separate division, with Michael Pitfield, (who was by then Attaché to the Governor General) as its part-time Supervisor.[149]

In addition to being responsible for the conduct of specific research projects as set out in the research programme, each Supervisor undertook to answer technical questions from the Commissioners in his subject area, and to provide research support to the Commissioners in their examination of submissions and their questioning of participants at the public hearings.

Hartle and the Co-ordinators were expected to ensure that problems and alternatives were not considered in isolation from one another by refining the research outline and schedule, overseeing the various project proposals, and commenting on successive drafts of the studies and draft chapters of the Report. In order to bring together people from different projects and disciplines to discuss specific tax problems, Hartle established five "inter-area" or "topic committees": Corporate Tax, Business Tax, Personal Tax, Commodity Tax, and the

International Transactions Tax Committee.[150] During the early stages of the research the staff found that there was little to co-ordinate, and formal committee meetings often gave way to ad hoc lunch meetings.

As Hartle explained to the Commissioners at their meeting in January, 1963, the research group would serve three purposes:

> (a) assist [the] Commission in the conduct of hearings by comment on submissions, preparation of background material, memoranda to participants, provision of advisors.
>
> (b) make objective studies of issues involved in [the] terms of reference and indicate the alternative courses of action.
>
> (c) assist in the preparation of the final report.[151]

Hartle stressed the need to integrate the research activities with the outline of the final Report and urged the Commissioners to agree on such an outline as soon as possible. The chapters of the Report would be drafted from the research studies, both chapters and studies being presented to the Commissioners to decide on the alternatives presented.[152] These studies were to include descriptions of the existing system and assessments of its effects on the economy. The emphasis was to be on "the quantitative and factual rather than the hypothetical", and a range of alternatives with pros and cons, but no conclusions, would be submitted to the Commissioners.[153]

Conclusion

By the Spring of 1963, the Royal Commission had acquired the trappings of an established governmental organization. It had offices (in the Metcalfe Building at 88 Metcalfe Street, at Slater), a somewhat uncertain budget, and a staff of more than a hundred, with the lines of authority defined. In terms of its substantive mandate, the Commission had made a preliminary interpretation of its terms of reference, announced its intentions, and made plans for public hearings, and outlined a programme for research to be conducted largely by its own in-house staff of tax specialists. It had also made the first contacts with federal Departments and with all but one of the provincial governments.

Although not a word of its final Report had yet been drafted, nearly all of the actors who would define its content had joined the Commission. Unknown to those involved, decisions crucial to the Commission's ultimate adoption of the comprehensive income concept had already been taken. The Commission was not about to undertake a superficial "patch-up job", but had retained a large staff of professional researchers to get to the bottom of every significant tax problem and to probe exhaustively for solutions. While many organizations had been invited to submit briefs and to appear as witnesses, their arguments and evidence would be closely scrutinized by the Commission's Counsel, the three tax specialists among the

Commissioners, and by the Research Staff. The lines of authority within the Commission had been established, with Hartle exercising control over all research activities and directing them primarily toward supporting studies and eventually toward draft chapters of the final Report.

Notes to Chapter III

1. Globe and Mail, Toronto, April 16, 1962, p. 7.
2. Telephone interview with Donald M. Fleming, May 19, 1982.
3. Globe and Mail, April 9, 1962.
4. Globe and Mail, April 4, 1962, p. 13; April 9, 1962, p. 15
5. Globe and Mail, April 11, 1962, p. 6.
6. Ibid.
7. Ibid.
8. Ibid.
9. Ibid.
10. Fleming interview; Globe and Mail, May 7, 1962, p. 6. The paper noted that Manitoba had also publicly called for an enquiry.
11. Dalgleish to Frost, June 10, 1958, Ontario Archives, RG3 Leslie M. Frost, Riding and Personal Correspondence, Box 58, "Diefenbaker, Rt. Hon. John, 1958". I am indebted to Professor Roger Graham, Department of History, Queen's University for bringing this correspondence to my attention.
12. Ibid.
13. "Robarts Suggests Taxation Study", Hamilton Spectator, Aug. 30, 1962; Public Archives of Canada, RG 33/65, Vol. 151, p. 17. (Further citations to the Commission papers will be given as: PAC, RG 33/65, followed by the volume number, file name and page.) The newspaper story quotes Robarts' remarks to delegates to the Ontario Municipal Association Convention: "When I became prime minister, I advocated a thorough review of our entire Canadian Tax structure... I felt then and feel now that it is something that is urgently needed to put our financial house in order." Shortly before his death, however, Mr. Robarts denied having anything to do with influencing Mr. Diefenbaker to appoint the Commission. Letter to the author, June 25, 1982.
14. Globe and Mail, April 18, 1962., p. 7.
15. Ibid.
16. Globe and Mail, April 18, 1962, p. 6.
17. Donald Fleming believes this to be the primary reason for the Prime Minister's announcement of his intention to appoint the Commission. Fleming interview.
18. Globe and Mail, May 3, 1962, p. 1; Bothwell et. al., Canadian Politics Since 1945, (Toronto: University of Toronto Press, 1981), pp. 224-228.
19. Globe and Mail, May 3, 1962, p. 1.
20. Ibid.
21. Globe and Mail, May 4, 1962, p. 6.
22. Fleming interview, May 19, 1962.
23. Isbister, interview by telephone, June 15, 1982.
24. Diefenbaker, One Canada, Vol. 2, The Years of Achievement, 1956-1962, Vol. 2, pp. 120-121; Granatstein, The Ottawa men: the civil service mandarins, 1935-1972, (Toronto: Oxford University Press, 1982), pp. 266, 270.
25. Globe and Mail, May 7, 1962, p. 6.
26. Interview with Robert Bryce, Jan. 14, 1983, and with Douglas G. Hartle, Nov. 4, 1981.

Vol. 105; Vol. 109, Minutes of the Second Meeting..., "Pitfield" file.

130. "Minutes of the Second Meeting ...January 31st, 1962", RG 33/65, Vol. 109, "Pitfield" file; Hartle to Carter, Jan. 21, 1963, "Carter" file.
131. Hartle interview.
132. Hartle to Carter, "appointment of Non-Canadians to the Research Staff", Jan. 21, 1963, RG 33/65, Vol. 105, "Carter" file.
133. "Minutes of the Second Meeting ...January 31st, 1963", RG 33/65, Vol.109, "Pitfield" file.
134. Ibid.
135. "Appointment of Non-Canadians to the Research Staff", Jan. 22, 1963, RG 33/65, Vol. 105, "Carter" file.
136. Ibid.
137. Bennett to Carter, cc. Hartle, Feb. 18, 1963, RG 33/65, Vol. 105, "Carter" file.
138. Ibid.
139. Bennett to Carter, Feb. 15, 1963, "Outstanding Appointments", RG33/65, Vol. 105, "Memoranda -- Secretary" file.
140. Bennett to Carter, Feb. 18, 1963, RG 33/65, Vol. 105, "Carter" file.
141. Ibid.
142. Hartle to Carter, Mar. 6, 1963, "Appointments", RG 33/65, Vol. 105, "Carter" file. Hartle's emphasis.
143. Ibid.
144. Ibid.
145. Douglas Hartle recalls Carter battling with Bryce over this issue, and hearing a great deal of yelling by Carter into the telephone. Correspondence with the author, Dec. 30, 1984. Mr. Bryce does not recall exactly what happened, but explains it as "a normal bureaucratic problem", attributable to the high rates of remuneration and the appointments of non-residents. Bryce interview.
146. Minutes of the Third Meeting of Commissioners... April 18, 1963, RG 33/65, Vol. 112, "Meeting, April 18, 1963, Minutes" file.
147. "RCT Establishment as of May 8 and May 20, 1963", RG 33/65, Vol. 104, "Canadian Tax Foundation -- Ronald Robertson" file.
148. Ibid., Goodlet later became Associate Co-ordinator for Tax Structure Studies.
149. Ibid.
150. RG 33/65, Vol. 104, "Business Tax Committee" file, July 8, 1963, Sept. 9, 1963.
151. "Outline of Report of Research Director to Commission", Jan. 31, 1963, RG 33/65, Vol. 105, "Commissioners" file.
152. Ibid.; "Minutes of the Second Meeting ...January 31st, 1963", RG 33/65, Vol. 109, "Pitfield" file.
153. "Informal Meeting of Commissioners ...July 15-19, 1963", RG 33/65, Vol. 105, "Commissioners" file.

27. PAC, RG 33/65, Vol. 151.
28. Financial Post (Toronto) Oct. 7, 1961, p. 17; cited in R.L. Gardner, The Politics of Reform: Class Interests and Tax Reform in Canada, 1960-1971 (Unpublished doctoral dissertation, McMaster University, 1974), p. 226.
29. Directory of Directors (Toronto: The Financial Post, 1960).
30. Diefenbaker, Memoirs, Vol. 2, pp. 120-121; For an account of the events surrounding the devaluation, see: Robert Bothwell et. al., Canada since 1945, pp. 224-228.
31. Penticton Herald, Aug. 24, 1962, PAC, RG 33/65, Vol. 151.
32. Documentary evidence is not yet available, as Privy Council papers are subject to the thirty-year rule. The Diefenbaker papers are only now being catalogued, and will not likely be accessible, even on a restricted basis, for about five years.
33. Globe and Mail, Sept. 1, 1962, RG 33/65, Vol. 151, p. 23. Donald Fleming, however denies that the devaluation and exchange crises, the surplus-stripping problem, or even the capital gains litigation had any influence on the appointment, "except indirectly". Unless one understands as "direct" only those factors explicitly discussed around the Cabinet table, Fleming's recollection is difficult to accept in the view of the evidence to the contrary presented in this and the preceding chapter.
34. Fleming, telephone conversation, May 19, 1982.
35. Robert Bryce believes that Carter must have had such links, otherwise he would not have been appointed. Bryce interview.
36. Don McGillvray, in the Winnipeg Tribune (and 16 other Southam newspapers), Aug. 27, 1962; PAC, RG 33/65, Vol. 151.
37. Directory of Directors (Toronto: The Financial Post, 1960). This item had been scratched out of the capsule biography in the Commission's files. PAC, RG 33/65, Vol. 143, File 85-1, "Organization Generally".
38. Fleming interview.
39. Perry interview, Oct. 23, 1981; Perry, Background of Current Fiscal Problems, (Toronto, Canadian Tax Foundation, Tax Paper No. 68, 1982), p. 82.
40. Taxes, Tariffs and Subsidies, and Taxation in Canada, (Toronto: University of Toronto Press, 3rd. rev. ed., 1961).
41. Bryce interview.
42. PAC, RG 33/65, Vol. 143, File 85-1, "Organization Generally"; Directory of Directors, (1960).
43. PAC, RG 33/65, Vol. 109; and Vol. 143, File 85-1, "Organization Generally". The Royal Commission biographical sketch describes her as having been "active in the financial management of several large organizations for a number of years" and "believed to be the first woman from Manitoba to sit on a federal Royal Commission...."
44. PAC, RG33/65, Vol. 143, File 85-1 "Organization generally"
45. Report of the Royal Commission on Taxation, Vol. I (Ottawa: Queen's Printer, 1966), pp. v-vi.
46. Interview with Claude Isbister, July 17, 1982; Hartle interview.
47. Isbister interview; Bryce interview.
48. Isbister, Fleming and Bryce interviews. Mr. Bryce denied that this was done to "keep the Commission out of the Department's hair for as long as possible", as was suggested by a senior

member of the Commission staff.

49. Byrce interview.
50. Isbister, Bryce interviews.
51. Bryce interview.
52. Mr. Stanfield also made his views known directly to Carter. "Meeting with the Hon. Robert Stanfield... Feb. 5, 1963", PAC, RG33/65, Vol. 109, "Provincial" file.
53. Background of Current Fiscal Problems, pp. 78-79.
54. Ibid.
55. PAC, RG 33/65, Vol. 151.
56. Richard Jackson, "Tax Inquiry Will Listen To Anybody", The Journal (Ottawa, August 28, 1962); PAC, RG 33/65, Vol. 151.
57. La Presse (Montreal, Aug. 28, 1962); PAC, RG 33/65, Vol. 151.
58. The Journal (Ottawa) Aug. 28, 1962; PAC, RG 33/65, Vol. 151.
59. PAC, RG 33/65, Vol. 151.
60. Ibid.
61. "Looking into Business -- Robin Hood Image of Tax Collectors Out of Focus", PAC, RG 33/65, Vol. 151, Sept. 3, 1962.
62. The Telegram, (Toronto, Aug. 29, 1962); PAC, RG 33/65, Vol. 151.
63. Goudreault, Amédée. "A Ottawa, Vos Taxes (1)", Le Soleil (Québec, Aug. 29, 1962); PAC, RG33/65, Vol. 151.
64. PAC, RG 33/65, Vol. 151.
65. PAC, RG 33/65, Vol. 151, Aug. 30, 1962.
66. "Probable Major Studies to be Conducted by Staff and Professional Assistants", Memorandum to File, "Commissioner Carter on Terms of Reference...", Sept. 4, 1962, PAC, RG33/65, Vol. 112, "Terms of Reference/ Chairman's Copies" file.
67. Ibid.
68. Perry, "Anatomy of a Tax System", Proceedings of the Twentieth Tax Conference, (Toronto: Canadian Tax Foundation, 1968), p. 12; Perry interview, Oct. 23, 1981; Perry, Background of Current Fiscal Problems, p. 83.
69. Ibid.
70. "Commissioner Perry on Terms of Reference", Memorandum to File, Vol. 112, "Terms of Reference/ Chairman's Copies" file.
71. Perry, Background of Current Fiscal Problems, p. 83.
72. 'Commissioner Perry on Terms of Reference', Vol. 112.
73. Hartle, in correspondence with the author, Dec. 30, 1982.
74. "Commissioner Perry on Terms of Reference", Memorandum to File, Vol. 112, "Terms of Reference/ Chairman's Copies" file.
75. "Mr. McEntyre on Terms of Reference", Memorandum to File, (n.d.), and McEntyre to Carter, Oct. 12, 1962, Vol. 112, "Terms of Reference/ Chairman's Copies" file.
76. "Mr. Isbister on Terms of Reference", Memorandum to File, (n.d.), and Isbister to Carter, Oct. 11, 1962, PAC, RG 33/65, Vol. 112, "Terms of Reference/ Chairman's Copies" file.
77. Ibid.
78. "Mr. Thorson on Terms of Reference", Memorandum to File, (n.d.), Vol. 112, "Terms of Reference/ Chairman's Copies" file.
79. Ibid., "Terms of Reference/ Chairman's Copies" file.
80. Pitfield to Hartle, re; Perry's remarks to CTF Conference, attached, Nov. 26, 1962, RG 33/65, Vol. 109, "Pitfield" file.

81. "Meeting between certain representatives of the Federal Royal Commission on Taxation and certain members of the Ontario Royal Commission on Taxation, Toronto... January 4, 1963", [sic] attached: "Royal Commission on Taxation", RG 33/65, Vol. 109, "Provincial" file. The notes were taken by Marc Lalonde. Also present were: Carter, Harvey Perry, J.L. Stewart, Douglas Hartle, Lance Smith, Eric Hardy, B. Stapeldes. The parentheses surrounding the word "recommendations" was added afterword in ballpoint.
82. "Notes Concerning Relations with the Provincial Commissions and Committees on Taxation", January 7, 1963, RG 33/65, Vol. 112, "Dominion - Provincial Relations/ Chairman's Copies" file.
83. "Notes Concerning Relations With The Provincial Commissions and Commissions and Committees On Taxation", January 7, 1963, RG 33/65, Vol. 143, File 95-1, "Dominion-Provincial Relations Generally".
84. Hartle to Carter, May 8, 1963, "Re: Release of Staff Studies to Provincial Tax Commissions", RG 33/65, Vol. 143, File 95-1, "Dominion-Provincial Relations Generally".
85. "Minutes of the Second Meeting... January 31st, 1963", Vol. 109, "Pitfield" file. The Minutes record Carter as stating that "two matters were of the essence: first, the creation of official bodies within the provinces to whom the Commission might correspond, and second, that these bodies should be independent of the governments to which they were responsible.
86. Hartle interview.
87. Ibid.
88. Interview with Stanley E. Edwards, Q.C., November 22, 1982.
89. Pitfield to Research Director, Oct. 17, 1962, RG 33/65, Vol. 109, "Pitfield" file.
90. Pitfield to The Research Director, No. 3, Oct. 17, 1962, PAC, RG 33/65, Vol. 109, "Pitfield" file.
91. Ibid. Hartle, in correspondence with the author, Dec. 30, 1982, said that he was unaware of this particular proposal.
92. Hartle to Carter, c. Oct. 23, 1962, "Suggested Programme of Studies", (Research Memorandum to the Chairman, No. 1.), RG 33/65, Vol. 112, "Research Memorandum to Chairman" file.
93. Ibid.
94. Ibid.
95. Ibid.
96. Pitfield to Hartle, Nov. 1, 1962, RG 33/65, Vol. 109, "Pitfield" file.
97. Pitfield to Carter, cc. Perry, Hartle, No. 5, Nov. 2, 1962, RG 33/65, Vol. 105, "Carter" file.
98. Ibid.
99. Ibid.
100. Ibid.
101. Ibid.
102. Ibid.
103. Hartle to Carter, Nov. 9, 1962, Vol. 105, "Carter" file, and Vol. 112, "Research Memorandum to Chairman" file.
104. Ibid.
105. Ibid.

106. Ibid.
107. Ibid.
108. Minutes of Second Meeting..., Vol. 109, "Pitfield" file; "Outline of Report of Research Director to Commission", Jan. 31 1963, Vol. 105, "Commissioners" file.
109. Ibid.
110. Ibid.
111. Pitfield to Hartle, June 3, 1963, Vol. 109, "Pitfield" file. He was instrumental in getting Hartle to visit Pierre Trudeau and his colleagues at l'Institut de droit publique at l'Université de Montréal to sign a contract for a major study on administrative aspects of taxation. This was one of several pieces of "external" research which more closely resembled Pitfield's conception of the research programme than it did Hartle's.
112. See: Carter to Hartle, May 7, 1963; Hartle to Carter, May 8, 1963, "Re: Release of Staff Studies to Provincial Commissions"; and Carter to Hartle, "Re: Release of Staff Studies to Provincial Tax Commissions", Vol. 143, File 95-1, "Dominion-Provincial Relations Generally".
113. Hartle, in correspondence with the author, Dec. 30, 1982.
114. Hartle to Carter, Nov. 9, 1962, "Research Memorandum to the Chairman, No. 3", RG 33/65, Vol. 112, "Research Memorandum to Chairman" file.
115. Ibid.
116. Ibid.
117. Ibid.
118. Hartle to Carter, Nov. 5, 1962, Vol. 105, "Carter" file.
119. "Minutes of the Second Meeting ...January 31st, 1963", RG 33/65, Vol. 109, "Pitfield" file.
120. Carter to Pitfield, and Hartle, Dec. 5, 1962, re candidates for staff, RG 33/65, Vol. 105, "Carter" file; Stewart to Carter, Vol. 105, "Carter" file.
121. Ibid.
122. "Minutes of the Second Meeting ...January 31st, 1963", RG 33/65, Vol. 109, "Pitfield" file.
123. Ibid.
124. Stewart to Carter, Jan. 31, 1963, RG 33/65, Vol. 105, "Carter" file.
125. Pitfield to Perry to Hartle, n.d., "Economic Personnel -- Royal Commission on Taxation", Vol. 109, "Perry" file; Pitfield to Hartle, #11, Dec. 11, 1962, RG 33/65, Vol. 109, "Pitfield" file.
126. Carter to Hartle, cc. Pitfield and Wm. Martin, "Man from National Revenue (Customs and Excise)", and "Man from Department of Finance", both Jan. 16, 1963, RG 33/65, Vol. 109, "Pitfield" file.
127. Hartle to Carter, Nov. 9, 1962, RG 33/65, Vol. 105, "Carter" file.
128. Hartle to Carter, Nov. 9, 1962, and Jan. 22, 1963, "Appointment of Non-Canadians to the Research Staff", RG 33/65 Vol. 105, "Carter" file.
129. Hartle to Carter, cc. Perry, Secretary, Nov. 9, 1962, RG 33/65, Vol. 105; Vol. 109, Minutes of the Second Meeting..., "Pitfield"

Vol. 105; Vol. 109, Minutes of the Second Meeting..., "Pitfield" file.

130. "Minutes of the Second Meeting ...January 31st, 1962", RG 33/65, Vol. 109, "Pitfield" file; Hartle to Carter, Jan. 21, 1963, "Carter" file.
131. Hartle interview.
132. Hartle to Carter, "appointment of Non-Canadians to the Research Staff", Jan. 21, 1963, RG 33/65, Vol. 105, "Carter" file.
133. "Minutes of the Second Meeting ...January 31st, 1963", RG 33/65, Vol.109, "Pitfield" file.
134. Ibid.
135. "Appointment of Non-Canadians to the Research Staff", Jan. 22, 1963, RG 33/65, Vol. 105, "Carter" file.
136. Ibid.
137. Bennett to Carter, cc. Hartle, Feb. 18, 1963, RG 33/65, Vol. 105, "Carter" file.
138. Ibid.
139. Bennett to Carter, Feb. 15, 1963, "Outstanding Appointments", RG33/65, Vol. 105, "Memoranda -- Secretary" file.
140. Bennett to Carter, Feb. 18, 1963, RG 33/65, Vol. 105, "Carter" file.
141. Ibid.
142. Hartle to Carter, Mar. 6, 1963, "Appointments", RG 33/65, Vol. 105, "Carter" file. Hartle's emphasis.
143. Ibid.
144. Ibid.
145. Douglas Hartle recalls Carter battling with Bryce over this issue, and hearing a great deal of yelling by Carter into the telephone. Correspondence with the author, Dec. 30, 1984. Mr. Bryce does not recall exactly what happened, but explains it as "a normal bureaucratic problem", attributable to the high rates of remuneration and the appointments of non-residents. Bryce interview.
146. Minutes of the Third Meeting of Commissioners... April 18, 1963, RG 33/65, Vol. 112, "Meeting, April 18, 1963, Minutes" file.
147. "RCT Establishment as of May 8 and May 20, 1963", RG 33/65, Vol. 104, "Canadian Tax Foundation -- Ronald Robertson" file.
148. Ibid., Goodlet later became Associate Co-ordinator for Tax Structure Studies.
149. Ibid.
150. RG 33/65, Vol. 104, "Business Tax Committee" file, July 8, 1963, Sept. 9, 1963.
151. "Outline of Report of Research Director to Commission", Jan. 31, 1963, RG 33/65, Vol. 105, "Commissioners" file.
152. Ibid.; "Minutes of the Second Meeting ...January 31st, 1963", RG 33/65, Vol. 109, "Pitfield" file.
153. "Informal Meeting of Commissioners ...July 15-19, 1963", RG 33/65, Vol. 105, "Commissioners" file.

Chapter IV: Searching for the Carter Philosophy

Not long after the release of the Commission's Report, the phrase "a buck is a buck" was what most people would have been able to associate in their minds with the name "Carter". These words are a capsule summary of the comprehensive income concept, that all economic gain, regardless of the source, should be included in income, and treated alike for tax purposes. However, this principle did not find its way into the Report in a simple fashion. The composition of the Commission, the authority of the tax professionals, the influence of most business interests, and the tendency for politicians to discount the future beyond the next election more heavily than do royal commissioners, all made the odds very long against it.

The odds had been shortened considerably, however, by the decision of the Commissioners to make their enquiry more of a research effort than a polling of interested parties, and by the strategic placing of an economist, Douglas Hartle, at the head of the Commission's research staff. An exploration of the events taking place within the Commission during its four-year life span will show how the comprehensive income concept found its way into the Report.

Development of the Research Outline

The very extensive research conducted by its staff and by others

on contract was the most important influence on the direction of the Commissioners' thinking and on the contents of their Report. This research effort, by providing the analysis and supporting the recommendations set out in the Report, was intended to both inform and persuade government representatives and the various publics concerned. The research activities of the Royal Commission were key elements of the logical phases of problem definition, the search for alternatives, and the evaluation of alternatives leading to the Commission's adoption of the comprehensive income concept.

The general outline for the research programme developed out of a list of problems with the existing tax system drawn up by Carter immediately after his appointment, and Harvey Perry's prospectus of tax studies[1] which were modified and incorporated into a "Suggested Programme of Studies" by Hartle.[2] By the end of January of 1963, Hartle had drawn up a tentative outline which divided up the Report into four parts:

I, The Canadian Tax System: The Issues;
II, The Effects of the Tax System on the Economy;
III, Problems of the Tax Structure; and
IV, Summary of Conclusions and Recommendations.[3]

Hartle anticipated the addition of a fifth section on "Intergovernmental Tax Arrangements", with the various economic and tax structure studies being included in appendices.

The first part, on "The Canadian Tax System: The Issues" included

five sections which were to cover the background of the Commission; a description of the existing tax system, the economic effects of the existing system; the objectives of the tax system; and the issues before the Commission. The objectives of the tax system were stated as:

(a) The financing of government expenditures
(b) Stability and growth
(c) Equity
(d) Administrative efficiency
  (i) the problems of definition of objectives
  (ii) assessing the degree of achievement
  (iii) conflicts among competing objectives.[4]

Contrary to what ultimately appeared in the published Report, there was no indication that equity should be ranked higher than the other objectives. Hartle listed it third, and, unlike "stability" and "growth", "equity" was not noted under the heading, "The issues before the Commission". The prominence of "stability and growth" among the objectives reflected Hartle's Keynesian perspective on the importance and feasibility of using fiscal policy for moderating economic fluctuations.

In July, 1963, Hartle and his staff presented the research plans to a meeting of the Commissioners, at which the statement of the objectives of the taxation system and the draft outline of the final Report were approved. It was understood that the research Supervisors would be drafting at least some sections of the Report for consideration of the Commissioners.[5]

The research staff had produced detailed prospecti on about 94

separate research projects, including 42 economic studies, 49 relating to tax structure, and 3 of administrative, legal and constitutional aspects.[6] Hartle's research outline occupied 28 typed pages and listed hundreds of items to be investigated. Among "Exploratory and Comparative Studies" was:

> A study of capital gains taxation:
> (i) The relationship of capital gains to income;
> (ii) Empirical estimates of some of the consequences of the introduction of capital gains taxation.[7]

In Part III, "Broad Economic Problems", was a project on the distribution of the tax burden:

> A. Construction of estimates of the tax burden by income.
>
> B. An analysis of various tax changes that would alter the distribution of tax payments.[8]

Under Part IV, Personal Taxation, the "Concept of Income" was to receive detailed scrutiny, including:

> F. Concept of "Adventure in the Nature of Trade".
>
> G. Present principles of taxability induced from legislation and jurisprudence.
>
> H. A discussion of inconsistencies in the above.
>
> I. An attempt at an objective definition of the concept.
>
> J. A discussion of rental income and a review of existing provisions and jurisprudence.
>
> K. An examination of the possibilities of extending the tax base.
>
> L. A review of present exclusions, particularly regarding:

(i) capital gains;
(ii) computed income; [sic]
(iii) accrued income;
(iv) income exempt by statute
(v) various forms of non-cash income

M. A consideration of the equity problems which an extension of the tax base might raise.[9]

The final chapter of Part IV was devoted to "Capital Gains Tax": its implications, transitional and administrative problems, various rates, the effect of inflation and deflation, treatment of capital losses, the effect on corporate distributions, the possibility of averaging gains over a number of years, treatment of non-residents, short-term versus long-term gains, effects on supply of capital, business activity and investment, and the experience of other countries, particularly the U.S. and the U.K.[10] While no conclusions were suggested, the outlines of some of the most influential studies, notably those by Conway and Smith on capital gains, are evident. The comprehensive income concept, while not spelled out in the Outline, was slated for a close examination.

Public Hearings and Reception of Briefs

Shortly after it had been set up, the Commission advertised widely in both general newspapers and trade papers that it would welcome briefs on topics relevant to its mandate from all interested groups or individuals. The reception of submissions was followed up by public hearings at which these people discussed their submissions with the Commissioners and the Commission's Legal Advisor, John Stewart, or the

assistant legal counsel, Jack Coyne.

The research staff prepared confidential requests to a list of important organizations, outlining the issues which the Commission would like to see addressed in their submissions and requesting specific information.[11] They then analyzed the submissions, preparing detailed memoranda, or "blue sheets", in order to assist the Commissioners and the Legal Advisor at the public hearings. During most of the hearings, a member of the research staff took notes.

The Commission also sought the advice of recognized specialists in taxation and public finance. Professors Ash Wheatcroft of the London School of Economics, Carl Shoup of Columbia University, John Due of the University of Illinois (a specialist on sales taxes), and J. Van Hoorn, Director of the International Bureau of Fiscal Documentation in Amsterdam, were invited to attend special hearings at the Commission's expense to answer questions put to them by the Commissioners and senior staff. Shoup was a member of the Committee for the Harmonization of Taxes of the European Economic Community (or Neimark Committee), set up by the European Economic Community to study the effect of prevailing European tax systems on competition, and to propose methods of eliminating tax barriers.[12] Occasionally private meetings were arranged at which the Commissioners, Hartle, Stewart, and some members of the research staff, could discuss tax theories and problems with outstanding specialists.[13]

The Commissioners decided to develop their respective capabilities

in particular areas and, where appropriate, to deal individually with corresponding groups of participants.[14] Commissioner Walls specialized in commodity taxation, and even visited Australia to investigate its tax system. However, at most of the hearings, Carter took the lead in directing questions to the participants. Having carefully examined the briefs beforehand as well as the appropriate memoranda prepared by the research staff, the Commissioners and their legal counsel were able to engage the witnesses in a close and often critical cross-examination. Some groups appearing before the Commissioners found themselves agreeing to re-examine their proposals, to furnish the Commission with more specific information supporting their statements, or to consider new alternatives suggested by the Commissioners or their Counsel. Carter was not impressed by the presentation of the Canadian Labour Congress, whose spokesmen, he felt, had not been well prepared. Carter disagreed with the CLC's espousal of "ability-to-pay" as:

> ...the only acceptable principle to achieve equity. I felt that they did not sustain this point at all well. Whereas it is certainly a most important matter, it did not stand up as being the only principle.[15]

Nor was Carter impressed by the CLC's argument against the dividend tax credit, and he "reserved judgement on the merits of a capital gains tax until more [was] learned about its productivity and cost."[16]

Carter was equally skeptical of the presentation by the Canadian Manufacturers' Association, particularly their proposal to deduct

dividends from corporate profits before computing taxable income, to the extent that the corporation was owned by Canadians. In considering the perennial business complaint of "double taxation" of corporate income, Carter noted:

> At the present time, the dividend tax credit, it seems to me, offers a "middle road" compromise and I doubt if one can do better.[17]

At this early stage in the Commission's work it is clear that Carter himself was not a believer in what came to be called the "Carter income concept": that an equitable tax system had to be consistently based on the "ability-to-pay" principle, and therefore, that all economic gain, regardless of source, should be taxed at the same rate.

Following each day's hearing, Carter dictated his impressions of the discussion, with requests to the research staff to look into the questions raised, and then sent the recording to the Commission's offices in Ottawa.[18] The hearings sometimes proved to be of use to the research staff, as when witnesses would agree in the hearings to provide the Commission with data pertinent to its investigations. Occasionally, arguments were raised in the hearings or submissions which the staff felt it had to take the time and trouble to put to rest, or at least to bring the "fallacies" in the arguments to the Commissioners' attention.[19]

Compared to their visibility and the amount of effort lavished upon them by participants and Commission staff, the submissions and

public hearings made only a minor contribution to the Commission's Report. However, the Commission did not regard them simply as "window dressing" to convince taxpayers that their problems were being taken seriously. This is evident from the Commission's analysis of the briefs, the careful questioning of witnesses at the hearings, and (when requested by Carter or one of the Commissioners) the follow-up work carried out by the research staff. Commissioners and staff, however, came to regard most as special pleading by particular interests, rather than public-spirited suggestions for improving the tax system.[20] These interests had some influence upon the thinking of the Commission: in enabling it to anticipate the objections of particular groups to its proposals, The Report contains several references to views expressed in submissions and hearings, sometimes followed by systematic refutations or references to one or another of the Commission's studies which showed the particular point not to be valid.

Conversations with American Tax Reformers

Much of the public discussion preceding the appointment of the Royal Commission had focussed upon the tax systems of the United States and Europe. It had been widely claimed that business in some of those countries enjoyed tax advantages denied to Canadian business, and that Canada should adopt some of the tax incentive measures enacted in those countries in order for Canadian goods to compete successfully in foreign and domestic markets. It was also claimed

that a lower level of personal taxation in the United States was drawing badly-needed skilled and professional labour away from Canada -- the infamous "brain drain". The same argument was applied to investment capital, which was even more mobile than skilled labour. Moreover, President Kennedy's programme for substantial tax cuts to stimulate the economy were given wide publicity in Canada, stimulating demands from Canadian taxpayers for similar reductions. In the hope that the Royal Commission could learn some lessons from the more advanced American tax reform debate, Carter spent a week in Washington and New York in March, 1963, for discussions with twenty-six U.S. Government officials, politicians, and public finance specialists.[21]

One of the first persons Carter met on his visit to Washington was Harvey Brazer, Director of the Office of Tax Analysis in the Department of the Treasury, who gave Carter a copy of his monograph, A Program of Federal Tax Revision.[22] A proponent of the comprehensive income concept of taxation, Brazer favoured a tax on capital gains from considerations of equity, which led them to a discussion of the incidence of the tax burden, that is, who actually bears the burden of a tax. Brazer referred Carter to Richard Musgrave's work on the incidence of the corporate income tax.[23]

Carter discussed President Kennedy's tax reform proposals with Stanley S. Surrey, Assistant Secretary of the Department of the Treasury. Among the issues raised were the proposed changes in the taxation of capital gains, including the taxation of capital gains on succession. This was intended to eliminate the possibility previously

available to investors of avoiding capital gains tax by holding on to securities rather than selling them. Carter learned from Herbert Stein, Director of Research for the Committee for Economic Development that the Committee approved of the proposal by the Department of the Treasury to tax capital gains on succession.[24] Taxing capital gains on succession was expected to greatly reduce the "lock-in" effect, or immobility of investment capital, which, it was argued, impaired the efficiency of capital markets.[25] This, in fact, became the solution adopted by the Commission to the "realization problem" surrounding taxation of capital gains.

In his discussion with James W. Knowles, Executive Director of the Joint Economic Committee of Congress, Carter learned something of the background of the tax reform debate in the U.S. Knowles was involved in the 1955, 1956 and 1959 Congressional committee hearings from which emerged the tax reform proposals put forward by President Kennedy. He referred Carter to the published record of the 1955 and 1956 hearings, Federal Tax Policy for Economic Growth and Stability, and also, "The Federal Revenue System - Facts and Problems", which was the result of a November, 1955 symposium of about a hundred panelists. Knowles told him that "these people represented the start of the debate on taxation", which was brought up to date by the Joint Economic Committee hearings of 1959.[26]

Mortimer Caplan, Commissioner of Internal Revenue, answered Carter's questions regarding the relationship of lawyers and accountants to his Department, and about the administration of the tax

on capital gains.[27]

Joseph Pechman, Director of Economic Studies of the National Bureau of Economic Research, and author of several books on tax policy,[28] discussed American tax reform issues with Carter. Both Pechman and Norman Turé, an officer of the Bureau, felt that capital gains should be taxed at the same rate as other income, but that the general rate should be lowered. They warned that the current taxation of capital gains at preferential rates was "hideously complicated, particularly in all the fringe areas, such as the matching of costs and income in the case of securities, and the question of evaluation of gifts in kind, such as securities."[29] Pechman and Turé were working under the auspices of the Brookings Institution in preparation for an autumn conference on tax incentives and offered their assistance to the Commission. Before leaving, he picked up a number of publications, including Essays in Federal Taxation by Herbert Stein and Joseph A. Pechman; Some Fiscal Implications of Metropolitanism by Harvey Brazer; Income Consumption and Property as a Bases of Taxation by Richard Good.[30]

Walter C. Sauer, Executive Vice-President of the Export-Import Bank of Washington, told Carter that he, like many others, felt that the effect of taxes on the economy had been exaggerated. Sauer found more persuasive John Kenneth Galbraith's views[31] that, instead of cutting taxes, social expenditures should be increased. Carter was sufficiently impressed by these ideas to suggest to Hartle that they invite Professor Galbraith to testify before the Commission.[32]

At the Columbia Law School in New York, Henry Bloch, author of a three volume work on Israeli taxation, referred Carter to other specialists and publications, and suggested that the Commission take a careful look at the British experience as set forth in their Royal Commission reports.[33]

Perhaps as a result of Carter's conversation with Joseph Pechman, Hartle received an invitation from Professor John F. Due, on behalf of the National Bureau of Economic Research and the Brookings Institution, to attend the tax conference in Washington in October which Pechman had mentioned to Carter.[34] Papers, on the theme, "the role of direct and indirect taxes in the Federal tax structure", were presented by, among others, Arnold Harberger of the University of Chicago, and Richard Musgrave of Princeton University, both supporters of the Haig-Simons, or comprehensive income, concept of taxation. It was in reading Richard Musgrave's textbook on public finance that Hartle came to favour the idea which became the basic philosophy of the Commission's Report.[35] The conference was intended to be an exclusive gathering of the top American public finance specialists.[36] Among those present were some of the people Carter had met in Washington: Harvey Brazer, Walter Heller, James Knowles, Joseph Pechman, Herbert Stein, Stanley Surrey and Norman Turé. John F. Due and Carl S. Shoup (both of whom later appeared before the Commission), Roy Blough, Harold Somers and Dan Throop Smith also participated at the conference. During the course of its work, the Commission came into contact with the ideas generated by these tax specialists, either

in person, through their publications, or through the publications of others. With the exception of Smith, they were supporters, to varying degrees, of the comprehensive income concept.

The Ideologies of Taxation

Even when on vacation in Bermuda, during June of 1963, Carter continued to read books on taxation and sent frequent letters to Hartle, requesting information and reporting on items he had read. One of his more remarkable letters was an enthusiastic report on a book he had just read and enjoyed immensely:

> Eisenstein is a Washington tax lawyer "who is attempting to be a scholar" but in my view he most successfully fills a scholar's rôle. He is a champion debunker and his views are most critical of many valued organizations including the American Bar Association. He concludes that income tax has become a thing of "shreds and patches". Our vaunted progression is largely a myth. He secures support for this last statement in a study by Richard Musgrave referred to on Page 56 of "Ideologies", "The Incidence of the Tax Structure and Its Effects on Consumption".[37]

Carter said he would have his copy mailed to Hartle, but that the Commission Librarian should secure some more copies for Commissioners and the staff.[38] Hartle had just read Eisenstein's book himself and concurred with Carter's enthusiastic assessment and ordered an additional copy for circulation among the Commissioners and the Legal Advisor.[39]

Debate on tax policy, according to Eisenstein, is based upon the

attempts of various groups in society to ensure that their own taxes are minimized at the expense of other groups. Where possible this is done through a monopoly of political power, enabling the ruling groups to levy taxes in accordance with their own preferences, and justify this by equating their own well-being with the welfare of the community.[40] In democracies, where the people of modest means outnumber the wealthy, "reasons have to be given" to persuade the many to accept tax burdens on themselves. Hence the development of ideologies of taxation to obscure the economic interests of particular groups by recourse to "some immutable principle that rises majestically above partisan preferences."[41]

Eisenstein focuses on three such ideologies: "ability", "barriers and deterrents", and "equity". The ideology of ability is an attempt to make the rich pay more taxes by putting forward the principle that the tax burden should be distributed according to one's ability to pay, which is held to vary directly with income or wealth. The ideology of ability therefore argues for progressive taxation.

The ideology of barriers and deterrents replies that progressive taxes will discourage the enterprise of the wealthy and those who would like to become wealthy, thereby undermining the very process of the creation of wealth in society. The people who create wealth in our society must be encouraged with tax incentives, for the good of everyone else. Eisenstein summarizes the "barriers and deterrents" philosophy with the epigram: "...if less is taken from those who have more, more will be given to those who have less."[42]

The third ideology, that of "equity" is based on the concept of equality before the law, one which all tax ideologists claim to hold in great respect. Its main principle, "those who are similarly situated should be similarly taxed", is sufficiently flexible to be used by partisans of the first two ideologies.[43] The "ability-to-pay" ideologists interpret it in terms of arithmetic equality of income: "a ~~dollar~~ is a dollar and ...capital gains are like any other dollars", an apt epigram to sum up the comprehensive income concept.[44] The adherents of "barriers and deterrents" argue that the "similarities" could refer to any number of categories, not simply income: in interpreting "equity", one must first determine what are the "relevant circumstances" which justify similar or different treatment.[45] They use "equity" selectively to extend the tax incentives which they first supported with the "barriers and deterrents" ideology. Once granted, one good tax incentive deserves another: "All who are similarly situated are equally entitled to pay less."[46] Hence, "equity" becomes "the fair distribution of dispensations."[47] Since most of these dispensations are for the wealthy, the so-called progressive taxation system is but a myth, and the income tax system, a "thing of shreds and patches".[48]

Each ideology of taxation has its ideologists. Eisenstein divides them into three categories, based on their motivations: "those who believe through interest" (such as the the Chamber of Commerce, and the American Mining Congress), "those who believe through compensation" (such as lawyers, economists and retired congressmen),

and "those who believe through principle" (largely "statesmen, scholars, and professional experts").[49]

As a tax lawyer, Eisenstein considers himself something of an expert on that species of ideologist: "A lawyer is not a competent tax adviser unless he is well acquainted with the highways and byways of avoidance." Tax avoidance is a "thriving business" and tax lawyers are "the retained rationalizers that keep that business going."[50] Likewise for the professional organizations of lawyers: the American Bar Association and its Tax Section, and the American Law Institute. The Bar Association is in the "barriers and deterrents" camp, to the extent of proposing a constitutional amendment to deprive Congress of the right to impose estate and gift taxes, and to inhibit it from levying an income tax above 25 per cent. He quotes "an authoritative member of the Association" who said that any opposition to their amendment "can be explained only by an adherence to the taxation philosophy of Karl Marx."[51] The Association's Tax Section, which cultivates an image of non-partisanship and altruism, pursues a "notion of the public interest" which "prominently includes the effective advocacy of lucrative dispensations for groups in the upper brackets and a silent acquiescence in those obtained by others."[52]

Since most Congressmen are incapable of understanding the Internal Revenue Code, a "...vote on a tax bill... is an act of faith." Even when they do understand, they are the willing cogs in the machinery of pressure group politics. It would not aid the cause of the "ability-to-pay" ideologists therefore, to urge that Congress retain

more expert advisers, for the "primary purpose of a Congressional expert is to justify what Congressmen would otherwise desire or prefer."[53] The only answer, "to elect Congressmen who do not feel that they have to yield" to pressures for tax concessions, requires that voters be informed on tax policy, something neither political party is anxious to do.[54]

Although he chides the adherents of "ability-to-pay" for their logical inconsistency in allowing some concessions against their own doctrine, and for compromising with the "barriers and deterrents" school when there is no logical or empirical reason for doing so, Eisenstein is clearly more sympathetic with their position then with the gloomy doctrine of "barriers and deterrents". The former are simply inconsistent and too timid in applying their own principles, somewhat less than candid concerning their views on the distribution of wealth, and often naive in their understanding of the political system. The partisans of "ability-to-pay" would have the "many" on their side if they took the trouble to instruct the majority of voters in recognizing their own interests. Eisenstein was confident that the voters were capable of understanding the policy issues involved. If anything, the problem may well be "that they might understand too well."[55]

In reading Eisenstein's book, Carter encountered references to many of the tax specialists he had met while in Washington. In addition to Richard Musgrave, Eisenstein included in the "ability-to-pay" school Carl Shoup, Stanley Surrey, Walter Heller,

Joseph Pechman, and the Joint Economic Committee of the 86th Congress and referred to the same documents published by the Joint Economic Committee which James Knowles had recommended to Carter. One of the "ability-to-pay" advocates whom Eisenstein credited for his candor in acknowledging that one of the purposes of progressive taxation was to mitigate disparities in wealth, was Henry Simons. Other partisans of "ability-to-pay" cited by Eisenstein are Roy Blough, author of The Federal Taxing Process, and Challis Hall, author of a critical study on "Corporate Surplus Accumulations" for the Joint Economic Committee, both participants at the Washington tax conference attended by Hartle the previous October. Prominent among the adherents of "barriers and deterrents" was Dan Throop Smith, whose argument for tax incentives Eisenstein wittily annihilates.

One can appreciate Carter's enthusiasm for Eisenstein's book. It did what its author challenged the "ability-to-pay" school to do: present the most important tax policy issue, that of the distribution of the tax burden, in a way that the layman could understand. It dealt in a critical way with the same issues which motivated the appointment in Canada of the Royal Commission on Taxation, and Carter probably suspected that many of Eisenstein's devastating critiques of American law, behavior and institutions could, with minimal alteration, be applied north of the border. Eisenstein showed Carter that the pursuit of a truly equitable tax system by systematically closing loopholes could be both an honourable and a popular cause.[56] He presented both an inspiration and a challenge to the Commission to cut through the rhetoric of pressure politics, and to

address the majority of citizens who ought to be interested in tax policy.

Learning from the Europeans

In September of 1963, Carter travelled to Stockholm, Brussels, The Hague, Rome, Paris, Bonn and London to talk with European tax specialists and officials. Joined by Harvey Perry in Paris, Bonn and London, he sent back reports to the Commission staff summarizing the discussions of thirty-odd interviews with a total of at least sixty individuals.[57] With the exception of Great Britain, taxation was not a subject of great controversy in Europe at that time. There was some debate over the merits of going from sales taxes to the value added tax, however, and a good portion of Carter and Perry's discussions were devoted to this question. They also looked into the structure of direct taxes in each country, and also the administration of their taxation systems.

In Sweden, in addition to a sales tax, Carter took note of a capital gains tax on moveable property held for less than five years, on immovable property held less than ten years, a net worth tax on individual capital in excess of 80,000 kroner, and succession duties as well. Carter had the impression that only about 5,000 individuals were subject to the net worth tax, and that few estates were large enough to exceed the exemption of the succession duties.[58]

In Belgium, Carter learned that only business capital gains were taxed, with a complicated system of preferences depending on the holding period, and an exemption for gains which were reinvested or "rolled over". He noted that the Finance Minister took "some pride in the fact that capital gains [for individuals] are not taxed." The main reasons for this, Carter observed, were the difficulty of obtaining information on transactions, which were kept secret by brokers and banks, and also a "fear of driving out capital."[59] At a luncheon meeting with two senior representatives of the Federation of Industries, Carter learned that Belgian industrialists preferred to deal informally with tax policy matters, meeting with government officials and deputy ministers almost weekly.[60] Carter, however, was not very impressed with the Belgian taxation system, except with its complexity.[61]

In the Netherlands, Carter noted that "extremely high taxes on their middle classes..." was "causing some flight of wealthy persons to Switzerland...".[62] Government assurances had been given that the rates would be lowered. The Netherlands did not have a capital gains tax, though gains on the "controlling interest" portion were subject to tax on the grounds that these share-owners could regulate the accumulation of corporate income. There was also had a modest net worth tax.[63]

Perry and Carter spent much of their time in Paris investigating the value added tax, and attending a conference of the International Fiscal Association.[64] There they met Dan Throop Smith, Professor of

Finance at Harvard Law School, and formerly Deputy Secretary of the Treasury under President Eisenhower. Smith's idea of tax reform was the minimizing of complexities, uncertainties and regressive features, the stricter enforcement of rules and the removal of special privileges in order to reduce the over-all rates, but not the taxation of capital gains as ordinary income.[65]

Carter and Perry discussed French taxes with two partners at the Paris Coopers and Lybrand office. They were told that the corporation tax was 50 per cent, with no credit allowed to shareholders: "clearly a double tax on corporate income...", Carter observed.[66] Inheritance taxes were "not high", and there was no capital gains tax for individuals, except for gains realized by company directors owning more than 50 per cent of the company's shares. There was a capital gains tax for businesses, however, with exemptions for gains reinvested within three years.[67]

At a meeting with federal tax officials in Bonn, Carter and Perry learned that about 55 per cent of West German tax revenue was obtained from direct taxes. The officials said that changes would be made, as the existing tax mix put Germany at a distinct disadvantage with regard to exports in relation to the other Common Market countries. Carter observed, however, that the German economy was "good, and, in fact, there is over-employment".[68]

The Germans had made extensive use of tax incentives, but this had "considerably diminished" because "it was said that these had favoured

one group of citizens over another...".[69] Apparently as a result of investment incentives, about 65 per cent of corporate investment was provided by internal sources. To encourage greater corporate reliance on the capital markets, a split rate of tax on corporate profits was introduced: 51 per cent on undistributed earnings, and only 15 per cent on distributed. The officials readily admitted however, that this measure had not been successful in achieving its purpose. Personal tax rates had also been reduced in the upper brackets - the top rate being reduced from about 98 per cent down to 58.3 per cent.[70] The Germans had succession duties, and a tax on capital gains, or "speculative profits", levied on sales of immovable property held less than two years, and on moveable assets, including shares, held for less than six months. They had the same problem as Canadian authorities in defining a trader in capital assets. Moreover, the tax on sales of securities held for less than six months was not enforced, since share owners were not registered in Germany.[71]

The final stop on the European tour was London, where the two Commissioners spent four days talking with government tax officials, members of the Richardson Committee studying the proposal to adopt the value added tax, and some chartered accountants and businessmen.

Carter and Perry learned about the new tax on speculative profits from Mr. E.R. Brookes, a member of the Board of Inland Revenue, who

> ...made it very clear that this was not a tax on capital gains [but rather one] on speculative profits. They believe that the short-term speculator in securities, and probably in other assets, would not be taxable under

> the law or the phrase "venture in the nature of trade", but for this legislation.[72]

A Board official charged with enforcing the tax told them that "the new law was brought about to obtain social justice", that there had been "serious political demands for such a law". Although it had been opposed by the stock exchange on the grounds that such a tax "would discourage needed speculation",[73] he believed that it had not had much effect, and even helped new issues by encouraging owners to hold on to them for at least six months. Unlike the situation in Belgium and Germany, the law imposed the requirement of full disclosure on banks, lawyers and stockbrokers.[74]

While discussing tax incentives with senior officials of the Unilever Corporation, Carter and Perry learned that

> ...a company of the size of Lever Brothers is not much influenced by taxation incentives from time to time. Their capital expenditure is essentially based on commercial considerations and they are usually sufficiently well financed that there is no shortage of the availability of funds [sic]. What is more, I discovered that they do not usually apply a very careful selective test to the purchase of machinery.[75]

The United Kingdom tax system provided an allowance for earned income on the grounds that "earned income should be favoured, seeing that it continues during a shorter period of a person's lifetime than investment income",[76] and also that wealth provided security (and hence an element of personal consumption) in addition to income. After hearing this "discrimination" against unearned income attacked at the Addington Society Meetings, Carter concluded that "...there is

very little room in the tax system for any discrimination as between earned and unearned income",[77] a cryptic observation containing the germ of the comprehensive income concept.

Some of the European countries Carter had visited levied a net worth tax as an alternative to, or as a supplement to, capital gains and estate taxes. After listening to a discussion at the Addington Society Meetings on the merits of a capital, or net worth tax, Carter concluded that

> ...a net worth tax would discourage investment in resource industries, particularly those which do not pay dividends but which people invest in for capital gain. Accordingly, I did not believe that such a tax would be good for Canada.[78]

It had been one of the main purposes of Carter's visit to investigate the value added tax, then under discussion in Europe. What Carter learned from the Addington Society discussions convinced him that

> ...most of the value added was, in fact, wages, and that this would be a tax on wages or, in fact, a tax on employment. Seeing that our greatest national problem is probably employment [sic], the tax was not suitable to Canada.[79]

Deadline Pressures from Finance

Mr. Diefenbaker had said that the Commission was expected to present its recommendations with the least possible delay. During the spring of 1963 the Commission had to cope with strong pressures from

the Liberal government and the new Minister of Finance, Walter Gordon, to furnish a final Report in time to be of use in his 1964 budget.

Burdened with the Liberals' election promise of "sixty days of decision", which was to include economic policy initiatives in a Spring budget, Gordon asked Carter to meet with him in his Parliament Hill office. With Gordon was Claude Isbister, his Assistant Deputy Minister for Taxation, while Carter was accompanied by Perry, Bennett and Hartle.[80] Gordon saw no need for what he regarded as a Tory commission and which had been given what amounted to a blank cheque. According to Carter's account, the new Minister wasted little time in telling them what he wanted:

> 1. To secure a report ...in time to be useful to the Government and the Minister of Finance in its annual budgets. He wished to have a report by the autumn of 1963 to be used for the budget in the spring of 1964.
>
> 2. To maintain the expenditure of funds to the amount already authorized for 1963-64 of $981,800 plus $250,000 recently authorized; these amounts to provide for the completion of all we have to do, including printing.[81]

The Commission representatives pointed out that their timetable did not call for the studies to be finished before September of 1964, and the Report itself, not before May 1965, to which Gordon countered that this would be of little help to him in the next three budgets. Carter then defended his conception of the Royal Commission on Taxation as "a long-term proposal and at no time had he contemplated that the report of this Royal Commission would be immediately translated into budget resolutions."[82] This position was supported

by Isbister, who agreed that the previous government had not sought any immediate solutions for budgetary problems from the Commission. The meeting ended without any specific agreement being reached, though Carter agreed to "consider the suggestions" put to him by Gordon: "and it might well be that the terms of reference would have to be extremely modified in order to accomplish what he asks."[83]

This alternative was not viewed with any enthusiasm by the Commission, having already decided to use its broad mandate to undertake the first really searching and comprehensive study of the Canadian tax system ever undertaken. While the Commissioners knew that senior officials were unhappy with the planned scope and depth of their enquiry, they had hoped that once the hurdle of Treasury Board approval of staff appointments had been surmounted, the Commission would be free to follow its own judgement.

Carter met with the other Commissioners the following day and informed them of Gordon's demands. Bennett reported that about two-thirds of their total planned expenditures of about $2 million would be for research. Carter advised the Commissioners that the cost of the research planned under the existing terms of reference "...could not be substantially reduced".[84] Given an inflexible budget, the Commissioners reasoned, the terms of reference and the tasks required would have to be reduced, something only the Minister could decide to do. The only sanction Carter had against Gordon was that of resignation, with the associated unfavourable publicity for the government, a sanction he was prepared to use if need be:

> I informed the Commissioners that, if Mr. Gordon required us to continue to carry out the present terms of reference and make available to us no more funds than those referred to in the accompanying memo, I believe that the Commission should be discontinued.[85]

Carter's reply, having been approved by the Commissioners, was sent to Gordon the next day.[86] He agreed to move up the Commission's schedule so that the research studies would be completed in May, 1964, and the final Report completed and translated by the end of that year. The Commission also undertook to make do with the reduced budget for 1963-64, provided they could secure an additional $554,800 for the subsequent and final year.[87] Carter did not concede any curtailment of the research activities however, and defended the Commission's interpretation of its terms of reference:

> To carry out our terms of reference, the Commission is obliged to investigate in depth both the economic effects of taxation and the equity and efficiency of the tax structure, as well as the relationship between the two. This is a heavy and challenging task. It requires research into both the economic and tax structure aspects, such as never before has been undertaken in Canada. We do not believe we can substantially reduce the present research programme and, at the same time, discharge the responsibilities of the terms of reference. If the Government does not wish us to proceed with the programme we now envisage, we consider that new terms of reference are required.[88]

Carter was trying to defend the Commission's research programme, not induce the government to alter the terms of reference. He made it clear that the latter course would be a risky one for the government:

> Should you decide to change the terms of reference, may I draw your attention to two problems which would arise. Ninety briefs have already been presented to the Commission and one hundred and fifty briefs are now

> being prepared on the basis of the present terms of reference. In addition, tax committees or commissions have been established by seven provinces and, in some instances, these committees or commissions came into being with the main objective of co-operating with this Commission on the basis of its present terms of reference.[89]

Having warned Gordon that he could not alter the Commission's research programme without changing the terms of reference, and do the latter only at his peril, Carter volunteered to share with the Department of Finance the results of the Commission's studies as they progressed. The Commission's staff was also prepared to review the research outlines with Finance officials. Carter included some of these outlines in his letter, and added that the Commission:

> ...would be pleased to discuss any modifications which seems appropriate. If you advise us as to the priorities you attach to particular study areas, we will make every effort to schedule our work to meet your requirements and to accelerate the studies commensurate with [the] maintenance of quality.[90]

Gordon replied the next day, taking up Carter's offer to address the government's priorities in its programme of research. Gordon had raised the surplus-stripping problem during their meeting on May 27th, and told Carter that the government attached a high priority to this issue:

> I am anxious if at all possible to obtain by the end of 1963 your recommendations pertaining to the taxation of corporate distributions. I can understand your hesitancy to commit yourself in advance to provide recommendations by a certain date on a subject which you may not have considered very fully. As the year progresses, however, I would appreciate it if you would keep the responsible officers of my Department informed of the direction of your thinking and, further, if you will keep in mind the priority I attach to your

recommendations in this matter.[91]

Gordon and Carter had reached a compromise: the terms of reference would remain unchanged and the Commission would receive the bare minimum of budgetary resources which Carter considered acceptable. In return Carter would undertake to have the Commission's final report presented to the government by the end of 1964, five months earlier than originally planned, and the Commission would give immediate priority to the study of the surplus-stripping problem and to the presentation of recommendations to the Minister of Finance as soon as possible. Gordon had struck a hard bargain. He got something of what he wanted -- the Commission's undertaking to furnish the Department of Finance with recommendations on surplus-stripping, and a personal commitment from Carter that the final Report would be in the government's hands in time to be of use in preparation of the 1965 budget. The Commission had bought some time, while preserving its relative independence from the government. But the deadline pressures were increased and the Commission would have to deal with corporate distributions out of the context with the rest of its economic and tax structure research, research which had yet to begin.

The Interim Report on Surplus-Stripping

The undertaking to supply the Minister of Finance interim recommendations on surplus-stripping was not really a detour from the Commission's programme so much as it was out of phase with the overall

plan for research and writing. When Gordon asked the Commission, at the end of May, 1963, to give this matter top priority, some of the research staff had yet to report to work and many of the detailed outlines for the various research projects had not even been drawn up. Any recommendations concerning surplus-stripping would not have the benefit of the results of the economic and tax structure research on which they ought to have been based.

The assignment of an interim report was discussed in the initial meeting of the staff's Corporate Tax Committee on the 10th of June. It was pointed out that the Department of Finance was interested in "interim measures themselves rather than a review of the entire structure...".[92] Not surprisingly, the staff preferred the latter, which would reflect more credit on the Commission. While "interim measures could be suggested fairly easily", there remained the problems of collecting data for the economics side of the problem, and "obtaining a reasonably detailed analysis of the tax structure side", before the economic analysis could be carried out.[93]

Some thought had already been given to the matter. The surplus-stripping issue had been an important consideration behind the appointment of the Commission, and the Commissioners and their staff were no doubt aware that this was one of the "anomalies or inequities" implied in their terms of reference. As early as April of 1963, before their meeting with Walter Gordon, Carter had asked for Hartle's assessment of one possible solution:

(1) 10 or 15 percentage point reduction in the corporation tax on distributed profits.
(2) Co-incidentally, a reduction in the tax credit from 20% to 10%.
(3) Removal of any further tax on the distribution of income.[94]

By the first point, Carter had meant that the fraction of corporate earnings which were distributed in the form of dividends would enjoy a lower rate of tax than retained earnings. The meaning of points 2 and 3 is not clear, since "removal of any further tax on the distribution of income", that is, personal income tax on dividend income, would remove any need for a dividend tax credit, however small, unless it was intended to apply the credit to other than dividend income. These proposals would have removed the so-called "double taxation" of corporate income by eliminating personal tax at the point where corporate income was distributed as dividends.

The logic of the proposals can be re-constructed as follows: shareholders would no longer have the incentive to appropriate their portion of corporate profits by realizing a capital gain on the sale of a portion of their shares, or through surplus-stripping, since there would no longer be any personal income tax to avoid on dividend income. Retaining a reduced dividend tax credit against income from other sources was apparently intended to provide a further incentive toward receipt of dividend income, and away from the vehicle of share value appreciation due to retained earnings. The reduced corporate tax rate on that fraction of profits distributed as dividends would have offered a parallel incentive to corporate management to distribute a greater portion of earnings in the form of dividends.

Since shareholders of closely-held corporations would no longer have had any tax incentive to appropriate profits through retained earnings, surplus-stripping would have been eliminated. Overall, of course, the tax burden of the owners of corporate shares would be substantially reduced compared to that of other taxpayers.

Hartle replied with ten preliminary comments, eight of which addressed the implications for fiscal stabilization policy, uncertainties regarding the impact on retained earnings and an appropriate policy on retained earnings, the revenue effects, the possible response from provincial governments, administrative problems and possible effects on corporate behavior. His comments four and five addressed the implications for horizontal and vertical equity:

> 4. Under the proposed tax change the highest personal tax rate would be 50% for those individuals obtaining their incomes from closely-held corporations. Why discriminate against those getting their incomes in other forms? Wouldn't it be necessary to make the highest marginal tax rate 50% in order to treat equals equally? The issue must be faced squarely.
>
> 5. The effective rate of tax on individual[s] with large stock holdings is, as you know, much below the rates that appear on the tax table both because of the individual tax credit and because retained earnings result in capital gains which are not taxed. Our studies (and the study now underway by John Allen at Queen's) will quantify these impressions. In my view it would be desirable to await these results before advancing the proposal.
>
> First, the Commission must decide what the maximum marginal rate <u>should</u> be and <u>then</u> change tax provisions to make it effective. The strategy of lowering the top rate to the presently effective rate (approximately) might seem an avoidance of responsibility. At least we should be able to argue that the maximum rate <u>should</u> be x%; or that

> to push the rate beyond x% would create specific problems which would be so serious as to make the Commission lower its [sights].
>
> A whole range of tax complexities could be eliminated if the progressive rate structure were abandoned or substantially modified. But a socially acceptable rate structure (distribution of income) is at least as important an objective as a simple tax structure. I am not suggesting that the maximum rates should not be lowered. I do believe, however, that the rate structure should be considered as an issue and not altered piecemeal.[95]

Carter appeared to favour the proposals he outlined to Hartle,[96] volunteering the assessment that "It appears to me that, structurally, such changes would be an improvement, but we should have a look at what effect, if any, this would have on the provincial laws as well as the federal."[97] It is surprising that he makes no comment on the clearly regressive implications of the proposals. Hartle's comments, on the other hand, placed considerable emphasis on the distributive aspects, (devoting one-third of his response to the vertical equity aspects alone) and the importance of keeping within view the entire tax structure when discussing reforms of any one aspect. In the great importance attached to the principles of equity in Hartle's response, and its view of the necessarily interrelated quality of the tax structure, one can discern the spirit behind the key principles of the Carter Report.

In June, 1963, while the Commission's research was getting under way, Walter Gordon presented his first budget to Parliament. Prepared largely by three consultants brought in by Gordon, the budget was intended to reduce the extent of foreign ownership of businesses

incorporated in Canada, as well as to correct the surplus-stripping problem. The use of "outside experts", two of whom were still on the payroll of their Toronto firms, was seized upon by the opposition parties in an attempt to discredit both Gordon and his budget measures. The Royal Commission was not implicated, as even Gordon's anti-surplus-stripping measures were framed without the advice of the Commission.[98]

One of the "outsiders" who prepared Gordon's June budget was an accountant by the name of Geoffrey R. Conway, who had worked for Gordon's firm, Clarkson & Gordon before he went to Harvard to work on a doctorate in Business Administration. His initial thesis topic was the taxation of capital gains, and, with the rare dual qualifications of accounting and economics, Conway was just what the Commission needed. He agreed to join the Commission to work on capital gains taxation early in 1963, but paused to help Walter Gordon through 59 of the Liberals' "60 days of decision".[99]

Work on the surplus-stripping study, along with other Commission research, continued throughout the summer, and by the fall, the staff was preparing and revising drafts. Conway contributed a draft of one possible alternative solution which at that point, was considered too radical to put before the Commissioners except as a hypothetical policy option in the surplus-stripping study.[100] Under the heading "the capital gains method", Conway hastily sketched out on ledger paper the first proposal in the Commission's records consistent with the comprehensive tax base:

1) Capital gains to be taxed at full personal & corporate rates. This gets at the seller & other than problems raised by point 5/ removes problem of income definition from the act. As to incentive to obtaining gains through capital rather than dividends (other than postponement) will end most of corporate distribution problem.

2) Maximum personal rate lowered to 50 or 55%.

3) Corporate tax at a flat 45 or 50%.

4) Certified [companies] ...(say Cdn. controlled, profits on average [of] less than $100,000) allowed 100% depreciation, an allowable reserve of say 20 or 25% against inventory & accounts receivable, and possibly a straight tax exemption from the first $5,000 of income. All [companies] ...could be given [the] right to taxation as a partnership.

5) Dividend tax credit raised to 25 or 30% and extended to cover realized gains and realized losses on securities. Thus maximum tax on capital gains of 25% Some problems in defining a security & heavier tax burden placed on real estate & sundry transactions. However, certain transactions (sale of personal property including houses) could be tax exempt & others could be given tax credit treatment.

6) Averaging of income permitted if income of any year under 50% of prior year's income. Averaging extended to 3 years if 3rd year also under 50% of 1st year.

7) Deemed realization of capital gains on death or if a gift and if possible on a change of residence.

8) If [one] want[s] to reduce tax[es] on corporate capital gains (where [you] don't have [the] same definitional problem) [you] could only take half of [the] gain into income.[101]

Points 1, 2, 3, and 7 would later appear in the Carter Report. The Report's provisions for new, small businesses would resemble somewhat Conway's fourth point, inasmuch as the terms of depreciation would be liberalized. Conway's points on the dividend credit and averaging were to be surpassed in generosity in the Report, but the

logic and direction of Conway's tiny sketch were followed remarkably closely in the six-volume Report. However, it was an idea whose time had not yet come, and, pending the outcome of the decision-making process within the Commission, might never come.

By October 1963, the exact form the surplus-stripping report should take had still to be decided. The Commission was very reluctant to present public recommendations to the Minister of Finance before the results of the rest of the Commission's research were known.[102] Hasty recommendations might not be consistent with those in its final Report, and could be used to discredit it. Probably, the Commission was wary about being too closely associated with Gordon's second budget in view of the controversy aroused by the first. The agreement between Gordon and Carter of the previous May, by which the Commission accepted the task of presenting a preliminary report and recommendations on surplus-stripping, had been kept secret for fear of revealing that the government had successfully applied political pressure on the Commission.[103]

With these considerations in mind, Carter met with Walter Gordon on the 29th of October to discuss the form which the Commission's interim report on surplus-stripping was to take. Gordon told Carter that "he was quite prepared to receive a memorandum... on surplus-stripping in the form contemplated and without recommendations."[104] They agreed that it would not be made public, and that, as a memorandum between their respective staffs, it would "not be a form of communication".[105]

Meeting on November 15, the Commissioners reviewed and approved the third draft of the surplus-stripping report. Two weeks later, Hartle sent the final version to Carter for his comments, requesting permission to forward the study to the Department of Finance the following week[106] as an unofficial, confidential staff memorandum.

The authors of the interim study, Stripping of Corporate Surplus,[107] did not share the "grave concern" about the problem expressed by "the Minister of Finance and tax practitioners".[108] While acknowledging it to be a violation of the equity principle, the Commission doubted that it was the greatest of perhaps many inequities in the tax system.[109] The staff believed that attempts to "solve" the surplus-stripping problem in isolation from the whole question of corporate taxation could result in the creation of greater inequities. Nor did they consider the economic effects to be very important for the Canadian economy. What was important was the:

> ...greatly increased uncertainty surrounding an important part of the tax system. Uncertainty creates contempt for the system and results in more tax avoidance and attempted evasion.[110]

To prevent surplus-stripping without changing the treatment of retained earnings in widely-held corporations would put the owners of the closely-held corporations at a disadvantage relative to shareholders in widely-held corporations. It would be desirable, the study suggested, to deal with surplus-stripping in the context of "changes in the tax structure that would eliminate both inequities

simultaneously."[111] Four possibilities were put forward:

> 1. Provide that shareholders include in their personal incomes each year their portion of all of the current incomes of the corporations in which they hold shares....
>
> 2. Allow individual shareholders to exclude all corporate distributions from their taxable incomes....
>
> 3. Devise a tax structure that would be a compromise between approaches (1) and (2)....
>
> 4. Define personal income to include all the realized gains in the values of corporate shares and tax them at full personal rates.[112]

Each alternative was followed by a short explanation of its implications. The fourth alternative, which was consistent with the comprehensive income concept, was similar to that proposed by Conway the previous October, and the one finally adopted by the majority of Commissioners. The study however, passed over that alternative with the following brief comment:

> By extending the concept of personal income in this way all shareholders would be on the same footing and surplus stripping would be pointless. However, this approach goes far beyond the point at issue in this study, for it would impose taxes on gains that were completely unrelated to corporate income. This approach is not discussed in this study.[113]

Although there was nothing in the study that would rule out this alternative, it was played down. However, the general tone of the Interim report -- its attention to questions of horizontal and vertical equity, and its reluctance to accept patch-work solutions -- would eventually become well-known trademarks of the Carter Report.

More Deadline Pressures

With the surplus-stripping memorandum out of the way, the Commission was able to concentrate on the research programme and the schedule for producing its final Report. At the beginning of January, 1964, it appeared on the surface that the work was more or less on schedule. A memorandum from Carter to all the Commissioners summarized the progress to date and warned them to expect a 150 page draft outline of the Report from Hartle in preparation for the Meeting of Commissioners in the latter half of February.[114] This outline was intended:

1. To indicate the progress of the research work to date.

2. To show the way in which the research work will form part of the final report.

3. To set forth the tentative research findings that have emerged from the research work, including as far as possible statements of the alternatives available.[115]

Carter passed on Hartle's warnings about the limitations of the outline. The research work was far from complete. The outline was therefore very uneven in the detail it provided, and some of the research results were, in some cases, no better than a "best guess". No attempt had yet been made to integrate the results of the tax structure research with that of the economists. The goals of economic growth and efficiency, on the one hand, and those of equity and ease of administration on the other, had not yet been reconciled if and where they were in conflict.[116]

The same day, Carter learned that the Commission's work was behind the revised schedule. In a private meeting with Carter and Perry, Hartle warned them that the econometric studies would not be completed in time to enable the report to be prepared by the end of the year.[117] Given Carter's public commitment to Gordon the previous May that the Report would be in the hands of the Government by the end of 1964, and the slow progress of the econometric work, Hartle warned that they "...might be proceeding along a 'collision course' and... [he] was very worried as to the outcome."[118] In order to meet the existing schedule, the last studies would have to be completed by the end of September, which did not take account of the time required for the studies to be discussed by the Commissioners, or for their decisions and recommendations. The three men considered a number of possible ways to cope with this crisis, including issuing the Report in two or more stages, and converting part of the research into study papers which would be published later without recommendations. No alternatives were thought to be satisfactory, and all solutions canvassed threatened to dissociate the Commissioners' recommendations from the results of the research, something which Hartle had been trying to avoid from the very beginning.

Despite his disappointment and his great reluctance to go back on his public commitment, Carter accepted the inevitable responsibility of informing the Minister:

> I have given you complete assurance throughout that you would have a report from this Commission by the end of

this calendar year. In doing so I made some allowance for translation and printing, but I am now informed that this allowance is insufficient. It appears that in order to meet the undertaking which I have given it is necessary to follow one of three courses:

1. Greatly curtail the extent of the research work and produce recommendations on tax structure and a minimum of economics necessary to support immediate changes. This would quite obviously deal inadequately with the economics of taxation so far as they affect growth and stability and would give you little support for long-term policy.

2. Divide the project into two reports - one for release, translated and completed, by December 31, and the other for release some months later. This would in the first report cover our view of tax structure matters for immediate and future implementation, but would not provide a full treatment of the supporting economics at that time. The second volume would obviously fill you in on this matter and would set forth our views on long-term effects of taxation.

3. Produce the entire report by December 31 in typescript but not translated nor printed until some months later. We would, of course, sign the typescript and deliver it as a completed document, and no changes would be made in the final printing or translation so far as that were possible. You will promptly realize that this will put the Government in possession of our report before it is made public generally because we would not then deliver a translation or sufficient copies for it to be tabled in the House. I understand that to do this we would need some 700 or 800 copies.[119]

Carter closed his letter with the suggestion that Bryce, by then Gordon's Deputy Minister, and Hartle meet to discuss the problem in order to "seek the best solution...".[120] Though Carter attributed the delay to previous, overly optimistic estimates for translation and printing, alternatives 1 and 2 implied that it was the economics research which was behind schedule. Nor did he admit that the processes of integrating the research into draft chapters of the

Report, and the Commissioners' review of the chapters and arriving at recommendations had barely started.

Even though the extrapolation of the existing situation had suggested that the Commission might be close to the brink of disaster, Hartle reported to the Commissioners on the 13th of February, that "with relatively few exceptions, the research work has proceeded on schedule."[121] Only the econometric work, the economic growth studies, and the administrative studies were behind, and these delays would "not prevent completion of the first draft by the target date of October 15."[122] The timetable called for the research staff to present their findings and the Commissioners to reach their recommendations between June 15th and July 1, and for the Supervisors to draft sections of the final Report between July 1st and September 15th. As the Report would be longer than originally anticipated, the job of translation would require more time than expected. Rather than split up the Report, Hartle strongly recommended that the Commissioners accept an alternative suggested by Bennett, that the Report be presented in typescript and mimeograph or offset form to Cabinet by the end of the year, with translated and printed copies as soon as possible thereafter.[123]

Finding any alternative to this to be "extremely unattractive", Hartle defended the proposed scope and depth of the Report, as being consistent with:

a) the extremely wide terms of reference given the Commission;

b) the need to spell out all of the major alternatives available with the pros and cons of each, as well as the conclusions of the Commissioners;

c) the need to establish confidence in the Commission's findings by demonstrating that the Commission had done a thorough job in the investigation of the economic, legal and administrative fundamentals of the subject;

d) the need to prepare a report that will be relevant over a significant number of years - and therefore gives consideration to long-run as well as short-run questions;

e) the need to inform and educate the public, in addition to advising the government;

f) the need to put tax questions in a wider context and thereby give some perspective;

g) the need to carefully comment on the views of participants.[124]

If these objectives were accepted by the Commissioners, Hartle concluded, then a Report of about 2,500 to 3,000 typed pages would be required. This, in turn would impose an additional burden on the translation services. The resulting delay in completing the translation and printing the Report, made Bennett's proposed "limited edition" for Cabinet the only solution that would deliver a Report to Cabinet, intact and on time.

As Carter had suggested, Hartle and Bennett met Bryce in his office, along with Ray Irwin, the Director of the Taxation Division.[125] After Bennett had reviewed the problems of translation and printing, it was agreed that the Commission would provide a Volume I, containing a Summary and Conclusions in English and French by the end of the year, and the remaining three volumes "as quickly as

possible". Bryce insisted that the additional volumes be delivered to the Government with the "utmost speed."[126] Hartle and Bennett assured Bryce that they would supply the Department with a typescript of the entire Report, so that the considerations relating to the Commission's recommendations in Vol. I would be available to them.[127]

While Gordon continued to press for at least the summary Report to be made available sooner,[128] the assurance that the Department would have access to the Commission's Report by the end of the year secured a measure of peace for the Commission.[129] The accord reached between Bryce and Hartle laid the groundwork for the formation of a departmental task force to study the Commission's Report, and which would, five years later, culminate in the Government's Proposals for Tax Reform, better known as the "Benson White Paper".[130]

Development of the Comprehensive Income Concept

Basic Tax Structure Alternatives:

In April 1964, Hartle, McDougall, Goodlet, Fields and Thompson jointly produced a research memorandum entitled "Basic Tax Structure Alternatives".[131] Aside from Conway's very schematic and limited proposal for the Report on Surplus-stripping the previous October, this document provided the first clear statement that the Research Staff was thinking along the lines of the comprehensive income

concept.[132] The memorandum was divided into several sections, each written by one or two of the group.

The first section, "Tax Structure Alternatives", written by Hartle, stated six "basic assumptions", taken from the "Draft Outline of the Report":

1. Only natural persons have taxable capacity....

2. Horizontal equity is served when individuals with the same taxable capacity bear the same tax.

3. Taxable capacity is defined as the market value of the goods and services that the recipient could consume over a given period without reducing the market value of his stock of assets. This is fundamentally an income concept of taxable capacity. The wealth or consumption concepts of taxable capacity are rejected (although the income concept is necessarily related to the wealth concept and consumption is a part of income).

4. Individuals with different taxable capacities should bear taxes that are "appropriately" different.

5. It is assumed that taxes are not shifted (or that because we do not know to whom and to what extent they are shifted we have to ignore all shifting).

6. It is also assumed that there is no change in the general level of prices (inflation or deflation).[133]

The first four assumptions, which Hartle acknowledged to be value judgements were consistent with the ability-to-pay view of taxation. Only a tax system which brought all types of economic gain into the tax base, and applied the same rate of tax, would be consistent with the definitions of horizontal and vertical equity set out in points 2

and 4. Point 3 provided a conceptual definition of "taxable capacity", which was probably chosen instead of "ability to pay" because of its appearance of greater objectivity. Point 4 implied that, in order to satisfy the criterion of vertical equity, the sum total of all economic gains thus included in the tax base should be taxed at some undetermined progressive rate.

The three subsequent sections, also written by Hartle, outlined the various implications and difficulties of adopting the comprehensive income concept. After retreating from the full rigour of the pure concept due to such problems as the valuation of accrued gains, liquidity problems in paying tax on unrealized gains, the tendency to understate personal consumption expenditures, and the administrative complications of assessing all gains no matter how trivial or poorly recorded, Hartle arrived at a tax base including most realized gains but allowing for "a statutory allowance for living expenses deducted from labour income..." in lieu of allowing deduction of all consumption expenses, and excluding from the base imputed rent, increases in business goodwill, accrued but unrealized gains in asset values, gains from sale of owner-occupied houses, and members' benefits from associations.[134]

He then listed eight "implications and administrative difficulties" arising from this modified tax base, including the relative advantage afforded recipients of accrued gains due to deferral of tax liabilities, the advantage given to people who owned their own homes, the need to declare realization of assets on the

death of the owners in order to prevent perpetual postponement of taxes, and the need for an averaging scheme to soften the effect of progressive tax rates on certain forms of "lumpy" income, such as gifts, inheritances and the receipts from the realization of assets.[135] The logic and implied conclusions were similar to that of the Commission's published Report.

"Section D", written by McDougall, dealt directly with the comprehensive income concept as outlined by Richard Musgrave, noting that this "would require the taxation of gifts and inheritances in full at personal progressive rates.[136] McDougall then presented a list of "pros" and "cons" for such a step:

Pros

1. It would provide greater revenue.

2. It is consistent with the broadened concept of income, in that in most instances gifts and inheritances increase the individuals' capacity to pay.

3. It would eliminate the need for separate gift and estate taxes.

Cons

1. The valuation problem which now exists would become more acute as a result of the substantially higher rates which probably would be exigible.

2. The conversion problem (liquidity) also becomes more acute. Even at the present rates this problem is held out to be a substantial one.

3. It could create a disincentive to save.

4. The unpredictability of receipt and its lumpy nature may qualify this kind of receipt for preferential treatment.[137]

McDougall then proceeded to a discussion of "Some Aspects of the Individual Tax Base", including problems of separating individual and business income. Concerning the problem of arriving at an equitable way of taxing realized gains in land and securities which had accrued over several years, he proposed two alternatives for preferential treatment:

> 1) stepped percentage exclusion of gains from tax base depending on the length of the holding period, with similar treatment of losses, such as [under] the Swedish system;
>
> 2) include 100% of gain, but apply tax credit or lower rate to the net gains.[138]

The following section, written by Goodlet, discussed various alternatives for dealing with the income of businesses and organizations, among them, the integration scheme finally adopted in the published Report. Goodlet however, did not argue in favour of the integration approach, preferring instead a tax on undistributed income and waiving any further tax when the income was distributed. Although Goodlet did not suggest a rate for the proposed tax, it was similar to the existing system in which tax was assessed on "designated surplus" of 15 or 20 per cent. In terms of the "taxable capacity" criteria expounded by Hartle in the first section of the memorandum, Goodlet's treatment was less equitable than the integration scheme, and oddly out of step with the move toward the comprehensive income concept apparent in other sections of the document.

In an appendix, Hartle tackled the question of taxing corporations as such, rather than attributing their income to individuals and taxing it in their hands. While conceding the administrative advantages of a corporation income tax, and the argument that corporations are legal persons, wielding considerable power, he maintained that any tax levied on corporations must necessarily reduce the taxable capacity of one or all of: employees, suppliers, customers, creditors and owners. Hartle rejected two arguments for taxing corporations: first, that the "corporate form gives rise to undesirable social or economic effects which should be restrained" and therefore bear an additional tax burden and the second, that the owners, or those who deal with corporations, should pay something extra for the advantages conferred on them through the use of the corporate form of organization:

> We take the position that the first of these propositions is factually false, and indeed we believe that on balance the corporate form has bestowed benefits on society as well as upon those who own or deal directly with the corporation. Having taken this position the second proposition is no longer valid. It is costless to society to extend the privilege of the corporate form and it is believed that the use of the corporate form, on balance, bestows political and economic benefits on society. Therefore, to tax this form of organization would, by restraining its use relative to other forms, impose a loss on society.[139]

Hartle's logic was unassailable, though he did not explain the basis for his contention that the first proposition was factually false. Many defenders of the Carter Report would eventually find cause to disagree with him.

The "split corporate rate" (the existing low rate on the first $35,000 of corporate income) was analyzed and found wanting in another appendix, written by McDougall.[140] Reaching conclusions very similar to what eventually appeared in the published Report, he found the preferential rate to be "too blunt an instrument to achieve any but a broad political purpose".[141]

In a third appendix, D.B. Fields looked at a list of seven possible ways of taxing capital gains, beginning with "a broadened concept of income", and moving to progressively narrower alternatives. The first alternative would have taxed most realized gains, with the unexplained exception of gifts and inheritances.[142]

The joint memorandum was trying out different ideas in various combinations. There was an overall lack of consistency in the document, as might be expected given the multiple authorship and the relatively fluid state of their thinking at that stage. For the first time, however, they were taking the comprehensive income concept as the bench-mark for other alternatives, and in the sections written by Hartle and McDougall, it was treated as a preferred alternative.

The Need for Additional Time:

Most of the initial draft chapters of the Report were written by the research Supervisors, each responsible for those chapters most closely related to the special studies he had conducted. They were

then revised as necessary by the Co-ordinators and Hartle, then edited and translated by the editorial staff and given to Bennett for mailing to the Commissioners. The timetable envisaged by Douglas Hartle at this time called for all the draft chapters to be completed and mailed to the Commissioners during May, June and July.[143] It was planned that the Commissioners would meet in Ottawa for eighteen days in August to discuss and give final approval to 31 draft chapters. The Commissioners were warned by the Secretary of the heavy workload which this would entail: decisions on an average of two chapters per day.

At this stage it was expected that the Final Report would occupy four volumes and about 2,950 pages. If the Commissioners and staff were able to adhere to the demanding schedule, they planned to release the initial volume to the public, and present the remaining three volumes to the Government by December 30, 1964 for later release as they were ready.[144] However, events worked out otherwise. Meeting in Ottawa for a week in May, the Commissioners were able to deal with only six chapters. As the meetings dragged on into the Summer, it became apparent that Hartle's ambitious timetable could not be met.

At Hartle's invitation, Harvey Brazer, by then a Professor of Economics at the University of Michigan, came to Ottawa in June, 1964, to discuss the taxation of capital gains, the personal tax structure and the desired degree of progressivity, the averaging of personal income and the taxation of gifts and bequests.[145] To aid the discussions Hartle sent him in advance some material which the staff had been working on, including two studies on corporate taxation and

early draft chapters dealing with the taxation of capital gains. Brazer's visit helped the Research Staff iron out some of the difficulties apparent in the April paper on "Basic Tax Structure Alternatives" and moved the Commission a little closer to acceptance of the comprehensive income concept.

Hartle also explained the severe deadline pressures facing the staff, and the implications which they might have on the content and quality of the Report.[146] At Hartle's request, Professor Brazer wrote to Bennett, advising the Commission against undue haste:

> The task of the Commission and its staff is indeed a formidable one and, because of the lasting influence that is bound to be exerted by its report, I should strongly hope that the Commission will not feel excessive pressure to produce that report before it is fully ready to do so. One can never, of course, be "fully ready"; I mean to say only that the number of issues deserving careful deliberation is great and that mistakes made now could take generations to undo.[147]

Brazer's advice was intended for Carter, whom it helped prepare for yet another memorandum from Hartle on the timetable. A week later he wrote to Carter, advising him that the Commission's Report, if it were to have any lasting value, could not possibly be ready by the end of the year.[148] Much more than a warning that the Commission's Report could not be completed on time, Hartle's memorandum was also a critical appraisal of the way the Commission had been working up until that time, and set a standard to which the Commission should aspire in writing its Report.

The quantity and quality of the work of the research staff was

falling short of Hartle's most optimistic expectations, and it was upon such expectations that he had accepted the existing timetable:

> ...the staff is now in the position where even if it exerts superhuman efforts in the next four months it is certain to be ashamed of any Report that is sent to the printer in the fall. The deadline under which we labour was established with so little real knowledge of what was involved that it is, to all intents and purposes, arbitrary. If I had known in May of 1963 (the date of the meeting with Walter Gordon) what I now know, I would have resigned rather than accept the December, 1964, deadline. I am not willing to sacrifice content and quality in order to honour what I now know to have been a foolish commitment. I believe it is better to disappoint a few men than miss an opportunity to be of real service to the nation.[149]

Hartle then defined what he meant by an acceptable level of quality:

(a) There should be adequate coverage of all the issues raised in the terms of reference, together with a full discussion of federal-provincial tax arrangements.

(b) The issues must be set out objectively and all of the major alternatives must be presented fairly and frankly.

(c) the Report should include both short- and long-run recommendations.

(d) There must be full integration of the economic, administrative federal-provincial relations, and equity parts with the tax structure parts. This means that the numerous conflicts among objectives must be spelled out in dealing with each of the alternatives.

(e) It is sometimes difficult to know the difference between being politically expedient and being realistic. The Report must be realistic in the context of a society that is changing very rapidly. Given the mood for change that seems to be present today, and the belief that the Report is being written for a decade and not a particular budget, an attempt to please everyone who reads the

Report will make it pedestrian and futile. Every effort should be made to produce a bold and imaginative Report. This does not mean that the Report has to be vague, or careless or superficial. By writing it for both the present and the future it is possible to be practical and imaginative.

(f) The report should have a theme or themes so that it hangs together and tells a story. It will not be adequate if the reader gets the impression that he is looking at a string of unrelated items.

(g) The literary style must be clear, and vivid and free from the jargon of accountants, lawyers and economists; yet it must be written at a level that makes it of interest to these groups.

(h) The major ideas in the report must have been reviewed and commented on by the best specialists we can find before it is submitted.[150]

Any Report which could be prepared by October, Hartle was convinced, would fall far short of this standard. The reasons he gave for this amounted to a severe assessment of the Commission's efforts, and of his own. Some of the research projects were "lagging badly". The results of the work of other researchers was very disappointing, and he had to anticipate similar results from some of the projects still to be heard from. It was the same with the consultants: "Virtually all of the men we had counted on... have been unable to help significantly."[151] This put a greater burden upon the full-time staff at a time when badly-needed specialists, their terms of employment expired, were leaving the Commission: by the end of July, Hartle expected that only fifteen people "capable of doing independent research" would remain.

The economics and tax structure results had not yet been

adequately integrated. Hartle acknowledged that this was partly the result in an error in organizational design: "The two 'divisions' have tended to be just that!"[152] It was also due to the inability of the Commission to attract sufficiently qualified specialists. As a result, much of the early period was spent learning, and there was nothing to co-ordinate. Later, the speed-up of the work did not allow for co-ordination. As a result, Hartle feared that the draft chapters would not even recognize conflicts between the two areas, much less apply the results of the economic analysis to the material on the tax structure.

The changing of deadlines and "misunderstandings of government administration" had been bad for staff morale.[153] As a result, valuable time had been lost in dealing with staff problems. Hartle felt that the "speed-up" following the commitment to Gordon, had actually cost the Commission time.

Time was also lost "trying to elicit decisions from the Commissioners". Because the studies were still incomplete, the Commissioners did not have a complete picture of all the alternatives before them. Some of these "tentative 'decisions'" were upsetting to members of the research staff, some of whom tried to anticipate the Commissioners' views by ignoring alternatives which they thought the latter would reject, resulting in "a lack of objectivity".[154]

Hartle predicted that the draft chapters that would likely emerge from this situation by October, while covering most of the contents of

the Report,

> ...will be totally inadequate as a group. There will be large gaps. The decisions will be detailed in some areas and vague in others. There will be no theme to the report. The bigger issues will be less adequately discussed than the trivia. There will be endless inconsistencies between the economics and tax structure volumes. The latter will not really reflect the economic growth and stability conclusions; but will be largely based on administration, and "feasibility" grounds. In short, the report, in October, will look shortsighted, inconsistent, and expedient.[155]

All was not lost, Hartle assured the Chairman, for they would have in October, at least the raw materials for a Report with the desireable qualities he had described. The work of integrating the material would take several months more, and would likely not be completed before August of 1965.

Should the additional time that he requested be available, Hartle proposed a revised procedure for producing the Report:

> Because the research work is delayed, and in some cases inadequate, the Commissioners, under our present programme, are receiving a series of bits and pieces - and receiving them late. In many cases the bits and pieces are quite incomplete, even in their own narrow sphere, because of the lack of integration alluded to above. What is even worse, they are presented out of context. This means that our drafts lead the Commissioners to take too narrow a view. It also means that many of the decisions are inconsistent and will have to be reconsidered. To be perfectly frank, the sessions spent reviewing drafts with the Commissioners usually have not been helpful to the staff. They are, however, time consuming. I am sure the Commissioners also find these sessions frustrating.
>
> I would like to suggest that -
>
> (1) the present procedure of staff-commissioner discussions of isolated chapters be abandoned;

(2) the staff will continue to provide the Commissioners with draft chapters or chapter outlines, as these become available;

(3) no attempt will be made to review these drafts with the Commissioners until they have been revised and assembled into integrated units by the staff;

(4) the Commissioners will keep the staff informed of the alternatives they wish to see discussed in the Report;

(5) the staff will do its best to cover these items in the full draft submitted to the Commissioners if time, space, logic and style considerations permit;

(6) The full drafts of integrated units will be presented to the Commissioners as soon as they are available.[156]

Carter was not yet a convert to the comprehensive income concept, and Hartle would have been wasting words to have attempted to state his project in such an unguarded fashion. Were the Commissioners to continue to be given one draft chapter after another for their discussion and approval, paragraph by paragraph, when they had not even agreed on the basic principles of a tax system, the resulting Report would almost certainly have lacked consistency. In order to build the chapters around the comprehensive income concept in a coherent way, the remaining staff had to be temporarily free of the constraints imposed by the meetings of Commissioners.

Carter's reply is not preserved in the Commission's records, but he had little choice but to approve Hartle's proposal. The record of the summer and fall Commissioners' meetings[157] shows no indication of a change in procedure, but the absence of recorded minutes after the late Autumn of that year suggests that Hartle's revised procedure was

being followed.

The July, 1964 Meeting at the Seigniory Club:

In mid-July, the Commission hosted Professors Ash Wheatcroft and Carl Shoup at the Seigniory Club at Montebello to hear their views on some of the draft chapters, and to give some further direction to the thinking of the Commissioners. Carter's notes of the discussions indicate that he and the other Commissioners had not yet settled on even the broadest questions of principle concerning the tax base.[158]

The range of opinion within the Commission on the question of taxing capital gains and on what should be included in the tax base is especially significant:

> At one time the U.S. permitted a graduation of the capital gains bought into income somewhat along the same lines as the present Swedish system. This was done as a crude form of averaging and apparently had no particular regard for the fact that short-term holdings were more of a speculative nature and, therefore, more properly included in tax. It was recognized that such a graduated tax would have the effect of locking in the gain waiting for the erosion of tax liability and, as such, might have an unfavourable impact upon the capital market. In all events, everybody recognized that capital gains could only be fairly taxed if there was an imputed realization upon death.
>
> At this point, I explained to our visitors my own thoughts as to the use in Canada, for capital gains purposes, of the Swedish system running out to zero over a period of years. This seemed to be thought to be a not unreasonable compromise. As an alternative, Professor Shoup suggested that capital gains should be

brought into income as every other form of income, with some simple averaging system.[159] Then, having done this, for reasons other than equity, it might be necessary to discount the amount by which taxes were applied to the capital gains portion. We all recognized that, so long as capital gains were taxed at anything less than the tax on other income, it raised administrative and structure problems which were quite serious. For stabilization purposes, Professor Shoup welcomed a heavy deduction of losses in capital gains taxation. It was suggested that, if we went to the graduated system, a small residue of gain - say, 2% - should always be taxed so as to recognize the fact that all income was subject to tax.

Professor Wheatcroft made the point that income from different sources is clearly not all the same and, on equity grounds, should not necessarily be taxed in the same manner. Professor Shoup pointed out that, on economic grounds, we must distinguish between different types of income and probably tax them differently.[160]

In discussing businesses, it was pointed out that the U.S. depends largely upon the definition of the asset and does not have to decide if a taxpayer is in business. Very often the conduct of the taxpayer governs the nature of the asset and so he cannot be entirely left out of consideration in deciding whether or not it is a business asset....

We proceeded to discuss an additional tax in respect of corporation undistributed income, for Professor Shoup was very much concerned that such income was greatly favoured under the U.S. tax scheme and, of course, more favoured under the Canadian.

Professor Hartle countered by saying that the staff of the Commission had felt that the only really good system would be to reduce the higher rates of tax to 35% or 40%, to impose a capital gains tax at normal income tax rates, to impute the capital gains upon death, and then to have a single lower rate of corporation tax only. He was of the opinion that some such proposal would provide greater equity and would overcome most of the administrative difficulties. I gave it as my view that our report should set out his ideal tax system, which would probably be the best conceived, and that we should conclude by stating to what extent we believe the country might move in that direction in its initial step and suggest that it might be some time before it accomplished the entire move.[161]

What Hartle was proposing on behalf of the Research Staff was a succinct statement of some key elements of the comprehensive income concept, and which was close to what eventually emerged in the Report. Although Carter was persuaded that capital gains should be taxed, he did not think that Hartle's suggestion was practical in the near future in Canada. Hartle still had a formidable selling job in front of him.[162]

Approving the Draft Chapters

By September, 1964, most of the staff had left the Commission and the Commissioners moved the location of their meetings to Toronto, where Carter and Perry had their offices. They were joined by Hartle, John Bossuns, Geoffrey Conway and John Tinker in offices on Bay Street, between King and Adelaide, near those of Carter and Perry. This small rump of the Commission's formerly large staff wrote and revised the remaining draft chapters and filled in holes in the research as they became apparent. Most of the chapters which finally appeared in the Report were written in Toronto, drafted and re-drafted before and after almost daily meetings of the Commissioners.[163]

Attendance at the Commissioners' meetings was usually restricted to the Commissioners themselves, Douglas Hartle, John Stewart, and the authors of the draft chapter or special study under discussion. The actual deliberations of the Commissioners were focussed upon the material contained in the draft chapter or special study before them.

Much as Hartle's critique of the Commission's procedures the previous July had asserted,[164] discussion centred only on one particular detail at any one time, such as whether a particular form of revenue or service should be included in income for taxation purposes, or whether a specified class of items should qualify as a valid deduction from taxable income. This consideration of particulars, however, often led the Commissioners into difficulties, disagreements, or uncertainty, edging them away from the particular and into the more general question of an appropriate concept of income for taxation purposes.

The Commissioners did not adopt the comprehensive income concept all at once and from theoretical considerations. Rather it was a slow, almost reluctant realization by one Commissioner after another that no other alternative offered acceptable solutions to the many particular problems discussed in the special studies and draft chapters, and during the long series of Commissioners' meetings.

The Taxation of Capital Gains:

The comprehensive income concept implies, among other things, the inclusion in the tax base of what is commonly called "capital gains", and the Commissioners spent more time on this question than on any other. The special studies: The Taxation of Capital Gains by Geoffrey Conway,[165] and The Law Concerning Capital Gains by Conway and John G. Smith,[166] played an influential role in the Commission's

deliberations. Taken together, the two studies made a compelling case for bringing capital gains into taxable income.

The first of the two studies examined capital gains from an economic standpoint. The existing treatment was shown to be a violation of both equity and logic. As the combined result of court decisions (discussed in the second study) and of Department of National Revenue's reluctance to pursue litigation, gains on securities transactions were generally treated as capital gains and therefore not taxed, while many transactions in real estate bore tax at full progressive rates,[167] a violation of the principle of horizontal equity.[168] Even if the exemption of capital gains were to be administered equally across all types of capital gain, it would still violate the criterion of horizontal equity, since all capital gains, to the same extent as other income, contributed to one's capacity to pay tax. Not to tax capital gains, the study argued, was to discriminate against labour, and other forms of income. Since the distribution of capital gains by income class was found to be highly concentrated among high income earners, the principle of vertical equity was also violated.[169]

The author was prepared to accept the inequities of not taxing capital gains if it could be defended on other grounds, such as that of incentive to save and invest. Even here, however it proved to be both inefficient and unfair, since only those who accumulated wealth through capital gains could take advantage of this incentive. As there was no evidence that saving from untaxed realized gains resulted

in any economic advantage over saving from other sources, an efficient (and equitable) incentive would be indifferent to the source of income from which savings were derived.[170] If a tax incentive to encourage saving were considered desirable, a more general incentive, such as higher exemptions for contributions to retirement savings plans would be a more equitable measure. Total savings, rather than just personal savings, could be stimulated by incentives to business capital investment.[171]

The same argument was then applied to the exemption of capital gains as an incentive to capital investment:

> If incentives are to be provided to increase capital investment by individuals, in a just society such an incentive should be broadly based so as to encourage all individuals to increase their net wealth. Certainly, it does not appear to be a tenet of our society that encouragements to the accumulation of wealth should be granted only to those who already possess such wealth.[172]

Not only was such a narrow investment incentive unfair, but Conway could find no evidence to support the belief that it was particularly effective. His analysis of the effect of a roughly comparable incentive, the introduction of the dividend tax credit for resident owners of Canadian shares in 1949, and its increase to 20 per cent in 1953, indicated that such incentives had little effect on Canadian stock prices and dividend yields. He also showed that, contrary to popular belief, Canadians were just as likely to invest in equities as Americans at the same income level, and attributed the greater American ownership of equity stock to the greater proportion of middle

and upper income-earners in that country.

There was no indication therefore, that Canadians needed an incentive to invest. The most conservative of Canadians in investment behavior were those making in excess of $150,000, the same income class which benefited the most from the tax-exempt status of capital gains. An incentive was therefore not needed, and, where one could argue that it was needed, it was not working.[173] Moreover, as Canadian individual investors, as opposed to institutions, were not a "major dominant force" in Canadian equity markets, moderate tax changes affecting only Canadian individuals, such as including capital gains in income, would likely have only a minor and short-term effect on stock prices.[174]

Conway also pointed out that, in weighing the economic effects of investment tax incentives, one must also consider the effects of the higher taxes required, in the absence of revenue from the taxaton of capital gains, in order to maintain an adequate level of revenue:

> There is another way of examining the situation. This is by contemplating what the net economic effect would be in the United States if capital gains were completely exempted from tax and the revenue loss was recouped by raising the income tax rates in the middle and upper income brackets. It would be difficult to find support for the contention that, as a result, personal savings would be increased and risk investment stimulated, and even those who so argued would be hard pressed to maintain that any marginal gains justified the inequities involved. Yet this is one of the very arguments that would have to be accepted to support a continued exemption for capital gains.[175]

The other economic argument often advanced against taxing capital

gains was that it would reduce the mobility of investment funds, thereby making capital markets less efficient and making it more difficult for new ventures to attract investor support. This could be expected to arise from a situation such as that existing in the United States, where only realized gains were taxed, and a preferential rate applied to long-term gains. Investors could thereby reduce substantially the income tax on their share gains by holding on to them for a longer period, or postpone the tax indefinitely, since capital gains were not subject to income tax when received as gifts or bequests. Conway's examination of studies of investor attitudes and behavior in the United States revealed that there was some evidence to support the view that the rate of disposition of stocks was probably affected somewhat by the six month holding provision: investors tended to hold on to stocks long enough to qualify for the reduced tax rate on capital gains.[176] However, dispositions which resulted in a loss (which would be fully deductible only if realized within six months) tended to increase stock turnover, and Conway concluded that the overall effect was not nearly enough to disrupt the operation of the capital markets.[177] Furthermore, an unpublished study of the Carter Commission on individual tax returns showed Canadian share capital to be somewhat more immobile than in the United States. As Canada did not tax share gains, this could not have been the reason for the observed immobility.[178]

To the extent that capital immobility was a problem in a tax environment such as that of the United States, the answer would have had to lie in taxing all gains at the same rate regardless of length

of time held, and taxing all gains as if realized when ownership was transferred in the form of gifts or bequests.[179] These measures would have greatly reduced the tax incentive for investors to hold on to their securities, allowing market considerations to predominate.

The study also examined other arguments which had been advanced to defend the tax-free status of capital gains, and found each to be untenable. Far from adding administrative complications, it would simplify matters, removing the question of the fine distinction between income and capital gains which had been the source of so much litigation and uncertainty, and also the surplus-stripping problem, since the incentive to distribute corporate profits in the form of share price increases instead of as dividends would be greatly reduced.[180] Conway reminded his readers that much of the complexity of the existing Income Tax Act arose from attempts to prevent these tax avoidance activities and would not be required if all gains were taxed at the same rate.

Conway then addressed the argument that not enough revenue was at stake to make the administrative effort worth while. He argued that revenue considerations were not relevant in any case, since, if each item in the tax base were individually subjected to this revenue criterion there would be nothing left to the tax base. The author then quoted Carl Shoup's demonstration of the absurdity of the not-enough-revenue argument:

> A second fallacy is that, so long as the amount of revenue involved is not very important, there is little

> point to making an effort to solve the problem of taxation to the individual of undistributed profits [which accrue in the form of capital gains]. The nature of this fallacy may be exposed by supposing that some responsible official of the Treasury (say) suggested that complete exemption from the personal income tax should be granted to all individuals with incomes of $1 million or more, on grounds that the impact on the federal revenue would be negligible, and that there would clearly be some saving in administration and compliance cost, not to mention the boost given to incentive to invest. The public would properly be outraged at such a proposal, even though no taxpayer could claim that his own tax burden would be perceptibly increased by the fiscal measures that would be needed to make up the minor loss in revenue. The issue at bottom is an ethical one, and it is so, indeed, largely just because so small a percentage of taxpayers are favoured.[181]

Even though he had argued that revenue yield should not be an important consideration in deciding whether or not to tax capital gains, Conway went to considerable trouble to derive estimates of the expected yield of such an extension of the tax base. Allowing for a number of uncertainties due to the fact that capital gains were not reported in Canada, he arrived at an estimate of close to $1 billion annually of potentially taxable capital gains.[182] Depending upon the specific tax treatment of these gains, and after a transitional period had passed, he estimated that revenues would range between $230 million and $400 million, or between 8 and 13 per cent of personal tax revenues. The addition of capital gains realized by corporations would add about another 20 per cent.[183] Even with capital gains taxed at reduced rates, therefore, potential revenues would exceed $300 million, hardly a negligible amount. This additional revenue could be used to offset the revenue loss from general rate reductions for middle and upper-income taxpayers,[184] which, he argued, would

alleviate any adverse economic effects arising from the taxation of capital gains.

Having presented a strong case for taxing capital gains at the same rate as other income, Conway then addressed the question of the personal tax rate structure. Critics of the existing structure in Canada, Britain, and the United States had been arguing for some time that the upper brackets in the progressive rate structure were too high and had the effect of stifling initiative and economic growth. While rates in the latter two countries had been reduced somewhat, the political difficulties of openly reducing the tax burden on the upper classes had generally encouraged governments to adopt the more subtle strategy of keeping the rates high while narrowing and bending the tax base so that only the effective average rate was lowered.[185] While successful in achieving its immediate purposes, this strategy resulted in the gross inequities outlined in Conway's study and in its companion study, The Law Concerning Capital Gains, the growing scandal of surplus stripping and other tax avoidance devices, and an increasingly complex and arbitrary statutory framework in order to combat these activities.

Within this context, and already having made the case for taxing capital gains, Conway proposed a new strategy:

> If the incidence of capital gains in Canada is even close to that of the United States, it is obvious that our high progressive rate schedule does not represent the actual burden of tax. The question therefore is should the tax base be expanded and the rate schedule lowered, particularly in the upper brackets, to

> accomplish directly what is now managed indirectly? Such an argument might not warrant excessive attention in view of the difficulties involved if all persons were receiving an equal proportion of their income in tax-exempt forms, or even if all persons in similar income classes were receiving approximately the same proportion of tax-free gains. However, neither of these situations now exists, nor are they ever likely to exist. Therefore the use of exclusions from the tax base to reduce the overall tax burden is a very inequitable means of attaining what may well be an acceptable goal.
>
> In any event the taxation of capital gains raises two immediate considerations -- the implications of a new source of revenues that could be used to offset tax reductions in other fields, and the problems of equity and economic effects if the present tax rates were to be imposed on realized capital gains. The question of capital gains cannot be considered in isolation from the balance of the tax system; and, in fact, it is a practical necessity to consider as a package the inclusion of capital gains in the income base and a reduction in the rates of personal income tax in the middle and upper income brackets. Certainly, the latter adjustments -- even if it could be demonstrated that they are desirable from an economic aspect -- would be difficult to support from the point of view of equity and political reality unless a reasonable offset could be simultaneously put forward. The obvious companion proposal is the taxation of capital gains.[186]

Conway's study then concluded with a presentation of alternative reforms to the existing income tax structure as it related to capital gains. The favoured alternative was presented first: "The Broad Concept of Income" which would define income in a manner similar to that of section 61(a) of the United States Code: "all income from whatever source derived", then, for greater certainty, including a list of types of income introduced by a phrase similar to that of the U.S. Code, "including, but not limited to, the following items", among which would be realized increments on the disposition of property.[187] All business gains and gains on non-residential real

property would be included and losses would be fully deductible. Property gains would be taxed at the same rate as other income, on the assumption that rates on middle and upper brackets would be lowered, that a general averaging scheme would reduce the tax burden on fluctuating incomes, and that integration of corporate and personal taxes "would more than offset any adverse economic effect on the demand for Canadian stocks."[188] This alternative, which would bring the income tax system much closer to the comprehensive income concept, was clearly preferred by the author of the study and the one overwhelmingly supported by his analysis.

Conway's other alternatives constituted varying departures from the comprehensive income concept by lessening the burden on gains realized from Canadian securities, and were prefaced with the author's reservations concerning such narrow incentives. Much better would be incentives to saving available to all, such as incentives to retirement savings:

> However, if it is felt that a specific tax incentive is required for stock investment in general and investment in Canadian stocks in particular, then one of the alternatives other than the full taxation of all gains would be appropriate. Inclusion of these alternatives in this study does not necessarily mean that the analysis in the previous chapters supports such alternatives, but rather is a recognition of the fact that the all-inclusive concept of income might not be fully acceptable initially and therefore some part-way measures must be considered.[189]

Conway was telling the Commissioners that there was really only one alternative justified by the evidence: the taxation of capital gains on the same basis as other income.

The Jurisprudence of Capital Gains:

The second of the two companion studies, The Law Concerning Capital Gains,[190] co-authored by Conway and John G. Smith, a young lawyer on the Commission's staff, examined the income tax laws and jurisprudence of the United Kingdom, the United States and of Canada. It focussed upon an anomaly which had been noted by earlier authorities: while much of the language of the Income War Tax Act of 1917, particularly that section defining "income" followed that of the American statute, the Canadian courts followed the jurisprudence of the United Kingdom courts.[191]

Conway and Smith traced the development of English jurisprudence on capital gains which made a careful distinction between income and the source which gave rise to that income, and how this distinction was followed in Canadian decisions. Taxing statutes in both of these countries tended to be very specific and judicial interpretation focussed more on the precise letter of the law than on its purpose or spirit. Tax legislation of the United States, on the other hand, was framed in broad, inclusive terms, and was interpreted by American courts to include capital gains. While the Canadian statute adopted the American form of an all-inclusive phrase defining income, the courts seldom attached any significance to its sweeping character. Instead they tended to base their decisions upon United Kingdom case law, notably on the phrase "adventure or concern in the nature of

trade", which did not even appear in the Canadian statute until the revised Income Tax Act of 1948.[192]

After describing this anomalous situation in some detail the authors concluded:

> In Canada the situation can be over-simplified by saying the courts have approved of, and have therefore adopted, the English judicial approach despite the fact that they are interpreting a non-schedular statute which taxes "income" from all sources and which includes the phrase "undertaking of any kind whatsoever" that would appear to expand further the scope of the Canadian legislation.[193]

The authors acknowledged that the Minister of Finance in 1950, the Honourable D.C. Abbott declared in his Budget Speech of that year that it was not government policy to tax capital gains, provided they were not "profits from carrying on a trade or business", a distinction which he preferred to leave to the courts to make in specific cases.[194]

However, the ~~import~~ of this study was that the courts had failed to adequately discharge that responsibility. The authors reviewed the Canadian jurisprudence concerning capital gains, showing the logical inconsistency and unpredictability in the various decisions. Instead of a steady progress of jurisprudence leading progressively toward greater precision and certainty in the law, the current state of affairs was "...that the taxpayer (and his advisors) is left with no clear guidelines..." and that "...the fortunes of the taxpayer are subjected to the whim of the courts with little indication of what

tomorrow will bring."[195] The policy implications were therefore clear:

> ...although one might find both the statutes and the courts lacking in this area, the only way to correct the situation is to amend the legislation to clearly indicate
> (1) what is, and what is not income, and
> (2) what special treatment is to be accorded to explicitly defined types of income.[196]

The study demonstrated the impossibility of clearly and consistently distinguishing between regular income and gains accruing from appreciation in the value of property. The logical conclusion was clearly that both should be subject to the same income tax. Combined with the first study, by Conway, which examined the economic and administrative arguments for according a tax preference to capital gains, the argument was stronger: both (and perhaps all) forms of income should be treated in the same manner for income tax purposes.

This evidence was persuasive enough to convince the Commission's counsel, John Stewart, that opposition to a capital gains tax could not be justified on grounds of jurisprudence. Up until that point, Stewart had been a strong opponent of taxing capital gains, as all his professional training and instincts had been against it. Once convinced, however, he was instrumental in persuading his close friend, Carter, and then a majority of Commissioners that capital gains should be included in the concept of income.[197]

A Split Decision on Capital Gains:

The meetings from September 3rd to the 10th dealt exclusively with the question of capital gains. In addition to the Commissioners, Hartle, Stewart and Conway were present.[198] Early on the first day, Carter, in referring to Conway and Smith's study of the jurisprudence concerning capital gains, expressed his disturbance at the "setback" introduced by the Irrigation Industries case.[199] He then indicated that he "was satisfied that the law was not clear, and thus the taxpayer cannot be sure of the outcome".[200]

However, there was no easy consensus on the question. Perry wondered what effect a tax on capital gains would have in Canada: "Are Canadians so conservative in investment spheres that a capital gains tax would be a serious block?"[201] A discussion then ensued on the various pros and cons of taxing capital gains, including such considerations as "revenue yield, equity, and administrative feasibility". Walls was not persuaded at this stage, pointing out

> ...that the original purpose of the capital gains tax, according to the Commissioners, was 1) prevent dividend stripping and 2) to catch speculators; and, perhaps the Commissioners should return to consideration of this more limited goal.[202]

The following day, September 9th, marked a major point of decision for the Commission. Stewart gave a brief historical account, following that of Conway and Smith, to explain the different judicial treatment of capital gains in Great Britain and the United

States.[203] The British judiciary, he said, had been recruited largely from the landed classes and interpreted the law in such a way as to protect their class interest as landowners. Increments to capital were thus considered to be distinct from capital and not to be income for tax purposes. He compared this to the United States, which, lacking such a landed aristocracy, made no legal distinction between capital gains and income. Perry, who had published a remarkably similar account in the Canadian Tax Journal eleven years earlier,[204] must have smiled and nodded in agreement. Given the inconsistency of the jurisprudence relating to capital gains, Stewart told the Commissioners that legislation would be "required to obtain real reform", and he warned that the provisions concerning capital gains would have to be very clear in order to overcome the judicial tendency to "treat prior decisions as part of the law".[205]

The discussion of the unsatisfactory state of the jurisprudence on capital gains was decisive in moving a majority of the Commissioners toward the comprehensive income concept. Carter appeared to have accepted the principle by this time. Following Stewart's remarks, Carter pointed to a quotation in an appendix of Conway and Smith's study:

> From the point of view of taxable capacity it is irrelevant whether an increase in spending power occurs as a result of an unexpected windfall, or whether it was expected, planned or achieved in the course of a business organized for the purpose.[206]

Although Conway tried to reassure the Commissioners that the impact of a tax on capital gains would be considerably softened by

generous averaging provisions, Beauvais and Grant had not been won over. Grant expressed opposition, not in terms of any specific disadvantage of the capital gains tax, but as a general value preference:

> ...that tax treatment depended upon the type of state one wished to live in. It depends whether it is thought that a windfall should be treated favourably, for example, if a person likes to gamble without the thought of paying tax.[207]

Beauvais was opposed to a more specific aspect of the capital gains tax proposal, that of deemed realization on transfer of property. This means that property given away, bequeathed, or otherwise transferred without being sold for cash, would be valued by the taxing authority at the current market value, and tax a levied on the net gain in value. Beauvais felt that

> ...deemed realization would constitute a hardship for a closely held company. A tax would have to be paid on a gain which perhaps could not be realized...[and he did not believe that] a tax should be levied until a gain is realized.[208]

To this objection, Carter pointed out that any liquidity problems could be eased by allowing deferred payment, and he

> ...reminded Beauvais that during the hearings, the Commissioners asked for cases in which a closely held company had been forced to liquidate in order to pay taxes. None were presented.[209]

Conway also cautioned Beauvais that one should not assume that the Estate Tax would remain at its current level, implying that, with deemed realization at death, including capital gains in income might

constitute an alternative to the Estate Tax. The Commissioners had not yet reached this conclusion, nor had the proposal even been made explicit, but the idea was in the air. However, the possibility of lowering the rates on the Estate Tax was not sufficient to persuade Beauvais, who countered that any federal action to lower the Estate Tax could possibly be offset by provincial decisions to increase their succession duties.[210]

With Beauvais' dissent noted, the Commissioners recorded their decision:

> 1) Assuming the taxation of capital gains the commissioners agree with Item 2 on page 54 in Appendix I, which favours taxation of net gains. They added that losses should be allowed against other income.
>
> 2) The Commissioners, with the exception of Mr. Beauvais, seemed to agree with item 3 (not to distinguish at this stage between short- and long-term gains, and deem realization on transfer of property.)[211]

In electing not to draw any distinction between assets held for a short period (and presumably for speculative or business purposes) and those held for longer periods (presumably for investment purposes) the Commission was departing from the American system of taxation of capital gains, which taxed long-term gains at a preferential rate, while taxing short-term gains at the same rate as other forms of taxable income.[212]

This departure from the American system was made explicit in the next recorded decision:

> ...that all gains on shortly held and longer held securities be taxed with no distinction in the treatment on the basis of time periods. They are to be treated leniently (with the exception of the trader). An averaging provision will be included.[213]

The exception noted above in parentheses is significant, as it shows that the majority of the Commissioners had still not accepted even some of the more direct consequences of the comprehensive income concept. Had they done so, they would have considered capital gains to be the same as other income regardless of source, whether received as the realization of an investment, or in the course of a business or trade. It illustrates how old habits of thought die hard. The Commissioners had been so accustomed to the idea of taxing traders and professional speculators at the full marginal rate that they failed to notice that retaining this discriminatory feature would deprive them of much of the power and simplicity of the solution which they were on the point of accepting. Only by taxing all gains at the same rate could they avoid the problems outlined by Conway and Smith.

Nor had the Commissioners yet followed all the implications of the principle they had all but accepted. In the field of corporate taxation, for example, where a significant portion of corporate share gains was a reflection of profits retained by the corporation, Carter and Walls suggested that the retained earnings of corporations might be taxed.[214] It is not clear whether they were thinking of this as a method of implementing the principle they had just approved, or as an alternative. At this point Perry proposed "comprehensive taxation at the corporate level with recognition of this at the individual

level",[215] which was both an extension of the principle behind the existing dividend tax credit and also a hint of the proposal finally adopted by the Commission: the integration of corporate and personal taxes. The integration proposal was firmly linked in the Report to the taxation of capital gains at the same rates as all other income.

In response to Carter's request, Conway supplied the Commissioners, Hartle, Stewart and Bennett, with copies of an article dealing with arguments for and against taxing capital gains.[216] The author, himself a partisan of the view that capital gains should be taxed as other income, presented and analyzed the various arguments "from that point of view, but the presentation can be serviceable to one of the opposite persuasion."[217] The author cited and recommended a number of other writings on capital gains on which his compendium was based, but reserved the highest praise for Henry Simons' two volumes, Personal Income Taxation, (1938), ch. 7, and Federal Tax Reform, (1950): "the most persuasive and penetrating analysis of the capital gains issue".[218] In reading this material, the Commissioners encountered the views of Henry Simons, an early advocate of the comprehensive income concept, and also those of specialists Carter and Hartle had met in Washington the year before: Stanley Surrey, Walter Heller, Harold Somers, also Carl Shoup, and others.

While chapters were being drafted, discussed, re-drafted and approved, others were being sent to acknowledged specialists for confidential critical comment. Conway had sent a chapter on the

taxation of capital gains to Pat Thorsteinsson, who could find little amiss in the material, and who advised the authors on matters of emphasis, presentation and strategy.[219] Hartle had sent a number of chapters to Professor Richard Bird, a specialist in public finance and the economics of taxation, for critical comment. On the 12th of January he brought Bird up to date on the Commission's progress:

> The work here is going quite well now. There are only about six of us working on a full-time basis and this is much more productive and a great deal less frustrating. Most of the basic decisions have now been reached (although until the last word has been written it is hard to know how final they are) By and large, the staff is happy with the decisions the Commissioners have reached.[220]

The major battles of principle were over, but not the work of integrating the basic principles throughout all chapters of the Report, resolving inconsistencies, strengthening the presentation, and ironing out some remaining substantive problems. Under the pressure of time, and the small number of people totally immersed in the work, formal procedures went by the board. A note from Stewart on a section of one chapter dealing with capital gains was prefaced with the remark that his comments would be "very general" as "it is clear from the discussions which have occurred that draft chapters of this nature are subject to substantial revision by the Research Staff."[221] Stewart's influence was felt in, among other things, an increased coherence and rigour in the argument for the comprehensive tax base. He wrote to Carter that they should "...demolish the arguments against the taxation of capital gains which were made by the participants."[222]

In the same note, Stewart's comments indicated that some important questions of substance had yet to be settled:

> The general proposition is that all realized gains should be taxed except for specific exclusions and that all losses should be disallowed except as specifically permitted. We also proceed on the basis that capital gains (with the possible exception of capital stock gains) will be taxed in full....[223]

Carter still hoped to get Beauvais and Grant to accept the comprehensive tax base, which may account for the lingering uncertainty regarding the rate of tax on stock gains. At one point, Grant was almost persuaded to accept the concept, at least with the compensating features of reduced rates, and the elimination of the estate tax and succession duties. As he learned more, however, he dissociated himself from it completely and told Carter he would have to write a minority report.[224] While a unanimous Report would have been easier to sell to the Government and to the public, the gap between the majority and minority was too great to be bridged by minor amendments.

While the process of drafting and editing continued, Jack Stewart had to be hospitalized for exhaustion, and asked Stanley Edwards, a senior partner in his firm, to take his place. On joining the small group that remained, Edwards was shocked to learn of the Commission's major recommendations.[225] He was opposed to the inclusion of bequests in income, since the Commission was already recommending deemed realization of assets at death, but this, and most of the other

major decisions, had already been taken. What remained was largely a matter of applying the Commissioners' decisions to a large array of situations. Edwards did, however, manage to exert a residual moderating or conservative influence, toward what he regarded as the "practical".[226] He assisted Conway on the re-drafting and editing of the tax structure chapters, though the two men were far apart on most issues.

Conclusion

In order to get the comprehensive income concept into the Carter Report, a large number of events had to work out the right way. The idea was already available in the published writings of American public finance specialists, beginning with Robert Haig and Henry Simons; hence the label, "Haig-Simons". The idea caught on in the 1950's in the United States, especially among academic public finance specialists and members and supporters of the Democratic Party, and mixed comfortably with Keynesian ideas on fiscal policy which were becoming dominant in the same circles. With the election of John Kennedy, both sets of ideas merged into the new President's tax reform agenda.

The comprehensive income concept found its way to the Commission by three routes. The highest road was through Carter's rubbing shoulders with the men in Washington who, to varying degrees, espoused the idea, or who simply drew his attention to it. Eisenstein's deadly

wit, directed most effectively at the opponents of the comprehensive tax base, must have lingered in Carter's mind. His European tour provided additional stimulus to loosen somewhat his prior attachment to more conservative ideas, and to deepen his skepticism regarding the case for tax incentives and preferences.

The second road was via Hartle, who picked up the idea by reading Richard Musgrave's textbook on public finance. Hartle was suited by training to appreciate the value of the concept, was strategically placed in the organization of the Commission to direct the research activities toward it, and possessed the personal qualities needed to sell it to a majority of the Commissioners.

The third route was through Geoffrey Conway, who was studying the taxation of capital gains before joining the Commission. In Conway, the Commission had an expert in capital gains and a skilled and dedicated propagandist for the comprehensive tax base. Ironically, the young lawyer, John Smith, who did most of the research for the study of the capital gains jurisprudence, had no idea of the magnitude of the influence of his work on the Commissioners' decision to adopt the comprehensive tax base.[227]

Even with three routes into the Commission, the comprehensive income concept came close to falling to one side as just another alternative. Had Gordon won his battle with Carter over the scope of the Commission's research and timetable, or had Hartle not been able to delay production of the Report, or had Stewart not found the

capital gains jurisprudence so convincing, the final Report would have been quite different. As it was, the partisans of the comprehensive income concept had barely succeeded: the Report was the masterpiece that Hartle wanted, and which Carter was proud to have as his monument; but it was late, and only four of six Commissioners supported all the major recommendations.

Notes to Chapter IV

1. Perry interview; Perry, Background of Current Fiscal Problems, (Toronto: Canadian Tax Foundation, 1982), p. 83; Perry, "Anatomy of a Tax System", Proceedings of The Twentieth Tax Conference, (Toronto: Canadian Tax Foundation, 1968.), pp. 12-13.
2. Hartle to Carter, (Research Memorandum to the Chairman - No. 1), RG 33/65, Vol. 112, "Research Memorandum to Chairman/ Chairman's Copies" file.
3. RG 33/65, Vol. 105, "Carter" file, Hartle to Carter, Jan. 30, 1963
4. Ibid.
5. Ibid.; Vol. 104, green binder.
6. Vol. 104, "Hartle" binder.
7. "Part II, "Effects of Taxation", "Outline by Headings of Final Report", Vol. 104, "Hartle" binder.
8. Ibid.
9. Ibid.
10. Ibid.
11. "Questions put to special participants", Mar. 13, 1963, RG 33/65, Vol. 105, "Carter" file.
12. "Report on discussions between Mr. J. Van Hoorn ...and Professor Carl Shoup ...and Members of the Commission", RG 33/65, Vol. 105, "Carter" file.
13. "Memorandum of a meeting held at the house of Kenneth Carter during the evening of Wednesday, November 28, 1962", attended by Carter, Wheatcroft, Perry, Stewart and Hartle, RG 33/65, Vol. 105, "Carter" file; "Meeting at the Seigniory Club, July 10-13, 1964", Vol. 104, "Commission's Decisions" binder.
14. Ibid.
15. "Carter, K. LeM., Notes On Hearings", RG 33/65, Vol. 105, "Carter" file.
16. Ibid..
17. Ibid.
18. RG 33/65, Vol. 105, "Carter ...Notes on Hearings" File; Carter to Hartle, Feb. 27, 1964, Vol. 105, "Carter" file.
19. RG 33/65, Vol. 109, "Notes on a Meeting with Dr. J.R. Petrie", "Petrie" file.
20. Interviews with Perry, Hartle, Conway.
21. Carter, Royal Commission on Taxation/ Discussions by K. LeM. Carter/ Washington and New York", RG 33/65, Vol. 105, "Carter" file; Vol. 112, "Washington and New York/ Visits by Chairman, Mar. 17-27/63" file.
22. Ann Arbor: Institute of Public Administration, University of Michigan.
23. "Royal Commission on Taxation/ Discussions by K. LeM. Carter/ Washington and New York", Vol. 105, "Carter" file. Musgrave, one of the leading public finance specialists, was being sought (unsuccessfully) by Hartle to join the staff of the Royal Commission.
24. Ibid.
25. Ibid.
26. Ibid.

27. Ibid.
28. Ibid. Among Pechman's publications was "What Would a Comprehensive Income Tax Yield?", in Tax Revision Compendium on Broadening the Tax Base, Submitted to the House Committee on Ways and Means, (Washington, D.C., 1959).
29. Carter, "...Discussions by K. Lem. Carter/ Washington and New York", Vol. 105, "Carter" file.
30. Ibid.
31. Sauer was probably referring to Galbraith's The Affluent Society.
32. Carter, "...Discussions by K. LeM. Carter/ Washington and New York", Vol. 105, "Carter" file.
33. "...Discussions by K. LeM. Carter/ Washington and New York", Vol. 105, "Carter" file.
34. John Due to Hartle, May 7, 1963, RG 33/65, Vol. 108, "National Bureau-Brookings Institution" file.
35. Hartle interview.
36. Only 44 participants had been invited, and Hartle was not even able to secure an invitation for his Co-ordinator of Economic Research, Duncan McDougall. The only other Canadian invited was Ronald Robertson, Director of the Canadian Tax Foundation. Due to Hartle, Oct. 7, 1963, and Due, "Memorandum to participants...", Oct. 3, 1963, "National Bureau-Brookings Institution" file.
37. Carter to Hartle, cc. Bennett, Perry, June 13, 1963, RG 33/65, Vol. 105, "Carter" file. Eisenstein cites Federal Tax Policy for Economic Growth and Stability, Joint Committee on the Economic Report, 84th Congress, 1st Session, (pp. 96, 98, 102).
38. Ibid.
39. RG 33/65, Vol. 105, "Carter" file.
40. Eisenstein, The Ideologies of Taxation, (New York: The Ronald Press, 1961), p. 11.
41. Ibid.
42. Ibid., p. 104.
43. Ibid., pp. 147-148.
44. Ibid., p. 105.
45. Ibid., p. 149.
46. Ibid., p. 166.
47. Ibid., p. 177.
48. Ibid., p. 230.
49. Ibid., pp. 13-14.
50. Ibid., p. 206.
51. Ibid., p. 209.
52. Ibid., p. 208.
53. Ibid., p. 215.
54. Ibid., p. 230.
55. Ibid., p. 227.
56. Hartle, correspondence with the author, Dec. 30, 1982.
57. G.M. Roy to Hartle, Sept. 25, 1963, and Carter's notes, attached, RG 33/65, Vol. 105, "Carter" file; "Notes on European Visit of K. LeM. Carter and J. H. Perry, September, 1963" binder, Vol. 112.
58. Ibid., pp. 1-4.
59. Ibid., p. 1.
60. Ibid., p. 8.

61. Ibid., p. 7.
62. Ibid., p. 14.
63. Ibid., p. 11.
64. Ibid., pp. 19-26.
65. Carter to Hartle, October 3, 1963, RG 33/65, Vol. 105, "Carter" file. Smith's ideas were available to the Commission in published form: Federal Tax Reform: The Issues and Prospects (New York/Toronto/London: McGraw-Hill, 1961).
66. Carter to Hartle, Oct. 3, 1963, RG33/65, Vol. 105, p. 26.
67. Ibid.
68. Ibid., p. 27.
69. Ibid.
70. Ibid.
71. Ibid.
72. Ibid., p. 30.
73. Ibid., p. 32.
74. Ibid.
75. Ibid.
76. Ibid., p. 30.
77. Ibid., p. 39.
78. Ibid.
79. Ibid.
80. "Meeting with the Honourable Walter Gordon... May 27, 1963, at 4:00 P.M.", (draft) RG 33/65, Vol. 105, "Carter" file. While Claude Isbister did not recall this meeting, its substance was confirmed by Professor Hartle, in correspondence with the author, Dec. 30, 1982, and by Mr. Gordon, Sept. 16, 1982.
81. Ibid.; The Commission had requested $1,351,800 for 1963-64 from the previous government, which had been cut to $981,800. Carter had notified Bryce, and later requested of Pearson, that an amount of $350,000 be included in the Supplementary Estimates to restore the original level of financial support. Carter to Bryce, Jan. 31, 1963; Carter to Pearson, May 9, 1963, "Carter" file.
82. Ibid.
83. Ibid.
84. "Appendix "B" to Minutes of the Fourth Meeting of Commissioners", "Memorandum of a Meeting in the Offices of the Commission, on Tuesday, May 28, 1963." by Carter, RG 33/65, Vol. 112, "Meeting - May 28/63, Minutes" file.
85. Ibid.
86. Carter to Gordon, May 29, 1963, Vol. 105, "Carter" file.
87. Ibid.
88. Ibid.
89. Ibid.
90. Ibid.
91. "Excerpt from a Letter to Mr. Carter from the Minister of Finance, Mr. Walter L. Gordon, Dated May 30th, 1963", Vol. 105, "Carter" file.
92. "Minutes of the 1st Meeting of the Corporate Tax Committee at 10 a.m. June 10th in Room 1006", RG 33/65, Vol. 105, "Dobson" file.
93. Ibid.
94. Carter to Hartle, April 4, 1963, RG 33/65, Vol. 105, "Carter"

file.

95. Hartle to Carter, April 14, 1963, "The Proposal to solve surplus-stripping problem", Vol. 105, "Carter" file.
96. Hartle was and is convinced that Carter did favour the proposals. Correspondence with the author, Dec. 30, 1982.
97. Carter to Hartle, April 4, 1963, Op. cit.
98. Hartle to Carter, June 18, 1963, Vol. 105, "Carter" file.
99. Interview with G.R. Conway, July 16, 1982.
100. Hartle, correspondence with the author, Dec. 30, 1982
101. G.R. Conway, "capital gains method", Oct 15, 1963, RG 33/65, Vol. 113, "Preliminary Report to the Minister of Finance" file.
102. Stewart to Hartle, Oct. 28, 1963, RG33/65, Vol. 113, "Preliminary Report to the Minister of Finance" File. Stewart considered it "doubtful" that they "could deal finally with surplus stripping without determining whether and to what extent capital gains should be taxed", to which someone had pencilled in, "agreed Cap Gains at full personal rates".
103. Hartle to Carter, Dec. 2, 1963, Vol. 105, "Carter" file; Hartle, correspondence with the author, Dec. 30, 1982.
104. Carter to Hartle, Oct. 29, 1963, "Re Conversation with the Honourable Walter Gordon, this date", Vol. 105, "Carter" file.
105. Ibid.
106. Hartle to Carter, Nov. 29, 1963, Vol. 105, "Carter" file.
107. The study was subsequently published along with a number of other studies undertaken by or for the Commission. Further references are to the published version: (Ottawa: Queen's Printer, 1967).
108. Ibid., pp. v, 10.
109. Ibid., p. 10.
110. Ibid., p. 10.
111. Ibid., p. 11.
112. Ibid., pp. 11-13.
113. Ibid., p. 13.
114. Carter to All Commissioners, Jan. 31, 1964, Vol. 105, "Carter" file.
115. Ibid.
116. Ibid.
117. "Meeting with Messrs. Hartle and Perry..." notes taken by Carter, cc. Perry and Hartle, Jan. 31, 1964, Vol. 105, "Confidential" file.
118. Ibid.
119. Carter to Gordon, "second draft", marked "revised", (not signed) stamped "Royal Commission on Taxation, Feb. 12, 1964.", Vol. 105, "Carter" file.
120. Ibid.
121. "Memorandum to the Chairman and the Commissioners, Addendum to Secretary's Memo of Feb. 12 on Commission's Report", Feb. 13, 1964, "Carter" file.
122. Ibid.
123. Bennett to Commissioners, Feb. 12, 1964, "Re: Commission's Report to Government", Vol. 105, "Carter" file.
124. Hartle, "Memorandum to the Chairman...", Feb. 12, 1964.
125. Bennett to File, Feb. 25, 1964, "Memoranda for Prof. Hartle from

Staff" file.

126. Ibid.
127. Ibid.
128. Gordon to Carter, (c. end of March, 1964), quoted in Bennett to Bryce, April 6, 1964, Vol. 108, "Memoranda to Prof. Hartle from Staff" file.
129. Hartle, in correspondence with the author, Dec. 30, 1982.
130. (Ottawa: Queen's Printer, 1969). The formation and operation of the task force, the "Tax Analysis Unit" is discussed below in Chapter 6, the White Paper, in Chapter 7.
131. Vol. 104, "Basic Tax Structure Alternatives" file.
132. Memorandum by Hartle, McDougall, Fields, Thompson and Goodlet, April 7, 1964, Vol. 104, "Basic Tax Structure Alternatives" file.
133. Ibid.
134. Ibid.
135. Ibid.
136. Ibid.; although the document did not include a specific reference, the source was probably Richard Musgrave, The Theory of Public Finance, a Study in Public Economy (New York, Toronto, London : McGraw-Hill Book Co., 1959), pp. 164-165.
137. Ibid.
138. Ibid.
139. Ibid.
140. Ibid.
141. Ibid.
142. Ibid.
143. "Timetable", Hartle to Co-ordinators and Supervisors, Mar. 2, 1964, "Professor D.G. Hartle" black binder, Vol. 104; Bennett to Commissioners, April 9, 1964, Vol. 104.
144. "Timetable", Hartle to Co-ordinators and Supervisors",Mar. 2, 1964; Bennett, "Memorandum to Commissioners", April 9, 1964, Vol. 104, "Professor D.G. Hartle" black binder.
145. Hartle to Brazer, June 18, 1964, Vol. 104, "Brazer" file.
146. Hartle, correspondence with the author, Dec. 30, 1982.
147. Brazer to Bennett, June 25, 1964, Vol. 104, "Brazer, Prof. Harvey" file. Bennett sent a copy of Brazer's letter, with an acknowledgement by Bennett, to Carter and Hartle.
148. Hartle to Carter, July 2, 1964, "The Need for Additional Time", Vol. 105, "Confidential" file.
149. Ibid.
150. Ibid.
151. Ibid.
152. Ibid.
153. Ibid. The quotation follows the pencilled revisions. Here, the original read: "Battles with administration, whether based on real or imagined complaints...."
154. Ibid.
155. Ibid.
156. Hartle to Carter, July 2, 1964, Vol. 105, "Confidential" file.
157. RG33/65, Vol 104, "Commissioners' Decisions" file.
158. "Some Notes on Meeting at the Seigniory Club, P.Q., July 10-13, 1964", Carter to Perry, Stewart, Hartle, July 15, 1964, Vol. 104, "Commission's Decisions" binder.

159. Hartle's copy is marked in pencil in the margin down to this point.
160. This part is marked in pencil in the margin of Hartle's copy.
161. Ibid.
162. As Hartle later recalled: "I was being 'humoured' and had not yet convinced them to bite the bullet", (correspondence with the author, Dec. 30, 1982).
163. Hartle, correspondence with the author, Dec. 30, 1982.
164. See above, p. 242.
165. Royal Commission on Taxation, Study Number 19A, (Ottawa, Queen's Printer, 1968).
166. RCT Study Number 19B, (Ottawa: Queen's Printer, 1967).
167. Conway, p. 2.
168. Ibid., p. 63.
169. Ibid. Since capital gains did not have to be reported under Canadian tax legislation, inferences were made using a combination of United States and Canadian data. For American taxpayers with adjusted gross incomes over $200,000 the average net capital gains amounted to about half of total reported income. This small group of taxpayers, less than 0.1 per cent of those United States residents filing returns, accounted for 22.5 per cent of total reported capital gains in 1964. Ibid., pp. 115 and 96.
170. Ibid., pp. 18, 286.
171. Ibid., p. 328.
172. Conway and Smith, p. 18.
173. Ibid., p. 300.
174. Ibid., pp. 290-305, 325.
175. Ibid., p. 327.
176. Ibid., pp. 312-319.
177. Ibid., pp. 312, 319.
178. Ibid., p. 315.
179. Ibid., pp. 309, 329.
180. Ibid., p. 243. If gains were taxed on realization or on death rather than as accrued, there would still remain a residual incentive, since the tax could be postponed.
181. Ibid., p. 255, quoted from Carl S. Shoup, Federal Tax Policy for Economic Growth and Stability, p. 398.
182. Conway, pp. 273-275.
183. Ibid., pp. 277-278.
184. Ibid., pp. 278, 281.
185. See the remarks of Claude Isbister to the Commissioners, above, Ch. 3, pp. 152-3.
186. Ibid., pp. 334-335.
187. Ibid., p. 339
188. Ibid. p. 341.
189. Ibid., p. 337
190. (Ottawa: Queen's Printer, 1967).
191. S.C. 1917, Ch. 28, later R.S.C. 1927, Ch. 97 and amendments thereto; cited in Conway and Smith, p. 88; the authors also quoted a passage from J. Harvey Perry, Taxation in Canada, 3rd ed., (Toronto: University of Toronto Press, 1961), p. 45 in support of this.

192. Conway and Smith, p. 90.
193. Ibid., p. 96
194. House of Commons Debates, March 28, 1950, p. 12; cited in Conway and Smith, p. 97.
195. Ibid., p. 118.
196. Ibid., p. 97.
197. Hartle interview.
198. Vol. 104, "Commission's Decisions" file.
199. Ibid.; See above, Ch. 2, pp. 98-100.
200. Vol. 104, "Commission's Decisions" file.
201. Ibid., Sept. 8, 1964.
202. Ibid.
203. Ibid., Sept. 9, 1964.
204. "Capital Gains: The British Point of View", Canadian Tax Journal, Vol. 1, No. 6 (Nov.-Dec., 1953), pp. 548-561.
205. Vol. 104, "Commission's Decisions" file.
206. Ibid.; Carter referred to pages 50-51 in Appendix I.
207. Ibid.
208. Ibid.
209. Ibid.
210. Ibid.
211. Ibid.
212. Of course, the system then in force in Canada also differed from that of the United States, but in the opposite direction: capital gains were exempt unless they were judged to be part of the stock in trade of a business, in which case they were taxed at the same rate as other income.
213. Ibid.
214. Ibid.
215. Ibid.
216. Conway to Carter, et. al., Sept. 11, 1964, Vol. 105, "Conway" file. The "article" was a photocopy of a section of Ch. 5 of a textbook, although no citation was given.
217. Ibid.
218. Other recommended sources were: Seltzer, The Nature and Tax Treatment of Capital Gains and Losses, (1951); United States Treasury Department, Federal Income Tax Treatment of Capital Gains and Losses, (1951); Vickrey, Agenda for Progressive Taxation, (1947), Ch. 5; Somers, "An Economic Analysis of the Capital Gains Tax", 1 National Tax Journal, 226 (1948); Blum and Kalven, The Uneasy Case for Progressive Taxation, (1953); Surrey, "Definitional Problems in Capital Gain Taxation", 59 Harvard Law Review 985 (1956); Blum, "Simplification of the Federal Income Tax Law", 10 Tax Law Review 239 (1955); Miller, "Capital Gains Taxation of the Fruits of Personal Effort: Before and After the 1954 Code", 64 Yale Law Journal 1 (1954); Blum, "How the Growth of Favoured Tax Treatments Affects Taxpayers and Practitioners", Journal of Taxation 28 (1956); and Shoup, "The Dividend Exclusion and Credit in the Revenue Code of..." 8 National Tax Journal 136 (1955).
219. Smith to Conway, "Re: Concept of Income", Oct. 16, 1964, Vol. 105, "Conway" file.
220. Hartle to Bird, Jan. 12, 1965, Vol. 104, "Bird, R." file.

requirements.[16] The Commission therefore derived, not only the principle of progressive taxation, but also an initial graduated rate schedule from the principle of ability to pay.

The concept of equity in taxation was linked in the Report to the vision of an equitable society. The genuinely progressive (rather than the simply nominally progressive existing system) tax system they recommended, when "combined with a progressive transfer expenditure system that provided relatively greater benefits to low income families and individuals"[17] would mean that the net benefits from government activities would be greater the lower the income of the tax unit:

> These results are as they should be in a society committed to providing greater equality of opportunity and improving the well-being of those who have the least economic power.[18]

At the lowest end of the income spectrum, however, the progressivity of the income tax constructed according to ability to pay would be out-weighed by the regressive effects of property and sales taxes. The Commissioners acknowledged this, and pointed out that, "ideally", taxpayers should be given a refundable credit for sales and property taxes consistent with a progressive rate structure applied to the comprehensive tax base. However, they declined to recommend this system, for, "to do so would be to recommend, in effect, the adoption of a negative income tax...."[19] The Commission preferred that this be considered within the context of a review of the entire system of transfer payments, which it found to be

221. Stewart to Carter, cc. Perry, Hartle, March 31, 1965, Vol. 143, File 80-5 "Commission reports / Commissioners' Final Report"
222. Ibid.
223. Ibid.
224. Interview with Donald G. Grant, Halifax, Dec. 3, 1983.
225. Interview with Stanley E. Edwards, Toronto, Nov. 22, 1982.
226. Ibid.
227. Interview with John G. Smith, Toronto, Nov. 22, 1982.

Chapter V: The Carter Report

Introduction;

The Report of the Royal Commission on Taxation was never published in type-set form. The public was presented instead the same 2,575 typed pages, in six, plastic-bound volumes as had been made available to the government. The printing quality was uneven, with some pages barely legible. Opponents of the Commission's recommendations could already have guessed that the Report was a political orphan.

On the front page of each volume, readers were offered the apology:

> This edition of the Report had been produced in limited quantity. As soon as possible another edition will be available for general distribution.

The new edition never appeared. The Carter Report, now out of print, remains an underground classic. Although the awkward bulk and forbidding appearance of the Report would make it unlikely to be popular reading material for commuters on their way to the office, the style of the text itself was aimed at the educated layman who knew little about the tax system beyond that required to face his annual income tax return.

The first volume contained an "Introduction" and brief summary of

the major recommendations, as well as acknowledgements and the minority reports of Commissioners Beauvais and Grant. The "Introduction" began with a re-statement of the terms of reference, followed by seven "conclusions" which the Report acknowledged "constitute a severe criticism of the present tax system."[1] Canadians were being taxed inequitably, and were less well off than they would otherwise have been due to the economic inefficiencies resulting from the tax system. Nor was the system being used to good advantage for achieving social and economic goals; its administration was not as efficient, nor as free from political interference as it ought to be; procedures for the formation and review of tax policy were "inadequate"; and judicial appeal procedures were "deficient and require reform".[2]

In considering the objectives of a good tax system, the Commissioners decided that Canadians wanted "equity, more goods and services, full employment without inflation, a free society and a strong, independent federation." Obviously, trade-offs were necessary, and the Commissioners had "...consistently given the greatest weight to the equity objective".[3] If equity, or fairness, were not so important, taxes would not be required, as "[t]he state could simply commandeer what it needed."[4] Aside from the concern with the intrinsic value of the fair treatment of individuals, equity was essential for the safety of the state:

> The first and most essential purpose of taxation is to share the burden of the state fairly among individuals and families. Unless the allocation is fair, the social and political fabric of a country is weakened and can be

> destroyed. History has many examples of the severe consequences of unfair taxation.[5]

Equity, the Report explained, had two "dimensions", horizontal and vertical. Horizontal equity was satisfied when individuals in similar circumstances bore the same tax burden. Vertical equity required that individuals and families in different circumstances bore "appropriately different" tax burdens. Here the Commissioners admitted that the exact meaning of vertical equity was a matter of belief: "We can do no more than recommend what we believe to be fair."[6] They believed that the universal yardstick ought to be the amount of discretionary economic power available to each tax unit, that is, the "residual power to command goods and services for personal use after providing the 'necessities' of life and after meeting family obligations and responsibilities."[7] This concept was refined slightly in Volume 3, where discretionary economic power was defined as "the product of the tax unit's total economic power and the fraction of the total economic power available for the discretionary use of the unit."[8] The latter term is "the proportion of the unit's total economic power that does not have to be exercised to maintain the members of the unit."[9] Maintenance meant, not physical subsistence, but "the provision of services necessary to maintain the appropriate standard of living... [of one unit] relative to others."[10]

The Commission understood horizontal equity to mean therefore that persons or families having the same amount of discretionary economic power should pay the same tax, while vertical equity implied that

persons and families pay taxes in proportion to their discretionary economic power.[11] This was the single principle on which the entire six volume Report is based: the equity yardstick of one's ability to pay, a criterión discussed in writings on public finance, from Aristotle to Musgrave.

The Comprehensive Tax Base

In Volume 1, the Commissioners derived four additional principles from the central equity principle to guide their other recommendations for a reformed taxation system:

1. The family, that is, parents and dependent children, should be the basic unit for tax purposes, and therefore intra-family transactions and transfers should not have any tax consequences.
2. All tax units should be taxed according to the annual net change in their economic power, regardless of what form it may take. This is the "comprehensive tax base."
3. The comprehensive income base should be subject to progressive rates of tax, to reflect the diminishing proportion of non-discretionary expenses as income rises.
4. As some units experience unusually heavy non-discretionary expenses, their tax burdens should be reduced accordingly, either by a separate rate schedule or by tax credits.[12]

The more detailed discussion in Volume 3, Chapter 7, listed five "fundamental principles", the first being the family unit, and the others:

> 2. Taxes should be allocated among tax units in proportion to ability to pay....
> 3. The ability to pay of a tax unit should be assumed to be proportionate to its discretionary income....
> 4. The discretionary income of a tax unit should be assumed to be equal to the total income of the unit multiplied by the fraction of that income available for the discretionary use of the unit.
> 5. It should be assumed that, other things being equal, the greater the income of a tax unit the larger will be the fraction of that income available for discretionary use.[13]

The Commissioners believed that non-discretionary expenses rose with income, but not in the same proportion as income, and therefore, that principle number five held true.[14] Above an income of $100,000, the Commissioners assumed that all additional income to be discretionary, and below that level, that "equal proportional differences in income... [were] associated with equal absolute differences in the fraction of income available for discretionary use."[15] Since the tax burden should be apportioned according to ability to pay, that is, in proportion to discretionary economic power, it followed that the rate schedule should be proportional when applied to discretionary income and progressive when applied to total income. Income brackets should therefore contain equal percentage differences in income, and the marginal rate should rise by an equal amount with each bracket. The Commissioners set the top marginal rate at $100,000, above which the marginal rate was the rate of tax on discretionary income, which could be determined by revenue

requirements.[16] The Commission therefore derived, not only the principle of progressive taxation, but also an initial graduated rate schedule from the principle of ability to pay.

The concept of equity in taxation was linked in the Report to the vision of an equitable society. The genuinely progressive (rather than the simply nominally progressive existing system) tax system they recommended, when "combined with a progressive transfer expenditure system that provided relatively greater benefits to low income families and individuals"[17] would mean that the net benefits from government activities would be greater the lower the income of the tax unit:

> These results are as they should be in a society committed to providing greater equality of opportunity and improving the well-being of those who have the least economic power.[18]

At the lowest end of the income spectrum, however, the progressivity of the income tax constructed according to ability to pay would be out-weighed by the regressive effects of property and sales taxes. The Commissioners acknowledged this, and pointed out that, "ideally", taxpayers should be given a refundable credit for sales and property taxes consistent with a progressive rate structure applied to the comprehensive tax base. However, they declined to recommend this system, for, "to do so would be to recommend, in effect, the adoption of a negative income tax...."[19] The Commission preferred that this be considered within the context of a review of the entire system of transfer payments, which it found to be

"cumbersome and... [with] important gaps and... some overlapping."[20] Yet the chief reason for not recommending the inclusion of refundable credits was an economic one:

> It must be recognized that the full integration of these taxes would require a dramatic increase in marginal rates. These higher rates might have substantial disincentive effects that would have to be weighed against the improvement in equity that would be attained.[21]

This was an important departure from the application of the principles of equity and ability to pay, which were traded off here against an assumed gain in economic growth. The Commissioners took what they call a "middle ground" position by suggesting the relative weight of sales and property taxes be gradually reduced, by compensating for the regressive incidence of sales taxes, and by implementing their recommendations on the income tax. Canada could thereby "move closer to the objective of allocating taxes according to ability to pay."[22] The Report was intended as a "start", and either an increase in the width of the zero brackets, or a system of refundable tax credits would "be consistent with [their] ...basic approach." The latter "...would represent the natural evolution of the tax system we are proposing."[23]

A second departure from the ability to pay principle was the Commission's proposal for a top marginal rate not exceeding 50 per cent. This was done largely for fear of hindering the economic incentives to work and invest, and also to enable the top personal rate to equal or be close to the top corporate rate of 50 per cent, in

order to integrate personal and corporate taxes. The corporate rate could not greatly exceed this figure, the Commissioners believed, because of the free mobility of corporate investment capital between national jurisdictions, or, as the Report expressed it, "because of the depressing effects on domestic investment and because of the international ramifications."[24] If a greater degree of progressiveness were desired in the tax system, the Commissioners would have preferred to add a net worth tax to the income tax system, though they were not actually recommending such a tax.[25]

Further discussion regarding the constraints for the recommended rate schedule in Chapter 11 added the objective of reducing the weight of taxes on middle income tax units "to narrow the unfavourable income tax differential between Canada and the United States"[26], specified the constraint contained in the Commission's terms of reference, that the recommended system raise approximately the same revenue as the existing system, and added the constraint that, aside from the elimination of "inefficient concessions" to certain industries, "the weight of taxation on equity investments should be no greater than at present, despite the widening of the tax base to include capital gains."[27] The latter constraint was accepted in order to eliminate any adverse effect on saving from corporate-source income as a result of the taxation of capital gains.[28]

As a means of measuring taxpayers' economic power, the Report proposed measuring all changes in economic power over the year, expressing it as the sum of the tax unit's consumption, gifts

received, and the net change in assets, each expressed in terms of its market value.[29] This, the Report called the "comprehensive tax base":

> The distinction between wages, interest, dividends, business income, gains on shares, bequests, sweepstake winnings, and so on, all would disappear. Because it encompasses more than the present tax base, we have called our new concept the 'comprehensive tax base'.[30]

The authors acknowledged that this concept was "a modification of the definition of income advocated by Henry Simon[s], ...following the definition of R.M. Haig.[31]

In order to make compliance and enforcement of a tax system based on this concept feasible, the Commissioners reformulated the concept into one of "net gains", which would include all net gains received in cash, as personal services or benefits in kind, gifts and bequests, "imputed income", that is benefits derived from the ownership of assets which could have been rented to others, and net gains in the market value of property rights (the old-fashioned "capital gain"). By net gain, the Commissioners meant that "all expenses reasonably incurred to earn gains, other than personal living expenses" and gifts to other tax units, would be deductible.[32]

Considerations of administrative simplicity again led to some departures from the net gains concept. The Commissioners conceded that imputed income, where the services provided were of benefit to oneself, presented "serious valuation problems" which prevented the inclusion of most of them in the comprehensive tax base.[33] By the

same token, although their equity principle called for the taxing of capital gains on accrual, valuation problems in cases where property was unique and infrequently traded made this administratively impractical. Accordingly, they recommended that gains in property values be taxed only on "realization", which was defined to include virtually any transaction or transfer outside the tax unit, including gifts and bequests to other than spouses and dependent children.[34] They recognized that taxing gains on realization allowed a tax deferment and hence a substantial advantage to those tax units who could take advantage of it, and therefore they made the definition of "realization" as broad as possible. Nevertheless, the opportunities for deferment of tax arising from the failure to tax accrued property gains required the taxation of the income of economic intermediaries, such as corporations, trusts and co-operatives, since the income from those sources could otherwise escape taxation for very long periods.

Proposed Treatment of Personal Income

Inclusions in Personal Income:

The Commission's application of the net gains concept to the various sources of personal income would have included the following receipts in the tax base:

1. Employment income: all wages, salaries, bonuses, gratuities, the market value of specified deemed benefits received from an

employer, stock option benefits, allowances, employer contributions to non-registered pension plans, hospital and medical premiums paid by the employer on behalf of the employee, the employer's cost of free or subsidized goods and services provided for the employee, fees and dues paid by the employer on behalf of the employee, and travel and entertainment expenses beyond specified limits paid by the employer.[35]

2. Strike pay.[36]

3. Property Income: all income derived from holding property, such as rent and interest, dividends, royalties which was already subject to tax; plus all net gains on the disposition of all forms of property, including personal property, securities and real estate.[37] Gains would be taxed as "realized", that is when sold, or when a disposition had been deemed to have taken place. The latter would include exchanges, gifts, bequests, loss, or when the taxpayer ceased to be a Canadian resident, and would be taken to be at fair market value.[38] No property transferred within the tax unit, that is between spouses, or to dependent children, would be a disposition for tax purposes.[39] Gains from certain specified involuntary dispositions would not be taxable if the proceeds were re-invested in a similar asset within a specified period.[40] Nor would a disposition be deemed to have taken place in the case of business reorganizations where the beneficial ownership did not change.[41] There would be a $25,000 lifetime exemption for gains on the sale of a

taxpayer's residence.

4. Pension income, with full deduction of registered pension contributions up to the equivalent of a single life annuity of $12,000 a year, payable at age 65 with a ten-year guarantee.[42]
5. Income insurance benefits, including Government Unemployment Insurance, with premiums being deductible.[43]
6. Participating dividends from life insurance policies and investment income in the hands of the insurer attributable to the policy-holder.[44]
7. Gifts and bequests outside the family unit in excess of a lifetime exemption of $5,000 and smaller annual exemptions, with the corollary that the existing estate and gift taxes be repealed.[45]
8. All government transfer payments, on the understanding that each program and level of benefit would be reviewed and increased if necessary, before implementation.[46]
9. Gambling gains and windfalls, with limited deduction for gambling losses.[47]
10. Cancellation or forgiveness of debts.[48]

Deductions and Allowances:

Generally, only costs and losses reasonably attributable to the earning of taxable income would be deductible. Any costs or losses of a personal nature, that is, those attributable to personal

consumption, would not be deductible. However, an exception was made for losses on personal property, which could be deducted from gains on the disposition of similar property in the preceding two years, or in any subsequent year.[49]

Since the Commission was proposing to tax individuals and families in proportion to their discretionary incomes, they were prepared to exempt from income certain non-discretionary expenses, such as out-of-pocket medical expenses in excess of 3 per cent of income, as provided for in the existing system[50], and tax credits to offset against gifts to close relatives.[51]

A departure from the comprehensive income concept was the recommended continuation of deductions for charitable donations. A rigorous application of the net gains principle would have required inclusion of all donations in taxable income, since they were really gifts. However, the Commission was prepared to permit certain "concessionary allowances" which "serve a useful social purpose and, as a matter of public policy, should be encouraged."[52] Allowances "must be judged primarily in terms of their effectiveness in bringing about the desired result with the minimum departure from ability-to-pay principles.[53] While acknowledging that equity considerations indicated a tax credit for charitable donations, the Commissioners opted for a continuation of the deduction from income in order not to "stifle charitable giving by upper income individuals and families."[54] The Report also recommended tax credits to support post-secondary education, and deductions for other training which was

related to the earning of income.[55]

Income Averaging:

The taxation of gifts, bequests and realized capital gains, including deemed realizations, would have greatly increased the number of taxpayers with "lumpy" income in particular years. Because it would have been inequitable to tax fluctuating incomes at progressive rates, the Commission proposed two methods of income averaging be available to Canadian residents. "Block averaging" would permit the averaging of income over five years.[56] Taxpayers could also elect to deposit large sums in "Income Adjustment Accounts", which would be non-interest-bearing, non-transferable and non-negotiable accounts administered by the Government. Amounts deposited would not be taxable until the time of withdrawal, at which point the amount withdrawn would be included in income for that year.[57] In addition, non-taxable contributions could, subject to specified limits, be made to Registered Retirement Income Plans.[58]

Proposed Treatment of Intermediaries

The Commissioners conceived of corporations, trusts, co-operatives, and other organizations, as intermediaries, or conduits for the flow of income to individuals. Organizations do not have tax-paying capacity according to the Commission's definition: "for

us, tax-paying capacity arises from discretionary economic power, and intermediaries cannot have discretionary economic power -- the residual power to command goods and services for personal use. Consumption is a strictly human trait."[59] Since the income of organizations eventually benefits specific individuals, the Commission proposed the taxation of organizations as a convenient collection device, while allocating the taxes paid by the organization to the appropriate resident individuals. This was made necessary in the case of Canadian residents by the possibilities for deferment of taxes consequent on the recommendation not to tax property gains as accrued. The intermediaries would be taxed at the top marginal rate, with provision for a refundable tax credit to the persons to whom the income had been allocated, to bring their personal tax payable in line with their personal marginal rate. This would ensure that the burden of income taxes levied on organizations were born by resident individuals according to their ability to pay.[60]

The Commission saw their net gains concept, amended to exclude accrued capital gains and to include the integration of corporate and personal income, as the keystone, which, once in place, supported the whole edifice of an equitable, efficient, and almost unavoidable tax system:

> These proposals should substantially eliminate most of the avenues for personal income tax deferment by Canadians. Although deferment would still be possible in the form of unrealized property gains, many of the difficulties and inequities associated with the present system would disappear. The split rate of corporate income tax, with its attendant problems in dealing with associated corporations, would be eliminated, and the

> many procedures for minimizing personal tax on the distribution of corporate surplus would also become inapplicable. Differences in the tax treatment of various kinds of intermediaries would largely cease so that sole proprietors, partnerships, corporations and co-operatives would all be taxed in a similar fashion. Similarly, various industries would all be taxed on a similar basis; and the taxation of investment income, regardless of the form in which it was received, or the intermediary through whom it was received, would be uniform. The after-tax rates of return on different kinds of assets and from different kinds of economic activities would be subject to essentially the same tax burden, and would not be taxed at a variety of rates; much of the uncertainty and complexity of the present system would disappear; competitive inequalities between kinds of business, forms of organization, and forms of saving would be substantially eliminated; and the overall equity of the tax system would be immeasurably improved.[61]

For anyone familiar with the problems of the Canadian taxation system in the 1960's, these would have been understood as audacious claims indeed. The bulk of the Report was devoted to an analysis of the problems of the existing system, and an application of the comprehensive tax base to each to produce a list of conclusions and recommendations.

Corporate Income:

One of the most complex areas was the tax treatment of corporate income. Some of the most sophisticated tax avoidance techniques had made use of the corporate form of organization, such as the surplus-stripping schemes, and the use of associated corporations to qualify for the "small business rate" of 21 per cent on the first $35,000 of corporate income.

The Commissioners proposed that corporations be taxed on their profits, in order to minimize postponement of tax resulting from the absence of a tax on accrued property gains and also to tax the substantial fraction of corporate income attributable to foreign owners, which would otherwise not be taxed at all by Canada.[62] While recommending the continuance of a modified tax on corporate income, however, and in view of their equity principles and assumptions, the Commissioners preferred to view this tax, as far as Canadian shareholders were concerned, as an administrative withholding device for taxes meant to be borne at the personal level.

Hence the Commission's integration scheme: a device for allocating the weight of the 50 per cent flat-rate tax on corporate income to the individual shareholders so that they could adjust their tax payable to be consistent with their personal marginal tax rate. In this way a flat-rate tax could be converted (with a substantial revenue loss) into a progressive one. The corporation would pay tax at approximately 50 per cent on its net earnings, and allocate the tax paid to its shareholders regardless of whether or not the earnings had been paid out in the form of dividends. The individual shareholder would then "gross-up" his income by the amount of the pre-tax corporate income attributable to him, and deduct from his tax liability the corporate income tax paid on his behalf. If his personal marginal rate were less than 50 per cent, he would receive a credit against the remaining portion of his income tax liability, or receive a refund.[63] The idea can be understood as being analogous

to an employer withholding income tax at source on behalf of its employees.

After "an exhaustive examination of the alternative methods of taxing corporate income", the Commissioners decided at this alternative was "without doubt the best system."[64] Given the "inescapable facts" that capital gains could not be taxed on an accrual basis, and that corporate income of non-residents should not exceed 50 per cent, it best satisfied the criteria of equity and economic neutrality.[65] The Report listed ten advantages of the proposed integration scheme, which assumed the full taxation of capital gains realized by either the corporation or the individual shareholder:

1. The tax system would neither encourage nor discourage the retention of earnings by corporations, because the shareholder would be entitled to the same tax credit on an allocation by the corporation of its income as on the payment of a dividend.

2. Corporate cash retentions could be increased without worsening the cash position of most shareholders.

3. Corporations raising capital in Canada would be less affected by tax considerations in the choice between debt and equity financing.

4. To the extent that the reduction in the tax on corporate source income was not passed on in the form of lower prices or higher costs, the after-tax income from Canadian equities would be increased to most Canadians with the result that share prices would rise, the cost of equity capital would fall and the rate of capital formation by corporations would increase.

5. The increase in Canadian share prices should encourage non-residents holding shares in Canadian corporations to sell them to Canadians, and Canadian

corporations wholly owned by non-residents would be encouraged to raise capital by issuing equities in Canada.

6. The advantages of, and facility for, tax avoidance by means of "surplus-stripping" that are inherent in the present tax structure would be removed.

7. Tax avoidance through the creation of associated companies to take advantage of the dual rate would be eliminated.

8. The tax treatment of corporations, trusts and mutual organizations would be put on substantially the same basis.

9. The allocation of resources would be improved with a resulting increase in the output of the goods and services that Canadians want.

10. All corporate source income (other than the income accruing for non-resident shareholders) would be taxed at the progressive rates applicable to the individual shareholder.[66]

These advantages were in addition to the obvious one of the elimination of so-called "double taxation" of corporate source income, which had been a complaint of business and high-income Canadians for many years. A corollary to the benefit described under point 5 would have been the increased attractiveness of equity shares of Canadian corporations to middle-income Canadians.

Integration and the Taxation of Capital Gains:

The Commissioners emphasized the close linkage between their integration proposal and the full taxation of capital gains. Share owners had, in the past, been able to avoid the double taxation of corporate-source income to a considerable degree through the

non-taxable status of capital gains.[67] In the case of widely-held corporations, this could be done simply by selling a portion of the shares at a value which reflected undistributed earnings of the corporation; while for closely-held corporations, there were various surplus-stripping devices, or alternatively, designated surplus legislation imposing a modest tax on retained earnings. There was also the partial compensation for "double-taxation" provided by the 20 per cent dividend tax credit. When the tax credit was combined with the "small business rate", "double taxation" was practically eliminated for corporate income below $35,000.

As far as the Commission was concerned, the case for removing double-taxation of corporate-source income did not rest on equity for shareholders, as the burden of the double taxation of corporate income had long since been capitalized in a lower price for the shares.[68] Rather, the Commissioners were concerned about the misallocation of resources between the corporate sector and the non-corporate sector, with the resulting loss in goods and services to Canadians in general, and about the possibilities for tax avoidance which arose from differences in tax treatment of different kinds of organizations.[69] Their integration scheme, in suddenly eliminating the "double taxation" of corporate income, would give existing shareholders a windfall, one which was unavoidable in order to achieve the goal of neutrality, or economic efficiency. The full taxation of capital gains, however, would reduce this windfall:

> This is one of the reasons why we advocate both the full taxation of property gains and the full integration of

> personal and corporation income taxes. We could not countenance the unwarranted benefits that some shareholders would obtain from full integration if share gains were not taxed in full; similarly, we could not accept the adverse effects of taxing share gains in full without removing the double taxation of corporate source income. The two proposals are part of a package. Neither can be recommended in isolation.[70]

Taken together, the two proposals would have significantly reduced the tax burden on middle and low-income shareholders, and increased the average net tax burden on high-income shareholders, even when the lowering of the top marginal rate to 50 per cent was taken into account.[71] This was so because the Commission's studies indicated that the capital gains accruing to high-income shareholders was at least as large as their taxable dividends.[72]

The integration proposal had the remarkable advantage of making Canadian equity capital more attractive to Canadian individual and institutional investors without penalizing foreign shareholders. In fact, some of the latter might have benefited by capitalizing on the increase in the price of their shares which would result from the implementation of the proposal. As Canadians, especially middle income Canadians, purchased more shares of Canadian corporations, the Commissioners anticipated an increase in the supply of Canadian equities, and a greater attractiveness of equity financing for corporations.[73] They reasoned that foreign-controlled corporations would find it attractive to make more of their shares available on Canadian stock markets, thus solving the problem addressed unsuccessfully in Walter Gordon's 1963 budget:

> ...our proposal should have an effect similar to that sought by the Budget of 1963 without being open to the charge that the position of non-resident direct investors had been adversely affected. The rules of the game would be changed, but in a way that would benefit the resident investor without harming the non-resident investor.[74]

Mutual Organizations and Tax-exempt Entities:

The Commission included under this category co-operatives, credit unions, caisses populaires, mutual insurance companies, boards of trade, labour organizations, clubs and charitable organizations. In each case, the comprehensive income concept was applied to the specific form of organization, usually with the effect of removing special concessions and increasing the breadth of the tax base of each. The general principle was that such organizations conferred benefits on their members which should, as far as administratively practical, be included in the members' tax base. The Commission recommended that the organizations themselves, to the extent that they carried on business, should be accorded similar tax treatment to other businesses.

Co-operatives would have lost the three-year exemption from income tax, but also qualified for the Commission's recommended treatment for new and small business. Patronage dividends would have continued to be deductible, but only to the extent that half of the amount had been paid unconditionally in cash. These dividends would have been subject to a 15 per cent withholding tax and included in the income of

members. Losses arising from the provision of goods and services to members would have been deductible against like income, and could be carried back two years and forward indefinitely, but could not be deducted against other income. The taxable income of co-operatives would have been subject to tax at the same rate as corporations.[75]

Credit unions and caisses populaires, like co-operatives, enjoyed advantages over other businesses under the existing system. This had been justified, and apparently accepted by the Royal Commission on Co-operatives in 1945, on the grounds that such organizations served desirable social objectives, such as thrift and self-help, and did not really make business profits as such. Where such profits existed, they could easily have been eliminated by "pricing-out", that is, by reducing the prices of services to members.[76] However the Carter Commission, by applying its net gains principle, concluded that their members benefited economically from membership in the organizations, and therefore received "income" which ought to have been subject to tax like income from any other source.[77] Accordingly, the Commission recommended similar tax treatment for credit unions and caisses populaires as for co-operatives.[78]

With regard to mutual insurance companies, the Commission zeroed-in on the dividends to policy-holders, which had not been subject to tax. It recommended that these policy dividends be deductible from the income of the insurance company, and taxable as income to the policyholders.[79]

In order to close avenues for tax avoidance through the use of non-profit organizations, the Report recommended that all organizations, whether or not they claimed tax-exempt status, ought to be required to file a return to enable an "interdepartmental supervisory body" to verify the non-taxable nature of their activities.[80] Private clubs would have been taxed at the corporate rate on income other than that arising from their primary activity, and distributions of revenue to members would have been treated the same way as for co-operatives.[81] Other non-profit organizations would have been taxed at the corporate rate on undistributed income from non-portfolio investment. On distribution, this income would have been given the same integration treatment as corporate income. These organizations would not have paid tax on undistributed portfolio income, but it would have been subject to a "postponement fee" of about 15 per cent.[82]

Applying their principles to government-owned utilities and other business-oriented organizations owned by government, the Commission would have preferred that such publicly-owned entities bear the same tax burden as the private firms with which they compete. Recognizing, however, the constitutional problems associated with one level of government imposing taxes on organizations owned by another, they recommended that such corporations not be taxed without the agreement of the latter government.[83]

Trusts:

The Commission defined trusts as entities which acquire property by way of gift, bequest, or a consideration, and earn income. It proposed that, being conduits for the flow of income to individuals, they be taxed much in the same way as corporations, with some exceptions. As much of the income flowing through trusts was in the form of gifts, the Commission believed, consistent with its principles of horizontal equity and neutrality, that it should be taxed in the same way as gifts received directly or through any other vehicle.[84] However, trusts differed in three important ways from corporations which affected their proper tax treatment:

1. Much of the income flowing through trusts were gifts within the family unit.
2. Whereas the beneficial ownership of corporations could easily be determined, sometimes the beneficiary of a trust was discretionary or contingent.
3. Unlike the shares of corporations, the rights of the beneficiary were not marketable, or not under his control.[85]

Under the existing system, the income received by the trust was taxed as personal income but without personal deductions. A trust was able to deduct from its income payments to a beneficiary which were made out of the income of the trust, and this was taxed to the beneficiaries as their income. Tax credits could be transferred to the beneficiary to the extent that the corresponding income had been

allocated to the income to be distributed.[86] Gifts received by trusts were subject to gift or estates taxes, paid by the donor or his estate.[87]

The Commission proposed that trusts pay an initial flat-rate 50 per cent tax on their comprehensive income, which would be treated like a withholding tax and credited to the beneficiaries. Transfers via trusts within the family unit would have been exempt. Resident beneficiaries would have had the option of having their interest in the trust taxed at their personal rates.[88] Realization of all gains accrued in the trust would have been deemed to occur on distribution to the beneficiary.[89]

As with most of its proposals, the Commission was concerned to tax income received by and through trusts at the same progressive rates as all other comprehensive income. To achieve this it proposed several measures which it admitted were complicated, due to the fact that, "[u]nder the present law, trusts ...[had] in many instances been complicated by the desire to minimize or avoid taxes."[90] The Commissioners expected that their proposed system, including the elimination of taxes on intra-family transfers, would "reduce the number of trusts which were established."[91]

General Business Income

The business income corollary of the comprehensive income concept

was that:

> ...the business income accruing to the benefit of an individual taxpayer should be measured by common standards regardless of the particular kind of business or the form of intermediary through which it passes.[92]

While the recommendations covering business in general were many and varied, those relevant to the comprehensive tax base included:

1. all revenues should be included in business income, including property gains, gifts, windfalls, and the forgiveness or cancellation of debt;
2. all expenses reasonably related to earning income, including those of a "capital" nature, should be deductible at some time;
3. any element of personal benefit in business expenditures should be included in the personal income of the recipient;
4. all businesses, except for individuals whose principal source of income was farming or a profession, and whose gross revenue was less than about $10,000, should be required to report their income on an accrual basis;
5. the rules for applying losses against other income should be broadened to allow most losses to be carried back against any other income for two years, and forward indefinitely;
6. business losses determined by some arbitrary formula should be presumed to be of a personal nature (such as "hobby farming"), and would only be deductible against the gains from the same business in the two previous years or any subsequent year.[93]

However, the recommendations concerning business income which proved to be the most controversial were those directed toward "new and small business". The Commission proposed the removal of the existing dual rate, then set 21 per cent for the first $35,000 of income. This "small business rate" was applicable to all corporations, no matter how large their total income, but not to unincorporated businesses. The discussion in the Report made it clear that this concession, when combined with the 20 per cent dividend tax credit, effectively eliminated "double taxation" of corporate income for shareholders of corporations earning less than $35,000 whose personal marginal tax rates were 22 per cent or less, and more than eliminated it for higher income shareholders, those whose marginal tax rates were greater than 26 per cent.[94]

These figures were based on the assumption that the corporate earnings had been distributed as dividends. Very often, the earnings were retained, and, for widely-held corporations, some of the shares were sold to realize a portion of the earnings as a tax-free capital gain, while for closely-held corporations, various surplus-stripping techniques might have been used.[95] Therefore it is possible that some paid little or no personal tax on income from small corporations. Even in the absence of the tactics of realization of capital gains or of surplus stripping, but when "the optimum statutory provisions for special rates of tax on distributions" had been followed, the Commission estimated that the average combined rate of corporate and personal tax on low income corporate income had been about 35 per cent. Instead of suffering the burden of

"double-taxation", therefore, many high income shareholders of "low income" corporations were paying lower rates of tax on their corporate income than employees, professionals and partners of unincorporated businesses were on incomes of the same size.[96]

Concluding that the existing "new and small business" provisions were inequitable, inefficient and an avenue for tax avoidance, the Commissioners recommended the removal of the dual corporate rate.[97] An additional reason was the complication which such a dual rate of corporate tax would have posed for their method of integrating corporate and personal taxes. Anticipating the protests which this would arouse, the Report pointed out the many government-sponsored inducements to new and small businesses, and to their own recommendations which would have provided assistance:

1. a more liberal treatment of business losses, including the full deductibility of capital losses;
2. the full integration of corporate and personal income (thereby eliminating the "double taxation" of corporate income, which had been one of the justifications initially put forward for instituting the dual corporate rate);
3. the new top personal marginal rate of 50 per cent, replacing rates that went as high as 80 per cent;
4. a partnership option for shareholders of small unincorporated businesses which would allow them to pay taxes at their own marginal rates on a quarterly basis.[98]

The Report reproduced calculations to show that, with integration of corporate and personal income, low-income shareholders (those with personal marginal tax rates below 30 per cent) would enjoy a net reduction in tax. Any increase would have fallen on middle and upper income shareholders, who would see their marginal rate of tax on income from small corporations increase from about 35 per cent to 50 per cent.[99] If they had previously succeeded in avoiding personal tax almost entirely on such income, then the increase would have been even more severe.

The Commissioners did concede the need for some tax incentive which would be restricted to new small businesses only, and which would help off-set the difficulties which such businesses might encounter in raising capital for expansion. They proposed a system of accelerated capital cost allowances available to all businesses, including farms, and regardless of the legal form of the business. In order to qualify, businesses would have had to own less than $1 million in assets and earn less than $10 million in gross income, and have been at least 70 per cent owned and controlled by Canadian residents who had no interest greater than 30 per cent in any other qualifying small business.[100] Qualfifying businesses would have been permitted to claim capital cost allowances up to the full capital cost of the assets regardless of the allowance rates specified in the regulations, to a total value of $250,000, or until ten years had elapsed, whichever limit had been reached first.[101]

The Commissioners' incentive for new and small business was far

less generous than the existing low corporate tax rate and businesses would have had to apply for it, supplying in the process the information necessary to control its application. Instead of a permanent low rate available to all corporations, it represented only interest-free loans, available only to Canadian-controlled businesses for a strictly limited time and amount.[102] It would not be the wide avenue for tax-minimization that the existing small business rate had been. However, since "new" business was intentionally left undefined, most existing small businesses controlled by Canadian residents would initially have been able to qualify, and many of them would have been able to avoid paying taxes for several years. Even after the expiration of the set limit for the small business incentive, low-income owners of small businesses would continue to have benefited by paying business taxes at their own personal marginal rates. High-income business owners would have paid more, but no more than other people at the same income level, regardless of the source of their income, and no one would have paid at a marginal rate higher than 50 per cent.[103]

Mining and Petroleum Income

Under the existing tax regime, mining and petroleum companies had been able to deduct from their income all exploration and development costs, and any costs not absorbed against current income could be carried forward indefinitely. Investment in plant and equipment were subject to the normal capital cost allowance rates. In addition,

there was a three-year tax holiday for new mines. Since exploration and development costs and the normal depreciation allowances could be deferred until after the three-year tax holiday had expired, income from "new" mines often went untaxed for many years.[104] Taxpayers operating oil or gas wells, or most kinds of mines, were allowed to claim special allowances which reduced the effective rate of corporation tax by about a third, and non-operators were entitled to claim a depletion allowance of 25 per cent. In addition, shareholders in mining and petroleum companies were entitled to what was termed "percentage depletion", a deduction of from 10 to 20 per cent from income derived from petroleum or mining companies which met prescribed requirements.[105]

The Report argued that, while there may have been some justification for these special concessions under the existing system, which did not allow deductions for capital losses and imposed limitations on the deductibility of other business losses, and may therefore have discriminated somewhat against risky ventures, this would not have been the case under the Commission's recommended system. The full deductibility of capital losses, more liberal rules regarding deduction of losses and income averaging, the proposed new small business incentive, the integration of corporate and personal taxes, and the maximum top marginal rate of 50 per cent would have effectively removed any tax bias against risk-taking. The Commissioners' commitment to the principle of horizontal equity and the comprehensive tax base required a convincing justification to permit special concessions for one industry over the others.[106]

The Commissioners demonstrated the costs of the existing incentives by expressing them in terms of the revenues forgone from the three-year exemption for new mines, plus the depletion allowances, in terms of revenue from the entire corporate income tax. Without the special concessions, the general rate of corporate income tax could have been lowered by almost four percentage points while raising the same revenue.[107] The Commissioners did not dispute that the concessions had boosted investment, output and employment in the petroleum and mining industries, but they suspected that this had been achieved at the cost of an equal or greater reduction in other economic sectors. Even if there had been an overall improvement in the well-being of Canadians, which the Commissioners did not accept, then it had been achieved at too great a cost.[108]

The Report addressed each argument made on behalf of special concessions to the mining and petroleum industries, and, in the context of its other recommendations for a reformed tax system, rejected them all.[109] They were not even persuaded that ventures in the extractive industries were generally more risky than ventures of similar magnitude in other industries[110], and, in the event that the Government decided that incentives were needed, the Commission would have preferred to see these granted in the form of subsidies rather than tax concessions, so that the cost would be more apparent.[111]

The arguments for incentives aside, the Commission's analysis of the existing incentives showed them to be grossly inefficient. The

percentage depletion and the three-year exemption for new mines, being related to current profit, applied to the output that would have occurred without the incentive as well as to any additional output. In addition, new output might have been hindered by other factors, such as monopoly control, or prohibitive cost of new discoveries. On the other hand, if additional output resulted in a decline in prices, then, to the extent that the output was exported, any incentive to additional output would have been wasted.[112]

The depletion allowance to operators, being related to current profit, suffered from the same defect as percentage depletion. Moreover, the logic of its operation made it perverse and misdirected in its effects: since exploration costs had to be deducted before claiming depletion, a company derived less benefit from depletion the more it spent on exploration; and depletion benefited only established corporations with operating income from which to deduct the depletion allowances. Of the approximately $150 million in depletion allowances claimed in 1964, over three-quarters were accounted for by only eight companies.[113] Yet the cost of capital, supposedly the main justification for the incentive, was not high for these large, established companies with plenty of operating income. This was borne out by the price/earnings ratios of their shares.[114]

The most efficient of the existing incentives was found to be the rapid write-off of exploration and development costs, since the tax subsidy was directly related to the activity which was supposed to be stimulated. Again, however, it benefited mostly the large established

firms, since they had the operating income to make use of it. Also, this incentive applied to costs right though the final development stage, when risks would have been greatly reduced. This tax subsidy for development costs would thus tend to increase the rate of development of known resources rather than stimulate the search for new resources.[115]

The three-year exemption for new mines was found to be most advantageous in cases of short-lived mines owned by existing companies. It was more selective, and therefore a more efficient incentive than depletion. However, as it applied to all new mines rather than just those to which such an incentive would have been necessary to bring that mine into production, a great deal of revenue was foregone for no effect:

> Here too, the incentive was found to provide the greatest benefit to those who needed it least. During the period 1955 to 1964, five large mining companies reported about 70 per cent of the income exempted under the new mine provisions. These corporations had operating income against which exploration and development expenses could have been immediately offset, and they operate on such a large scale that they are quite capable of spreading their risks. There is no evidence of a capital market bias against their shares. Three of these companies claimed $117 million in tax-free income in 1964 alone -- at a tax revenue loss of nearly $60 million. It is open to question whether this tax saving had a major impact on the investment expenditures made by these companies. Even if it did, it is most unlikely that the benefits obtained exceeded the lost tax revenue.[116]

In place of these concessions, the Commission recommended essentially the same treatment as for other industries. In addition to the full inclusion of capital gains and full deductibility of

capital losses, this would mean that exploration costs could have been written off immediately, and could have been carried forward to subsequent years. Development costs, excluding the costs of acquiring properties or property rights, would have been written off at an annual rate of 20 per cent. Smelters and refineries would have been permitted only the same capital cost allowance rates as was applicable to buildings and machinery in other industries. Costs of purchasing mining or petroleum properties would have been written off in accordance with their ascertainable useful life, and "only to the extent that a loss in value could be shown to have occurred."[117] In accordance with the general rule adopted by the Commissioners for capital cost allowances, that depreciable assets should not be written off until they had been put to use, they proposed that the write-off of development costs and of assets used in production not be permitted until production had commenced, that it be restricted to operating income from that particular mine or well, and that it cease when that facility had been abandoned.[118] In addition, mining and petroleum companies would have been eligible to apply for the same small business incentive available to other industries.[119]

Although the Commissioners considered similar tax treatment as for other industries to be appropriate for the mining and petroleum industries, they showed some concern regarding possible "major adverse effects" of a sudden change.[120] As a transition measure, therefore, they recommended that these companies be permitted the accelerated write-off of all exploration and development costs, excluding smelters and refineries. This concession would have been gradually restricted

over a period of five or ten years to capital cost allowance rates applicable to other industries. In order to ease the shock of the loss of the three-year tax holiday for new mines, the Commissioners recommended the continuation of this exemption, up to a value of $1 million per mine, for the next five years.[121] They expected to reduce the impact of the withdrawal of percentage depletion by a third transitional provision: the deductibility, over a transitional period, of a portion of property costs which had not previously been deductible.[122]

In combination with the full deductibility of share losses and more liberal treatment of business losses, the Commissioners felt that their proposal was fully adequate to offset "any bias in the capital markets that might exist against the mining and petroleum industries", a bias which they had shown not to exist for the larger companies claiming most of the value of the existing concessions, but which might have existed for other companies in these two industries.[123] While some of the existing incentives had been limited in their application to persons whose major business was in mining and petroleum, the Commission could find no justification for such a limitation, and recommended that all the incentives it proposed be equally available to all Canadians, which would "encourage wider participation by Canadians in the mining and petroleum industries".[124]

Consistent with its principle that all economic gains should be taxable and that all expenses incurred to earn those gains should be

deductible, the Commissioners also recommended that the existing exemption of property gains for prospectors and grubstakers be removed, and their costs be allowed as deductions.[125] All transactions in mining properties would have become subject to tax, generally on the basis of fair market value.[126] Among legitimate expenses would be all provincial royalties, charges and income taxes, which would have been deducted in the same way as any other cost of doing business.[127]

The impact of the Commission's recommendations concerning mining and petroleum income would have hurt most the large integrated companies, that is, those which had sufficient operating income from which to fully deduct all exploration and development expenses, and which had therefore benefited the most from the existing concessions. While exact figures would depend on the specific situation of each company, the Report estimated the likely reduction in after-tax cash flow rate of return for integrated petroleum companies to be about 23 per cent, and for integrated mining companies, about 11 per cent.[128] The Report demonstrated that, where all income was distributed in the form of dividends, the shareholders of such companies would have been better off than under the existing system, and that even those in the top tax bracket would have been no worse off.[129] However, when the impact of the full taxation of share gains was taken into account, shareholders of integrated companies would have suffered a significant net loss in the after-tax rate of return. For shareholders with a marginal rate of tax of 30 per cent, the Report estimated the decline to be about 8 per cent.[130] For

high-income shareholders, those with a marginal tax rate of 50 per cent, the comparable loss would have been about 30 per cent.[131] Non-resident shareholders, unable to benefit from the integration of corporate and personal taxes, would have suffered a greater loss unless they received a tax credit from their own government in recognition of taxes paid in Canada.[132]

The Report then examined the operating figures of a number of large, integrated companies to estimate the likely impact of their proposals on corporate behavior:

> A review of four large mining companies, which together have claimed approximately $250 million in exempt income under the three-year provision, indicated that under our recommended procedures they would on average still not pay any income taxes until they had been producing for over ten years. This is somewhat more than a year earlier than would have been the case under the present system. The major difference is that under our proposals it would have been necessary to claim substantially all of the capital cost allowance available in order to eliminate their taxable income. In any case, the accelerated write-offs would mean that tax liabilities could be deferred for a considerable period of time, and certainly could be deferred until the total financing obtained to put the mines into production had been repaid. We do not believe that a procedure for computing taxable income that would have deferred the payment of income taxes for over ten years would have prevented the development of an economically feasible project.[133]

The Report cited a second example, that of the major uranium mining companies, which, up to 1964, had produced and sold over $1 billion of ore, based on an investment of less than one quarter of that amount. The net profit, after deducting all financing costs, was "about a quarter of a billion dollars", of which only about $30

million was paid in income taxes, including personal income tax on the amounts paid out in dividends. The Carter proposals would have resulted in about the same income tax liability but, again, all capital cost allowances would have been used up and their future taxes would have been "substantially higher".[134]

The Commission's examination of the operating figures of "a number" of large integrated mining and oil companies over "the past three to ten years" revealed that the total income taxes paid, including personal income tax on dividends, was "just over 40 per cent". As the authors estimated that the average tax rate applicable to all corporate-source income attributable to Canadian residents would, under their proposals, have been "substantially less than 40 per cent", they concluded that "Canadian shareholders in mining and petroleum companies would experience a reduction in the total income tax liability on their portion of the corporate profits of these companies."[135] They acknowledged, however, that with the inclusion of personal tax on capital gains, "the total taxes paid by a substantial proportion of the Canadian investors in mining and petroleum companies would be increased."[136]

In the case of non-integrated companies, the after-tax cash flow rate of return would have been raised by about 5 to 10 per cent for petroleum companies, and have declined by about 2 per cent for mining companies.[137] Figures in the Report showed that low and middle-income shareholders in non-integrated companies would have been further ahead under the Commission's proposals, even with the taxation

of share gains.[138] For shareholders with a marginal tax rate of 50 per cent, however, the after-tax rate of return would have declined by about 9 per cent.[139]

Banks and Other Lending Institutions

The Commission had little to say about the income of banking and lending institutions that was different from ordinary business income, with the exception of the question of contingency reserves and reserves for doubtful accounts. This concerned the banks, trust companies, mortgage loan companies, and finance and consumer loan companies. The Commission maintained its general stance in opposition to tax concessions, stating that, in the case of financial institutions, it was the responsibility of governmental authorities to see that these institutions conducted their business in such a way as to ensure their solvency and to protect the lending public, and therefore that the tax system should have no role to play in this.[140]

Under the existing system, chartered banks were permitted to deduct "contingency reserves", which were, according to the Income Tax Act, "not in excess of the reasonable requirements of the bank".[141] The maximum allowable amount for tax-free contingency reserves, which were in addition to the reserves based on a calculation of doubtful loans, were determined by the Minister of Finance by means of a formula and was then set at 3.504 per cent of eligible assets.[142] The Commissioners opposed recognizing as deductions any losses in

asset values and any liabilities in excess of what could "reasonably be expected to occur", and they believed that their general recommendations on the treatment of business losses should adequately cover the situation of financial institutions.[143] In cases where difficulties arose in the determination of reasonable allowances for losses, they acknowledged that some simple but arbitrary rule might be appropriate.[144]

Their opposition to tax-free contingency allowances was also based on their stated goals of "tax neutrality", which, in this case, implied that different financial institutions which performed similar functions should be subject to similar tax treatment.[145] A final consideration in their proposed treatment of financial institutions was the principle that more direct means than taxation should be used for regulating actions in accordance with public policy objectives.[146]

In examining the basis for calculating the contingency reserves of the banks, the Commissioners found that it was twenty times the actual loss experience over the previous twenty-five years, a margin which they concluded was "excessive."[147] They proposed instead that banks be allowed to deduct an allowance for expected losses which would be restricted to certain types of loans, and be calculated against specific assets according to rules which would bear some relationship to the degree of risk attached to each class of loan. The Commissioners expected that the tax-free reserves of the banks would thereby be "substantially reduced".[148]

The Commissioners also found the ability of financial institutions to write off loans at will as "bad debts" to be unacceptable. They recommended instead that such write-offs be permitted only when a "loss" had been established in a legal sense.[149]

As with the mining and petroleum companies the Commission allowed for a generous transition of ten years in which to adjust to the new system.[150]

Life Insurance Companies

Among Canadian financial institutions, the life insurance companies were second only to the chartered banks in terms of their total assets, amounting to over $11 billion at the end of 1964.[151] Investment earnings for Canadian companies in that year were $410 million, and about $140 million for non-resident companies.[152] Under the existing tax regime, the tax liabilities of life insurance companies were calculated in a different way from all other businesses. Instead of including all investment income, only the amounts credited to shareholders' accounts were included for tax purposes.[153] As a result, in 1964, while the net revenues of Canadian insurance companies (after deducting policy dividends and a normal increase in actuarial reserves) exceeded $90 million, tax was paid on only $5 million of income.[154] Taking $90 million as a realistic estimate of the income of these companies, their combined

average rate of income tax would have been about two per cent.

Mutual insurance companies, which do not have shareholders, and therefore do not distribute income, are in effect exempt from income tax.[155] Since 1958, "five large Canadian life insurance companies" had 'mutualized', a procedure under which the policyholders bought out the shareholders,[156] thus converting stock insurance companies, which paid very little in taxes, into mutual companies, which paid no taxes. The Report attributed this change to a desire "to keep control of the companies in Canada".[157] Moreover, the proceeds from the sale of the stock companies' shares were, by special statutory provision, tax free to the recipients.[158] Foreign companies, even if they were not mutual companies, were also exempt from income tax on their business operations, because they too did not have any shareholders' accounts in Canada. They were, however, subject to a withholding tax of 15 per cent on the portion of their Canadian investments exceeding 110 per cent of their Canadian liabilities.[159]

The Report highlighted the anomalous tax situation of life insurance companies in Canada, which was practically a tax haven in comparison to other countries:

> With only 30 per cent of the life insurance carried by Canadian companies being placed abroad, the $13.8 million paid by them in foreign income tax offers strange comparison with the mere $1.9 million paid in Canadian income tax. The foreign income taxes paid by Canadian companies may also be noted relative to the fact that foreign companies paid no income tax to Canada on a comparable amount of insurance placed by them in Canada.[160]

Not surprisingly, the Commissioners found the existing method of taxing insurance companies to be grossly inequitable and unsatisfactory.[161] In its place, the Commissioners recommended a method which would tax all life insurance organizations, resident and non-resident, in a similar manner, recognizing the income which flowed to shareholders in stock companies, to participating policy-holders of mutual companies and stock companies, and to members of fraternal benefit societies.[162] Deductions from income for actuarial liabilities should be based on an arbitrary investment yield exceeding four per cent, instead of the existing average of about three per cent.[163] Policy dividends, while being deductible from company income, should be taxable as income to the policy-holders. The recommendations applicable to corporate income would also apply to stock insurance companies.[164]

The Commission's calculations indicated that, following its recommendations, the tax revenues from the life insurance companies would have increased from $1.9 million to about $75 million.[165] The Commission expected its tax regime to "substantially reduce the future retained earnings and the cash flow of stock insurance companies", with possibly a portion of the additional tax burden being passed on to policy-holders in the form of higher premiums. In the absence of any compelling argument for a mild transitional period, the Report called for the immediate implementation of its recommendations on life insurance, "including the taxation of income derived from policies issued prior to the date of implementation of ... [its] proposals."[166]

International Income

The Commission approached the problems of the taxation of income flowing outside the country and that flowing into the country with the same principles which guided it throughout its Report, plus some additional constraints. Taxation of international income flows must:

a) ...not adversely affect our ties with the rest of the world;
b) ...maintain and preferably increase the net economic benefit which Canada derives from foreign investment; and
c) ...not abrogate our treaty obligations or offend against the normal standards of international taxation.[167]

The Commissioners acknowledged that the principle of neutrality could not be consistently applied in international taxation, due to many other factors causing market imperfections.[168] While having to bow a little further to administrative and economic realities in the field of international taxation than in domestic taxation, they sought to tax the foreign source income of Canadians at full progressive rates, minimize tax deferment, eliminate the use of tax havens by closing loop-holes, and minimize tax avoidance by non-residents by reducing the differences in tax treatment of income from different sources.[169]

Working from these principles and constraints, the Commissioners came to the following general conclusions:

1. Integration would not be extended to non-residents.
2. "The level of tax on foreign shareholders of Canadian corporations should not be raised except where necessary to carry out domestic

tax reforms."

3. Except for dividends, withholding taxes on payments to non-residents should be increased.
4. Canada should not tax non-residents except in connection with business or real estate transactions carried on in Canada.
5. Residents should be given credit for foreign withholding and corporation taxes actually paid at a rate that would ensure that their Canadian taxes on dividends did not increase.[170]

Among 22 more specific recommendations were the following:

1. The existing exemption for all income from foreign direct investment where more than 25 per cent of the shares were owned should be removed, as this had become a lucrative route to tax havens. The Department of National Revenue had provided the Commission with figures which supported this: Of $1.5 billion in dividends received by all Canadian corporations, only 10 per cent came from the United States and only 4 per cent from the United Kingdom.[171]
2. Residents having direct foreign investments would have to report their foreign income and taxes paid in each jurisdiction. A procedure was recommended to ensure that the combined foreign and Canadian taxes would be no less than 30 per cent.[172]
3. Residents receiving income from foreign portfolio investments should have the option of being taxed in the same manner as those receiving income from direct investment, or as under the existing system of a credit for withholding taxes paid.[173]
4. The income of trusts which was distributed to non-residents should

be taxed at 50 per cent, the same as for corporations, and the amounts distributed subject to the same rate of withholding tax as for dividends.[174]

5. "Foreign business corporations", that is, those which carried on their business outside Canada, should lose their tax-exempt status over a period of five years.[175]

6. "Non-resident investment corporations", that is, corporations which were at least 95 per cent owned by non-residents and paid only a 15 per cent tax, should be phased out over ten years. These had become vehicles for international tax avoidance, and the low rate was discriminatory against other investors.[176]

To the extent that tax havens and other methods of international tax avoidance were presumably limited to those in the high tax brackets, these recommendations would have hit wealthy, tax-sophisticated Canadians and non-residents especially hard.

Other Recommendations

The Commission made many other recommendations, most of them related at least indirectly to the comprehensive tax base or the principles of tax equity. Some of the more important ones were in the areas of commodity taxes, federal-provincial relations, and matters of tax policy formation, administration and adjudication.

Commodity Taxes:

1. In place of the existing manufacturer's sales tax, the federal government should impose a single-stage sales tax at the retail level, which should include services. In order to improve vertical equity however, the overall weight of sales and property taxes should be reduced.[177]
2. All excise taxes except those on alcohol and tobacco should be removed.[178]

Federal-Provincial Relations:

1. The federal government should seek to establish with the provinces, a joint, indirect retail sales tax, to be on a common base, administered by the provinces, and with a revenue guarantee to the federal government. The provinces would each be free to vary the rate but the base would be uniform.[179]
2. "While consultation with the provinces should occur, the federal government should continue to play a predominant role in income tax matters in order that it may:
   a) Pursue an effective stabilization policy.
   b) Ensure that the income tax does not become a device through which the stronger provinces take advantage of the weaker.
   c) Ensure that redistributive objectives are recognized."[180]
3. The federal government should seek to become the sole collection agent for all personal income taxes; and federal and provincial

death had been a contentious matter during the Commissioners' deliberations.[222] Carter had reminded Beauvais that, during the hearings, they had asked for cases in which a closely-held company had been forced to sell out in order to pay taxes. None had been presented. The majority Report underlined this fact:

> Many witnesses before the Commission made reference to the impact of estate taxes on the sale of private businesses, particularly sales to non-residents. In questioning these witnesses, we examined their statements carefully to appraise the seriousness of the charge and to determine whether or not such sales appeared to have unfavourable economic consequences. Most witnesses very quickly stated that taxation would not, by itself, direct business assets to non-resident purchasers, but would cause them to be placed on the market and because of circumstances apart from taxation they might be purchased by non-residents. Some witnesses undertook to conduct further enquiry into this matter and to furnish us, on a confidential basis, with any facts adduced concerning the enforced sale of family businesses. Although some material was, as a result, supplied to the Commission, it did not lead to any clear conclusion. We made enquiries into the more conspicuous incidents which have appeared in the press. In none of these cases did the impact of estate taxes seem to have even a minor influence in favour of sale.[223]

Even had some business been sold in order to pay taxes, the majority was not convinced that this was an economic calamity which ought to be avoided through tax measures: "There is little evidence to support the position that businesses tend to prosper to a greater extent because they remain in the same family."[224]

In his minority report, Grant used the phrase "double taxation on distribution", to refer to the fact that, under the majority recommendations, the estate of the deceased would have been taxed on gains that had accrued over a lifetime, with the accrued gains being

details of tax legislation following introduction in the House of Commons.[188]

7. "Ministerial discretion should be kept to a minimum in tax legislation; where it is employed, the taxpayer should have the right to require an advance ruling on stated facts, and a parliamentary committee each year should examine the manner in which the discretionary powers have been used and report on the continuing need for the discretion."[189]

Distributive Implications of the Recommendations

The distribution of the burden of direct taxes would have been affected most by three changes:

1. The reductions in rates, which would have helped mostly those in the upper income brackets whose earnings were derived largely employment, professional or business income;
2. The integration of corporate and personal taxes, which would have helped mostly those middle- and low-income people who held corporate shares;
3. The comprehensive tax base, which would have increased taxes substantially for those earning a large amount of income through previously untaxed receipts, such as capital gains, tax-sheltered income, or transfer payments.[190]

While it was true that most of the capital gains were received by those with high-incomes, the Commission's analysis of a large sample

of tax returns showed that there was considerable diversity of income sources within income classes.[191] The Report therefore warned readers to interpret its figures on the average tax burden by income class with caution.[192] Figure 5-1, below, reproduces the Commission's figures for the average effective rates of federal direct taxes by income class, under the existing system and under its proposed system. The most striking feature is the substantially increased tax burden for those with more than $50,000 of comprehensive income in 1964. There were 20,199 such people, representing only 0.3 per cent of resident taxpayers. The other feature readily seen is the modest decline in average tax rates for those earning less than $8,000.[193] The latter income classes represented a total of over 6 million resident taxpayers, including the great majority of wage and salary earners.

Table 5-2 shows the Commission's calculations of the distribution of changes in tax burden larger than 15 per cent. About 46.5 per cent, or about 3.1 million resident taxpayers, stood to gain significantly from implementation of the Carter proposals. A group almost as large would see no marked change in terms of the distribution of the tax burden, though the Report had argued throughout that everyone would gain through improved efficiency of the taxation system. Finally, about 630,000, or about 9.4 per cent of taxpayers, could have expected to suffer a significant increase in their tax burden. For most of these potential losers of tax reform, those earning less than $25,000, the dollar amounts of the loss would not have been large.[194] However, for most of those 26,259 taxpayers

TABLE 5-1
AVERAGE EFFECTIVE RATES OF FEDERAL DIRECT TAXES
FOR RESIDENTS BY LEVEL OF COMPREHENSIVE INCOME

INCOME ($1,000'S)	NUMBER OF TAXPAYERS	AVG. TAX RATES ON COMPREHENSIVE BASE 1964	PROPOSED	% CHANGE
0-1	698,227	1.3	nil	-101.9
1-2	919,539	2.7	1.4	-45.0
2-3	1,076,928	5.2	4.5	-12.9
3-4	1,072,471	6.5	5.9	-10.2
4-5	1,001,470	7.5	7.0	-7.9
5-6	722,461	8.7	8.3	-4.8
6-8	662,694	10.1	9.8	-3.5
8-10	231,123	12.3	12.2	-0.7
10-12	85,061	13.8	14.3	+3.4
12-15	83,529	15.2	15.9	4.1
15-20	67,292	17.5	18.3	4.5
20-25	29,406	19.9	20.5	3.2
00-35	29,842	22.6	23.5	3.8
35-50	18,663	25.7	28.2	10.2
50-75	10,790	28.0	32.6	16.4
75-100	3,710	30.2	36.5	21.0
100-150	3,113	31.1	40.0	28.5
150-200	1,119	32.3	42.9	32.7
200-300	834	33.2	44.7	34.6
over 300	633	35.3	47.3	33.8
All:	6,719,445	11.4	11.6	2.6

Source: Report of the Royal Commission on Taxation, Vol. 6, Table 36-7, p. 62, and Table 36-6, p. 61. The former table notes that average effective rates were calculated by dividing total direct taxes paid by or attributable to taxpayers in each income class by the taxpayers' total comprehensive income. The reduction would be more than 100 percent in the bottom group because of the attribution of some credits for corporation income taxes to trustees of Registered Retirement Income Plans.

with comprehensive incomes in excess of $25,000, the average loss would have been very substantial in dollar terms. The Commission's figures indicate that the average individual loss expected for the 633 taxpayers with comprehensive incomes in excess of $300,000 was over $67,000.[195]

TABLE 5-2
NET IMPACT ON DIRECT TAXES OF RESIDENT TAXPAYERS
BY COMPREHENSIVE INCOME CLASS

INCOME ($1,000's)	NUMBER OF TAXPAYERS FOR WHOM TAXES WOULD BE... DECREASED more than 15%	CHANGED less than 15%	INCREASED more than 15%
under 5	2,713,328	1,685,259	370,048
5-10	404,144	1,038,796	173,338
10-15	5,269	125,901	37,960
15-25	1,895	70,918	23,885
over 25	182	42,263	26,259
	3,124,818	2,963,137	631,490

Source: Report of the Royal Commission on Taxation, Vol. 6, p. 61.

Unlike Canadian residents, non-resident taxpayers stood to lose on average from the Carter proposals. This was not due to any burdens recommended specifically for them, but a result of the removal of special incentives and exemptions for industries which also happened to have a large proportion of foreign investment,[196] and also the removal of the "small business rate" for corporate income.[197] Table 5-3 reproduces the Report's summary of the impact of the recommended changes on the industries most affected. The stakes were high in life insurance and petroleum, but highest for foreign investors in the mining industry. The chapter on mining in the Report showed that this increased burden would fall to the large integrated mining companies, most of them subsidiaries of foreign corporations.[198]

Combining direct and sales taxes, the Commission showed that the overall distribution of its reformed system would increase the progressiveness of the system from what it had been. Table 5-4 reproduces the Commission's figures for the distributive effects of the sales and direct taxes combined.

TABLE 5-3
1964 AND PROPOSED CORPORATION INCOME TAXES
ATTRIBUTABLE TO RESIDENT AND NON-RESIDENT
SHAREHOLDERS OF CANADIAN COMPANIES, BY INDUSTRY
($ millions)

	Estimated Corp. Tax Base (Carter Proposals)	1964 Corp. Income Taxes		Corp. Income Taxes (Carter Proposals)	
		Total	Non-residents	Total	Non-residents
Mining:	501	117	79	251	185
Oil & Gas:	131	47	32	66	47
Life Insurance:	154	2	1	77	33
other insurance & financial:	240	93	25	120	43
other industries:	3,920	1,676	944	1,959	1,044
Total	4,946	1,935	1,081	2,473	1,352

Source: Report of the Royal Commission on Taxation, Vol. 6, Table 36-1, p. 51. Corporation taxes include old age security taxes and are before abatements to the provinces. Taxes on Section 105 distributions (under the designated surplus provisions of the pre-reform Income Tax Act) are not included in the 1964 figures.

TABLE 5-4
ESTIMATED CHANGES IN SALES AND DIRECT TAXES COMBINED
OR FAMILIES IN DIFFERENT INCOME CLASSES

Income Class	Average 1964 Tax			Average Change in Taxes	
$1,000's	Direct	Sales	Total	$	%
less than 2	$ 26	$ 80	$ 106	$-15	-14.6%
2-4	184	180	364	-40	-11.0
4-5	352	252	604	-61	-10.1
5-7	575	347	922	-69	-7.5
7-10	909	503	1,412	-81	-5.7
greater than 10	5,178	722	5,900	+807	+13.7
all	540	269	809	-7	-0.9

Source: Report of the Royal Commission on Taxation, Vol. 6, Table 36-11, p. 68. Average direct taxes attributable to families in each income class are assumed to be the same as the average attributable to all taxpayers in that income class. 1964 taxes include old age security taxes. All taxes are before abatements to the provinces.

Reports of the Dissenting Commissioners

While all six Commissioners signed the main Report, A. Emile Beauvais and Donald M. Grant each submitted a minority report in which he objected to the majority's adoption of the comprehensive income concept.

Grant's Minority Report:

Grant pointed to the principle adopted in the majority Report, "that taxation at progressive rates of all additions to economic power is the only equitable basis for taxation." "Complete adoption" of this principle, he argued, would "destroy certain elements of our present system which should be retained."[199] The first was the Report's proposals dealing with business losses: Grant proposed that business losses be applied over the same time period as suggested in the Report, but that they be deductible against all income in the year of the loss, and only against business income in other years. He opposed the restriction recommended in the majority Report regarding the number of years for which business losses could continue to be deducted against other income. While this would have allowed the continuance of an existing tax loophole used by "hobby farmers" and others using business forms of organization for recreational purposes, Grant argued that "...the great majority of such business undertakings should not be placed under arbitrary restrictions to block abuses of a relative few".[200] The recommended restrictions he continued, could force the closure of established businesses, inhibit the establishment of new businesses and the expansion of existing ones, and generally curtail initiative.[201]

Grant also opposed any restrictions on the deduction of losses on sales of personal property. The Report had recommended restricting the deduction of such losses to gains incurred on similar kinds of property within the preceding two years, which Grant considered to be

"inadequate as compensatory measures to ease what must be regarded as stringent legislation."[202] As his choice of words implied, Grant was not at all happy with the proposal to tax all gains at "full rates":[203]

> Capital investment of savings in Canada by Canadians is to be encouraged. Also it must be kept in mind that Canada's two principal trading partners, the United States and the United Kingdom, impose this form of tax at modified rates. Shares with growth potential have particular significance in a country such as Canada, and investment should not be inhibited by a high rate of tax on capital appreciation. The inflationary element is ever present in gains in securities and real estate, and to tax capital gains that resulted from a general increase in price levels at full rates would be inequitable.[204]

As an alternative, Grant proposed to tax capital gains at preferential rates depending on a holding period. Land held for more than three years, and other property held more than one year should be subject only to a tax of half the personal marginal rate, or a maximum of twenty-five percent, short-term gains should generally be taxed at "full rates".[205] Grant did not propose extending preferential treatment of capital gains to trading profits, which would "continue to be taxed at full rates, be they earned by the individual or by the corporation."[206] Readers of the full Report would have been aware that the determination of whether or not gains arose in the course of a trade or business was the most frequent bone of contention in litigation involving capital gains.[207]

Grant did not discuss how this preferential treatment would affect the revenue yield of the income tax, or how much higher the normal "full rates" would have to be in order to compensate for the revenue

loss. He did, however, defend preferential rates for long-term capital gains by reference to the "locked-in" argument, that is, that a "full-rate" tax on capital gains would seriously impede the mobility of investment capital, with consequent harmful effects for the efficiency of the capital markets in allocating investment capital to the most economical purposes. In support of this proposition, he cited the main Report's observation that the tax on capital gains in the United States, which accorded preferential treatment to long-term gains, had had "very little overall effect on the level of aggregate investment."[208]

The discussion in the main Report concerning studies on the mobility of securities in the United States indicated that, while the studies were not conclusive, the holding period provision and the dual rate for the taxation of capital gains had only a limited effect on mobility of investment funds.[209] On the other hand, some American studies had indicated that the tax exemption for gains accrued at death was a significant factor hindering capital mobility.[210] The majority Report had concluded that "to the extent immobility of capital investment does exist in the United States, it would appear to be largely the result of the tax deferment and exemption extended to accrued gains on property transferred by gifts and bequests."[211] In other words, it was not the fact of a capital gains tax in itself that caused any "locked-in" effects (whether that proved to be a serious problem or not), but the absence of deemed realization when transferred by gift or bequest, which Grant also opposed.

Grant supported the recommendation in the main Report that personal and corporate taxes be integrated, which would greatly soften the burden of inclusion of capital gains for those middle- and low-income earners dependent on investment income. However, in the event that integration not be implemented, he favoured allowing taxpayers the right to include only half of property gains in income, or to have them taxed at a preferential rate of 25 per cent.[212] Replacement of integration with a partial exemption on capital gains, that is, substituting a method of taxing corporate source income at progressive rates with tax relief for largely upper income people, would have had a decidedly regressive impact on the distribution of the tax burden by income group.

Grant was also critical of the main Report for not allowing a "roll-over" provision, which would have allowed owners of assets to sell them and re-invest the proceeds without being liable to income tax.[213] The authors of the majority Report had not done so because they found "a serious violation of equity", in allowing "some property owners to save from pre-tax dollars while others must save from after-tax dollars."[214] In addition, after "examining in detail a number of methods", they concluded that all were "subject to major complexities and serious definitional problems."[215] Acknowledging the violation of equity, Grant offered the "roll-over" provision as an incentive for investment in the manufacturing industry:

> Nevertheless, the inclusion of a "roll-over" provision in the tax system might well be justified by the fact that the Canadian economy depends so much upon establishing secondary industry and increasing the sale of manufactured products abroad, particularly if there is to be deemed realization at

death or on cessation of residence.[216]

The majority had found no need for such an incentive, though if one were considered necessary, they proposed more generous capital cost allowances or investment tax credits, the revenue loss being recouped through increased taxes on higher incomes.[217] However the best "tax incentive" for increased business investment, they pointed out, was effective fiscal policies to maintain full employment.[218] In considering the question of investment incentives, the majority Report argued that the integration proposal would have significantly increased the after-tax rate of return on most investments for middle income people, and some of this would have been directed toward manufacturing.[219] In addition, the majority's proposed new and small business incentive, by allowing an immediate write-off of $250,000 of capital investment, was designed to accomplish the same objective favoured by Commissioner Grant.[220]

Grant also dissented from the recommendation that accrued capital gains be deemed to have been realized on the breakup of the family unit, or on the death of the surviving spouse:

> In my opinion the latent hardships involved in such a policy, including forced sale of assets and double taxation on distribution, are far greater than any inconvenience to the Revenue which will collect its tax eventually. The decision whether or not to realize gains should be that of the taxpayer free from compulsion under the Income Tax Act. Therefore, to maintain neutrality the conclusion is: no taxation without realization except when a taxpayer ceases to be resident of Canada unless, as the Report recommends, such taxpayer elected to be taxed as a Canadian resident on his world income.[221]

It will be recalled that deemed realization of capital gains at

death had been a contentious matter during the Commissioners' deliberations.[222] Carter had reminded Beauvais that, during the hearings, they had asked for cases in which a closely-held company had been forced to sell out in order to pay taxes. None had been presented. The majority Report underlined this fact:

> Many witnesses before the Commission made reference to the impact of estate taxes on the sale of private businesses, particularly sales to non-residents. In questioning these witnesses, we examined their statements carefully to appraise the seriousness of the charge and to determine whether or not such sales appeared to have unfavourable economic consequences. Most witnesses very quickly stated that taxation would not, by itself, direct business assets to non-resident purchasers, but would cause them to be placed on the market and because of circumstances apart from taxation they might be purchased by non-residents. Some witnesses undertook to conduct further enquiry into this matter and to furnish us, on a confidential basis, with any facts adduced concerning the enforced sale of family businesses. Although some material was, as a result, supplied to the Commission, it did not lead to any clear conclusion. We made enquiries into the more conspicuous incidents which have appeared in the press. In none of these cases did the impact of estate taxes seem to have even a minor influence in favour of sale.[223]

Even had some business been sold in order to pay taxes, the majority was not convinced that this was an economic calamity which ought to be avoided through tax measures: "There is little evidence to support the position that businesses tend to prosper to a greater extent because they remain in the same family."[224]

In his minority report, Grant used the phrase "double taxation on distribution", to refer to the fact that, under the majority recommendations, the estate of the deceased would have been taxed on gains that had accrued over a lifetime, with the accrued gains being

eligible for averaging over the last five years of the life of the deceased taxpayer. Then, when the estate was divided among the heirs, the latter would also have been taxed on the amount each received, again, the amounts being averaged over a period as long as five years or longer by the use of Income Adjustment Accounts.[225] Since two sets of entities, the estate of the deceased taxpayer and the heirs, would both have been subject to tax at about the same time, it could be said that this was "double taxation", as it might well appear to the heirs. From the viewpoint of the Commission majority, this resulted from the fact that the deceased taxpayer had enjoyed an extended deferral of tax on accrued gains: had these gains been taxed as they accrued, no-one would have complained of "double taxation". The fact that two separate entities, the giver and the recipient, for administrative reasons, were being taxed at the same time, does not mean that the same persons were being taxed twice on the same income. Also, in the case of the estate, only the accrued gains would have been taxed, not the entire body of the estate. As for the heirs, the entire sum was to be added to their taxable incomes, less the remaining balance of their respective lifetime exemptions and annual exemptions, and presumably softened by the suggested averaging provisions.[226] The majority recommended that, where the estate consisted of non-liquid assets, the taxpayer should be allowed to pay the tax in installments at an appropriate rate of interest.[227]

The majority Report argued that failure to tax accrued property gains on death "would be a serious breach of taxpayer equity",[228] allowing a major portion of property gains to escape tax entirely.

This was the case with the partial taxation of capital gains in the United States. It would also lead to the same "locked-in" problems which Grant had said might be serious in the case of the majority proposal to tax capital gains at "full" rates. The majority Report had attributed any immobility of capital in the United States largely to the tax deferment and exemption extended to accrued gains on property transferred by gifts and bequests.[229]

Grant defended his proposal for "no taxation without realization" as maintaining "neutrality", but he did not say neutrality between what and what. It would not have been neutral in terms of treatment of capital gains, since some would (if realized after a short interval, or if judged to be business income) be taxed at "full" rates, some would be taxed at preferential rates, and some not at all. Nor would it be neutral across income groups, since the most wealthy taxpayers (to whom accrue the lion's share of capital gains) would derive the greatest benefit.

Commissioner Grant's main objections to the comprehensive income concept were not minor ones: if implemented, little would have remained of the comprehensive income concept. Had the offsetting recommendations of the Commission also been adopted (chiefly, the lowering of the top marginal rates, generous averaging provisions, integration and elimination of gift and estate taxes, and to which Grant registered no objection) then the "reformed" system would have been even more regressive than the existing system, or the American system.

Commissioner Beauvais' Minority Report:

Beauvais' minority Report was considerably longer, more detailed in its supporting arguments, and somewhat more conservative than Grant's. Beauvais opposed any extension of the current income tax base, with the exception of:

> ...certain assets specified on a list, primarily securities and real estate, which were held for a certain time; the tax should be based on the measures currently applied under the United States Internal Revenue Code, so that an amount equivalent to 50 per cent of the gain should be taxable at progressive rates, with a maximum rate of 50 per cent.[230]

The maximum rate on capital gains would therefore have been only 25 per cent of the full gain, which is essentially what Grant had proposed for long-term gains. Like Grant, he regarded the majority's proposals to tax gains at "full progressive rates" as too harsh:

> In most countries in the western world capital gains are taxed at special rates; such gains arise mainly from sales of securities and real estate. If my information is correct, Canada would be the only country in the western world to tax so-called capital gains at full progressive rates and, what is more serious, to tax these gains on a deemed realization basis at death.[231]

Like Grant, Beauvais also favoured the use of holding periods, similar to that used in the United States federal income tax system. He quoted a passage in the majority Report criticizing the American system because it perpetuated the distinction between "carrying on business" and "investing", without reference to the majority's arguments against the holding periods or why they considered the distinction between "carrying on business" and "investing" to be "so

unpalatable".[232] As we have seen, it was the uncertainty resulting from attempts to draw this distinction which had resulted in much of the tax litigation in Canada and Britain, and which had been one of the sources of dissatisfaction with the tax system motivating demands for tax reform.[233] Beauvais did not offer any argument in support of his own preference:

> I do not agree with the above mentioned assertions and, in so far as the United States concept of distinguishing between "carrying on business" and "investing" is concerned, I agree with it.[234]

Beauvais did defend preferred tax treatment for property gains on the grounds that capital gains, as opposed to employment income, arose from risk-taking:

> According to the Report, for a tax to be imposed equitably, a wage earner who pays for his car by working overtime and a fellow worker who uses his net gains from the stock market to acquire a car should get an equal tax treatment. I cannot share this philosophy. The wage earner does not take any risk, whereas his fellow worker, who uses his net gains from the stock market to acquire a car takes the risk of losing his savings.[235]

Given the highly concentrated distribution of capital gains income among wealthy taxpayers, it is unlikely that the typical recipient of enough capital gains income to purchase a car would have been the "fellow worker" of the wage earner who bought his car by working overtime. Nor does the analogy take into account the risk taken by the worker in terms of his safety on the job, and the effects of his work, including overtime, on his health. The wage earner, in addition to being subject to possible layoffs and other dislocations beyond his prediction or control, would (other things being equal) have had a

shorter "working-life expectancy" than the man who could afford to live passively off capital gains. Though neither the majority nor the minority reports did so, one might have argued that the wage earner faced somewhat greater risks and impediments than the owner of capital sufficient to earn the same income. The use of the term "wage earner" might also have suggested the principle of vertical equity in the question of the taxation of capital gains, though Beauvais referred only to their argument based on horizontal equity.

Beauvais' discussion of risk-taking in the context of the taxation of capital gains did not refer to the offsetting provisions of the majority proposal to allow full deduction of most realized capital losses and of costs required to earn capital gains, though they would have been relevant in evaluating the degree of risk of any investment.[236]

Like Grant, Beauvais opposed deemed realization of capital gains on death. He referred to the majority Report's comparison of two taxpayers having identical lifetime incomes, one having liquidated all his assets the day before dying, the other dying before any liquidation, and disagreed with the Report's conclusion that both taxpayers or their estates should bear the same tax burden since they had identical taxpaying capacity. They were different because each had made free but different choices:

> Both taxpayers had the opportunity of selling their assets and realizing their gains or losses. I do not see the necessity of taxing deemed realizations on death because the first taxpayer took the choice of selling his assets at a certain date. I do

> not see anything wrong in requiring the federal government to wait until a gain is realized, whether it be before or after the death of a taxpayer.[237]

While Beauvais implied that nothing would be lost in waiting, the Commission's study of the American income tax system had indicated that a substantial portion of the revenue was lost as a result of no provision for deemed realization of accrued gains on gift or bequest. Largely as a result of this, the overall income tax system was, at best, only proportional over the upper income range.[238]

Beauvais noted the Report's contention that any liquidity problems for the shareholder of a closely-held corporation did not warrant the introduction of complex provisions that would lead to greater uncertainty and tax avoidance, and simply countered that assertion with one of his own:

> To me it is very important that the shareholder should have the cash available to pay whatever tax might be due as a result of a transaction. The averaging provision might decrease his tax liability somewhat but would not provide him with the cash required.[239]

During the Commissioners' discussion of the question of deemed realization of accrued gains on death, Beauvais had not been persuaded by Geoffrey Conway's argument that the rates on the Estate could have been lowered as a result of increased revenues from the Income Tax.[240] In fact, the Report finally recommended not just the reduction of rates on the Estate Tax, but the outright abolition of estate and gift taxes. Moreover, the Commission's adoption of the family as the unit of taxation meant that there would be no tax

payable at all on property passing to the surviving spouse or to dependent children.[241]

Beauvais acknowledged that this was "a step in the right direction", but that more generous exemptions should have been allowed for gifts and bequests, apart from those between members of a family unit.[242] He illustrated the hardship that could be caused by taxing such transfers at progressive rates by calculations based on the receipt of a $100,000 bequest by a taxpayer earning $10,000 a year in employment income. He chose a set of assumptions most favourable to his case: that the donee had used up his proposed [$5,000] lifetime exemption; that the donee's Registered Retirement Income Plan limit had already been reached; and that no use was made of the proposed Income Adjustment Account. In addition, there was the implied assumption that the donee did not have a spouse with an additional $5,000 lifetime exemption for gifts and bequests.

Beauvais' calculations showed that this hypothetical donee would, under the Commission majority's system, have to pay $35,510 in income taxes over five years on a total of $150,000 income, including his normal employment income. Under the existing tax regime, the taxpayer would owe a total of only $18,420 over the same five-year period. Beauvais expressed the difference in tax as a percentage of the liability under the existing system to show that the new system would impose a 93 per cent increase on the taxpayer in question. However, he did not express the "before" and "after" tax burdens as percentages of the total income received in each case. Doing the calculations

ourselves, we get a "before" average rate of 12.28 percent, and of 23.67 per cent under the Carter proposals. Put this way, even the latter, heavier burden does not seem quite so harsh, especially when we remember that the "high" rate does not represent a typical case, but a transfer to someone other that the surviving spouse or dependent children, and that the lifetime exemption and averaging devices were ruled out by Beauvais' assumptions. Moreover, the ability to spread the payment of the tax over several years under the majority proposal would result in a lighter effective tax burden than Beauvais' figures suggest.

The majority Report had performed analogous calculations on the receipt of gifts of various amounts by a married couple (only one of whom was assumed to be earning an income) with three dependent children, and having an annual "before-gift" income ranging in different examples, from $6,500 to $25,000.[243] Aside from the characteristics of the family unit, the same assumptions were made as in Beauvais' example, with the addition of the use of the Income Adjustment Account. For a gift of $100,000 received by a family with normal annual employment income of $10,000, the average tax rate on all income would have been 18.5 per cent.[244]

Beauvais concluded from his figures that "If the bequest was in a non-liquid form, the treatment would certainly be very harsh."[245] While acknowledging that the Report had recommended that, in situations where payment of tax on non-liquid assets would create serious problems, the taxpayer be allowed to apply for the privilege

of paying the tax in instalments, Beauvais proposed that "bequests be granted a treatment similar to that of capital gains and taxed at the preferential rate suggested in my report."[246] Combined with the removal of what Beauvais (and Grant) had called "double taxation" of accrued gains at death,[247] not only would donees outside the family unit have been entitled to receive gifts and bequests at about half the rate of tax imposed on most other income, but the total amount of such transfers (due to the preferential tax treatment of capital gains) would be substantially increased.

One of the most remarkable parts of Beauvais' minority report was his objection to the proposal for the integration of personal and corporate taxes on the grounds that it would result in windfall gains for wealthy shareholders:

> I acknowledge the fact that it would greatly simplify the taxation system if such a recommendation were adopted, but I cannot reconcile myself to the idea of wealthy people receiving such a windfall in cases where no special transition tax was paid or in cases where such a tax would be paid when the transitional period had ended. The loss in government revenue from taxes on dividends would have to be compensated for by increasing other taxes which might fall to a certain extent on middle income taxpayers.[248]

As Beauvais pointed out, the majority Report had acknowledged that, depending on the amount of shifting of the decrease in corporate tax burden, current shareholders would reap a windfall capital gain. Nevertheless, the Report had recommended integration largely for economic reasons: to improve the allocation of resources between corporate and non-corporate investment:

> We recommend the abolition of the double taxation of corporate income, not to help existing shareholders, but primarily to obtain this additional output and to eliminate differences in tax treatment between different kinds of organizations that inevitably provide opportunities for tax avoidance. The capital gains that some shareholders would obtain on the abolition of the double taxation of corporate income would be an undesireable, but inescapable, consequence of the proposal. In equity, these gains should be taxed at 100 per cent. In practice, it is not possible to distinguish these capital gains from other capital gains. However, it would be grossly unfair to allow the gains resulting from the integration proposal to escape being taxed at full rates.[24]

It is remarkable that Beauvais, who had expressed dismay over the prospect of wealthy shareholders reaping windfall gains from the introduction of the integration proposal, opposed the instrument suggested in the majority Report for moderating this windfall: the taxation at full marginal rates of capital gains, with deemed realization in gift or bequest. While Beauvais, in the context of integration, was concerned about a one-time windfall to wealthy shareholders, he did not mention the existing and, if his own proposals were implemented, future prospects for gains to the same wealthy individuals arising from the preferred treatment of realized capital gains, gifts and bequests, and from the tax-free status of accrued but unrealized gains. Beauvais considered the two questions separately, opposing each for the opposite reasons: taxing capital gains in full, accrued gains at death, and gifts and bequests at market value in the hands of the recipients were all too harsh, while the integration scheme was too generous to wealthy shareholders. Both objections related largely to the same class of taxpayers: those earning the bulk of their income from corporate property. For the majority Report the two recommendations were inseparable parts of the

same package: under the existing system, the failure to tax share gains combined with the practice of surplus stripping had "undoubtedly reduced the adverse impact of the double taxation of corporate income", while the proposed full taxation of gains would have reduced the windfall accruing to shareowners resulting from the elimination of this "double taxation".[250]

The majority Report had said that the greater proportionate windfall would go to, not wealthy shareholders, but low and middle-income shareholders. This was because of the full taxation of capital gains, which would fall to a greater extent on wealthy shareholders, and also due to the fact that, through the integration scheme, corporate income allocated to shareholders would be taxed at the shareholder's personal marginal rate. The Commission had estimated that the "goodwill" portion alone the increase in value of business property attributable to prospects for improved earnings exceeded the amount hitherto received as dividends by wealthy shareholders, and therefore, that the full taxation of these gains would fully offset any advantage to them from integration.[251]

Further on in his minority report, Beauvais came close to conceding this point:

> There is no doubt that the benefit which would be granted to wealthy shareholders would be offset to a certain extent by the proposed tax on capital gains, and by the proposed tax on gains deemed to be realized at death if any, but at first glance, it looks nevertheless like a windfall for wealthy shareholders.[252]

Beaulieu, however, had already rejected these offsetting measures as being too harsh.

The majority Report had acknowledged that, as capital gains would have been subject to tax only as realized, the growth in revenues from this source would have lagged behind the immediate loss in revenues resulting from integration. The Commission majority suggested two alternatives for closing this gap: either a general but temporary increase in income tax rates, or a special tax on corporate source income during the transitional period. The first alternative was favored for its administrative simplicity and comparative lack of avoidance problems.[263] Beaulieu objected that a temporary increase in general tax rates would force "all low income, middle income and high income taxpayers... to foot the bill in order to pay for the windfall that would accrue to high income shareholders."[264]

The majority's second alternative for a transition tax would generally have fallen more on wealthy taxpayers but would have been administratively more complex.[265] It involved the attribution of corporate surplus on hand, on which corporate tax had already been paid, to resident shareholders and taxed at their personal marginal rates. The corporation could have taken advantage of the existing provision to pay a flat-rate tax of 15 per cent on up to half of its undistributed surplus. This amount of tax paid would have been deducted from the transition tax owed by the shareholder. Hence the tax would have fallen on corporate source income that would have been subject to full progressive rates of income tax (softened by the

existing 20 per cent dividend tax credit), had that income been distributed prior to the imposition of the transition tax. The burden of the transition tax would in all cases have been less than what the shareholder would have had to pay had the surplus been distributed as a cash dividend under the existing system. The personal tax burden, with high marginal rates, was probably the main reason for corporate surpluses not being distributed. Beauvais objected to the alternative of a transition tax on corporate income as being inequitable:

> I am of the opinion that this tax would be discriminatory, as it would be levied on shareholders of corporations having large surpluses, whereas no tax would be paid by shareholders of new corporations [because they would not have any tax-paid surplus on hand] or corporations having no accumulated surpluses. Shareholders of the former corporations would be induced to sell their shares and acquire shares of the latter kind of corporation in order to avoid the payment of the special transition tax.[256]

The majority Report had answered this objection, though readers of Beauvais' minority report could not have known unless they had turned to "Appendix J" at the back of Vol. 4:

> This transition tax does not purport to be equitable in any absolute sense to the shareholder of a particular company relative to another shareholder in the same or another company. However, even though the impact of the tax might weigh relatively more heavily on some companies than on others, the potential inequities are much less serious than might otherwise appear because most shareholders have some diversification in their portfolios, often through investments in mutual funds and pension plans. High income individuals holding shares in private companies that have had low pay-out ratios in order to defer personal tax are less likely to have this diversification than others. The transition tax would be relatively heavy in the case of this group. This feature of the tax seems to us to be desirable.[257]

In other words, what Beauvais called discrimination was for the

majority Report a subtle case of the punishment fitting the crime. Shareholders of companies which had distributed their surpluses, and on which either personal income tax, or the 15 per cent tax on allocated surplus through the use of section 105 had been paid, would have little or no transitional tax to pay.[258]

Instead of the majority's integration proposal, Beauvais advocated a modified version of a proposal recommended by a Special Committe on Corporate Taxation (or "Committee of Four", of which Beauvais had been a member) to the Minister of Finance shortly before the appointment of the Royal Commission on Taxation.[259] Beauvais supported a modified version, as recommendei by the Canadian Institute of Chartered Accountants and by the Canadian Bar Association in their briefs to the Commission.[260] The proposal would have substituted the existing mode of taxing dividends with a flat-rate tax of 15 per cent on dividend income, including on deemed distributions of accumulated profits.

The Commission had given this proposal detailed consideration, perhaps partly because it already had the blessing of a Government-appointed advisory committee and was proposed by the two associations which claimed to represent most of the tax professionals. However, the Commission majority was not impressed with the refund of withholding tax having a sharp cut-off point at the $10,000 income level, since it would have encouraged efforts to manipulate reporting of income around that level. Their main objection was that the proposal failed to apply the same schedule of

progressive rates to corporate source income as to other income, and therefore did not satisfy the criterion of horizontal equity adopted by the Commission.[261]

Beauvais had a ready reply to the latter criticism:

> The Committee of Four proposed a 15 per cent tax on dividends while the Report suggests that no tax be paid thereon. Therefore, how can one conclude that the Committee's suggestion substitutes a flat-rate tax for a progressive tax borne by the individual shareholder? Because the shareholder, while calculating the tax on income from corporate distributions or allocations at progressive rates, would receive full credit for the tax paid by the corporation at a flat rate. At least if the Committee's recommendation was adopted, the government would collect an appreciable amount of revenue that would not have to be collected from other sources.[262]

While it is true that the integration proposal, in itself, would have imposed no tax, its effect would nevertheless have been progressive, since shareholders would receive tax refunds corresponding to the amount by which their personal tax rates were below the 50 per cent corporate rate. The lower the annual taxable income of the shareholder, the greater the refund. The Committee of Four's proposal did have one progressive feature: the 15 per cent tax would be refundable to shareholders with taxable incomes below $10,000, although the majority Report pointed out that this was rather clumsy and would not make the tax progressive at other income levels. The Canadian Bar Association's amended version, however, would not have included a refundable credit for low-income shareholders.[263]

The authors of the majority Report recognized that the modified Committee of Four proposal could not be combined with the proposal to

tax capital gains at full rates, considering the resulting burden on shareowners to be "both unfair and incompatible with economic growth."[264] In weighing its implications, therefore, they combined it with what they believed to be "the obvious alternative", an approach similar to the American system: "the taxation of the full amount of share gains at one-half personal rates up to a maximum of 25 per cent."[265]

In comparing the effects of such a system to the those of the Commission's proposal it was necessary to estimate the likely proportion of "goodwill gains" to all corporate source income. Using a recent survey of historical share prices dating from 1926 to 1960 on the New York Stock Exchange, the Report estimated that about one-third of corporate source income could be attributed to "goodwill gains". Using these assumptions, and a 50 per cent, single-rate tax on corporate profits, the Report showed that, for shareholders at the top personal marginal rate of 50 per cent, the total tax burden on corporate-source income under the Commission's proposals would be slightly lower than under the modified Committee of Four proposal.[266] At the 20 per cent marginal rate, the total burden under the Commission's proposals would be less than half of that proposed by the Committee of Four.[267] The major difference therefore between the two alternatives was the relief accorded to middle and low income shareholders under the Commission's integration proposal. There was little difference in the net treatment of upper income shareholders under the two systems. The Report cautioned, however, that:

> ...if, as we believe, the foregoing estimate of the proportion of goodwill gains to total gains understates the "true" picture, the difference between our proposal and the alternative approach for upper income shareholders would narrow and possibly be reversed. The greater the goodwill gain in proportion to the total gain, the less would be the tax levied under the [Committee of Four] alternative, while the tax under our proposal would remain unchanged.[268]

Since capital gains, including "goodwill" gains, were not normally taxed or reported in Canada, accurate information on their extent and distribution did not exist. However, since the Commission majority's calculations were based on an estimate of American goodwill gains which included the period of the Great Depression, it was very likely that the proportion of goodwill in Canadian share gains would have been significantly higher. In that case, as the majority Report acknowledged, the modified Committee-of-Four proposal would have been more generous to high-income shareholders.[269]

The Commission majority rejected the proposal favoured by Beauvais, not only because it did not satisfy their equity principles, but also because it would have unacceptable economic effects:

> The major difference between the two methods is the treatment of the low and middle income shareholder. The present system greatly overtaxes the low and middle income shareholder relative to the upper income shareholder if the progressive rate schedule is used as a standard. The [modified Committee-of-Four] alternative approach reduces this vertical inequity. Our proposal removes it entirely. Another difference is that our proposal would make holding Canadian equities more attractive to low and middle income resident individuals and less attractive to upper income resident individuals. The alternative approach would make holding Canadian equities less attractive for all but those upper income individuals who are now paying extremely high marginal rates on their cash dividends. The alternative system might therefore tend to depress share prices and discourage capital expenditures by corporations. Certainly it would perpetuate the adverse effects on resource allocation that characterize the present system.[270]

Beauvais' rejoinder was that the majority's integration proposal would not have made Canadian equities significantly more attractive to low and middle income Canadians, since low income individuals did not tend to buy shares in any event.[271] While the question of the investment behaviour of low and middle income individuals under the two proposals must remain hypothetical, there is no doubt that their after-tax cash return would have been substantially increased under the majority proposal. To the extent that these individuals had cash to save, Canadian equities should have appeared relatively more attractive than other forms of saving than had previously been the case, or than under the modified Committee of Four proposal.

The majority judged the modified Committee of Four proposal to suffer several other serious drawbacks. It would, by depriving low income shareholders of a refund for corporate income tax paid, have made the removal of the "small business rate" of corporation tax inequitable. Hence, the tax avoidance problems with associated corporations would remain, along with the vertical inequity of allowing this benefit to high-income shareholders. Taxing capital gains at half rates would have perpetuated the problems of distinguishing between income and capital gains, and would have left opportunities for tax avoidance. Corporate income would continue to have been taxed differently from other business income, a violation of the Commission's goal of neutrality. Finally, assuming that all capital gains would have been taxed at half rates, the majority could see no justification in equity for such a concession.[272]

Conclusion

The Carter Report met Douglas Hartle's ambitious criteria for a Royal Commission Report of lasting significance. It was an encyclopaedic document. Almost every alternative in tax policy which might have seemed reasonable to even a small minority of Canadians was given some consideration. The various parts were coherently linked by the common theme of the comprehensive tax base, itself systematically developed from the basic principles of tax equity. Each recommendation was explicitly defended with reference to those principles, and to the other objectives adopted by the Commission.

In spite of the Commission's stated intentions, however, it did not consistently give equity priority over other goals and constraints. When equity had to take second place, it was either to practical problems of administration (such as the valuation problem for accrued gains), or "economic realities", such as the perceived necessity to keep the top marginal rate no higher than 50 per cent in order to provide sufficient incentive for foreign investment capital). Whenever the equity goals had to be compromised, the result was generally in the direction of reduced effective progressivity of the proposed tax system.

While making concessions where the Commissioners believed they had to, the Report was not opportunistic. It exposed the tax privileges of certain classes, industries, and groups, some of which had reputations for being politically powerful. It was practical, in the

sense of recognizing the economic power of some groups as forces which had to be taken as problems or constraints in making recommendations, and in the sense of proposing transitional policies to avoid individual cases of hardship or inequity. Yet it was also far-seeing in that it considered tax policy within a broader perspective of general social goals and values (such as a society providing its members with equality of opportunity), and proposed long-range policies to guide future governments in moving Canada toward fulfillment of those goals and values.

In spite of concessions to the practical, the development and defence of the comprehensive tax base was, for the most part, logically rigorous yet expressed in language most (with some effort and endurance) could have understood. Almost every conceivable objection to the majority's proposals had been anticipated and dealt with.

The minority reports of Commissioners Beauvais and Grant differed from the majority Report on important applications of the comprehensive tax base. While their objections had been quite effectively answered in the main Report, the fact that two Commissioners out of six, one of them an acknowledged tax specialist, had been unable to accept some of its key recommendations, deprived the Report of much-needed credibility. The disunity among the Commissioners, after struggling with the problems of tax reform for four years, foreshadowed and contributed to the controversy about to erupt over the Report.

Notes to Chapter V

1. Report, Vol. 1, p. 2.
2. Vol. 1, pp. 2-3.
3. Vol. 1, p. 3.
4. Ibid.
5. Vol. 1, p. 4.
6. Vol. 1, p. 5.
7. Vol. 1, p. 5.
8. Vol. III, p.5.
9. Ibid.
10. Ibid.
11. Vol. 1, p. 5.
12. Vol. 1, pp. 5-6.
13. Vol. 3, p. 6.
14. Vol. 3, p. 9.
15. Vol. 3, p. 8.
16. Vol. 3, p. 9.
17. Vol. 3, p. 12.
18. Ibid.
19. Vol. 3, p. 30.
20. Ibid.
21. Ibid.
22. Ibid.
23. Ibid.
24. Vol. 3, p. 37, note no. 8. On page 165, the reason for rejecting a higher top rate was due to the resulting "unacceptable increase in the weight of taxation on equity investment income and [the]... appreciable disincentive effects."
25. Vol. 3, pp. 28-29.
26. Vol. 3, p. 154.
27. Vol. 3, pp. 154-155.
28. Vol. 3, p. 164.
29. Vol. 3, p. 23.
30. Vol. 3, p. 24.
31. Vol. 3, p. 37, note no. 7. They cited Simons' Personal Income Taxation, Chicago: University of Chicago Press, 1958), 41.
32. Vol. 3, pp. 41-42.
33. Vol. 3, p. 47.
34. Vol. 3, pp. 50-51.
35. Vol. 3, pp. 317-320.
36. Vol. 3, p. 320.
37. Vol. 3, pp. 353, 358-359, 387-391, 393, 397.
38. Vol. 3, pp. 354-55, 368-378, 394-395.
39. Vol. 3, pp. 144-149, 370.
40. Vol. 3, p. 370-371.
41. Vol. 3, pp. 371-374.
42. Vol. 3, p. 455-457.
43. Vol. 3, pp. 438, 458.
44. Vol. 3, p. 446-454, 458-459.
45. Vol. 3, p. 513-516.
46. Vol. 3, p. 524-526, 534-535.
47. Vol. 3, pp. 526-527, 535.

48. Vol. 3, pp. 528-531.
49. Vol. 3, pp. 359-368, 393-394, 397-398.
50. Vol. 3, pp. 214-221, 234.
51. Vol. 3, pp. 227-229, 237.
52. Vol. 3, p. 233.
53. Vol. 3, p. 213.
54. Vol. 3, p. 222.
55. Vol. 3, pp. 229-232, 236-237.
56. Vol. 3, pp. 262-268, 277.
57. Vol. 3, pp. 269-272, 279-280.
58. Vol. 3, pp. 273-274, 279, 421-434, 455-456.
59. Vol. 3, p. 31.
60. In the absence of conclusive data, the Report assumed that organizations had not substantially shifted the tax burden forward to its customers or backward to its suppliers of goods and services.
61. Ibid., p. 53.
62. Vol. 4, p. 5.
63. Vol. 4, p. 7.
64. Vol. 4, p. 6
65. Ibid.
66. Vol. 4, p. 9.
67. Vol. 4, p. 28.
68. Vol. 4, p. 25.
69. Vol. 4, pp. 26-27.
70. Vol. 4, p. 28.
71. Vol. 4, p. 29.
72. Vol. 4, p. 30.
73. Vol. 4, pp. 32-33.
74. Vol. 4, pp. 33-34.
75. Vol. 4, pp. 105-106, 142.
76. Vol. 4, pp. 119-120.
77. Ibid.
78. Vol. 4, pp. 121-122.
79. Vol. 4, pp. 122-123.
80. Vol. 4, pp. 124, 144.
81. Vol. 4, pp. 136-139, 144.
82. Vol. 4, p. 144.
83. Vol. 4, p. 126.
84. Vol. 4, p. 151.
85. Vol. 4, p. 156.
86. Vol. 4, p. 154.
87. Vol. 4, p. 150.
88. Vol. 4, pp. 203-207.
89. Vol. 4, p. 205.
90. Vol. 4, p. 202.
91. Ibid.
92. Vol. 4, p. 215.
93. Vol. 4, pp. 282-285.
94. Vol. 4, pp. 268-269.
95. Vol. 4, p. 270. For a discussion of surplus-stripping practices, see above, Ch. 2, pp. 57-58, 81-83, 105-109.
96. Vol. 4, p. 270.

97. Vol. 4, p. 271.
98. Vol. 4, p. 274.
99. Vol. 4, p. 276.
100. Vol. 4, p. 278.
101. Vol. 4, p. 279.
102. Vol. 4, p. 281.
103. Vol. 4, p. 282.
104. Vol. 4, p. 295.
105. Vol. 4, pp. 295-296.
106. Vol. 4, pp. 296-297, 308-309.
107. Vol. 4, p. 297.
108. Vol. 4, p. 298.
109. Vol. 4, pp. 310-324.
110. Vol. 4, pp. 308-309, 325-327.
111. Vol. 4, p. 327.
112. Vol. 4, p. 328-329.
113. Vol. 4, p. 329.
114. Vol. 4, pp. 325, 329-330.
115. Vol. 4, p. 330.
116. Vol. 4, p. 331.
117. Vol. 4, p. 332.
118. Vol. 4, p. 332, 335.
119. Vol. 4, p. 332.
120. Vol. 4, p. 333.
121. Vol. 4, pp. 337.
122. Vol. 4, pp. 337, 346.
123. Vol. 4, p. 333-334.
124. Vol. 4, p. 355.
125. Vol. 4, p. 347
126. Vol. 4, pp. 350-354.
127. Vol. 4, p. 350.
128. Vol. 4, p. 361.
129. Vol. 4, pp. 360-362.
130. Vol. 4, p. 363. Table 23-5 estimated a return of $134.75 under the proposed system, compared to $146 under the existing system, based on $100 of corporate after-tax income per share under the existing system, retention by the corporation of 50 per cent of after-tax earnings, and goodwill gain equal to the retained earnings. The greater the proportion of goodwill gains, the greater the relative loss suffered by the shareholder under the Report's recommendations.
131. Ibid. Note (h) in the same table gives comparable figures of $138 under the present system, and $96.25 under the Commission's proposals.
132. Vol.4 , p. 365.
133. Vol.4 , p. 366.
134. Ibid.
135. Vol. 4, pp. 366-367.
136. Ibid.
137. Vol. 4, p. 360-361.
138. Ibid.
139. Vol. 4, p. 364, Table 23-6. At a marginal personal tax rate of 30 per cent, the after-tax rates of return were given as $146

under the existing system, and $175 under the Commission's proposals. For a marginal rate of 50 per cent, the comparable figures were $179 and $125, respectively.

140. Vol. 4, p. 383.
141. Sec. 11 4 , quoted in Report, Vol. 4, p. 385.
142. Vol. 4, p. 386.
143. Vol. 4, p. 388.
144. Ibid.
145. Ibid.
146. Ibid.
147. Vol. 4, pp. 38[illegible], 389.
148. Vol. 4, p. 397.
149. Vol. 4, p. 398.
150. Vol. 4, p. 399.
151. Vol. 4, pp. 381, 402.
152. Vol. 4, p. 402.
153. Vol. 4, pp. 412-413.
154. Vol. 4, p. 413.
155. Vol. 4, p. 406, 413.
156. Vol. 4, p. 406.
157. Ibid.
158. Ibid.
159. Vol. 4, p. 413.
160. Vol. 4, p. 414.
161. Vol. 4, p. 415.
162. Vol. 4, p. 422, 432-533.
163. Vol. 4, p. 428, 432.
164. Vol. 4, p. 432-433.
165. Vol. 4, pp. 414, 428.
166. Vol. 4, pp. 429-430.
167. Vol. 4, p. 570.
168. Vol. 4, pp. 481, 571.
169. Vol. 4, p. 570.
170. Vol. 4, p. 571.
171. Vol. 4, p. 511. The exemption was permitted by section 28(1)(d) of the Income Tax Act.
172. Vol. 4, pp. 515-522, 572-574.
173. Vol. 4, pp. 534-536, 574.
174. Vol. 4, pp. 554-555, 575.
175. Vol. 4 , p. 558-559, 576. This exemption was conferred by section 71 of the Income Tax Act.
176. Vol. 4, p. 559-560, 576.
177. Vol. 5, pp. 53, 189.
178. Vol. 5, p. 92.
179. Vol. 5, p. 215.
180. Vol. 5, pp. 213-214.
181. Vol. 5, pp. 214.
182. Vol. 5, pp. 195-197, 214.
183. Vol. 5, p. 157.
184. Vol. 5, p. 158.
185. Vol. 5, p. 158-159.
186. Vol. 5, p. 168.
187. Vol. 5, p. 130.

188. Ibid.
189. Ibid.
190. Vol. 6, pp. 52-60.
191. Vol. 6, p. 52-55.
192. Vol. 6, pp. 48-49, 61-65.
193. The change in direct taxes, expressed as a percentage, appears more dramatic at the low end of the income scale due to the small amounts on which the percentage calculation was based.
194. Table 36-6, Vol. 6, p. 60.
195. Ibid.
196. Vol. 6, p. 50.
197. Vol. 6, p. 69.
198. Vol. 4, pp. 360-366.
199. Vol. 1, p. 105,
200. Vol. 1, p. 106.
201. Ibid.
202. Vol. 1, p. 107.
203. Vol. 1, p. 107.
204. Vol. 1, pp. 107-108.
205. Vol. 1, p. 106.
206. Vol. 1, p. 109.
207. See: Vol. 3, pp. 326-331, 335-336. See also, above, Ch. 2, pp. 107-118, and Ch. 4, pp. 261-264.
208. Quoted by Grant, Vol. 1, p. 108.
209. Vol. 3, pp. 342-343.
210. Ibid.
211. Vol. 3, p. 369.
212. Vol. 1, p. 109.
213. Vol. 1, p. 109.
214. Vol. 3, p. 350.
215. Vol. 3, p. 351.
216. Vol. 1, p. 109.
217. Vol. 2, pp. 142-165.
218. Vol. 2, p. 172.
219. Vol. 4, pp. 29-33.
220. Vol. 4, pp. 276-282.
221. Vol. 1, p. 109.
222. See above, Ch. 4, pp. 263-224.
223. Vol. 3, p. 476.
224. Vol. 3, pp. 476-477.
225. As outlined in the Report, Vol. 3, pp. 259-260.
226. Vol. 3, p. 515.
227. Vol. 3, p. 370.
228. Vol. 3, p. 369.
229. Ibid.
230. Vol. 1, p. 53.
231. Ibid.
232. Vol. 1, p. 61. Beauvais was referring to Vol. 3, p. 348.
233. See above, Ch. 2, pp. 91-101, 113-114. The reader will recall that this was the issue which finally convinced both Stewart and Carter that capital gains ought to be taxed in the same way as other income.
234. Vol. 1, p. 61.

235. Ibid., p. 61. Beauvais was referring to Vol. 3, p. 331.
236. See: Vol. 3, pp. 359-368; and Vol. 4, pp. 60, and 227-249.
237. Vol. 1, p. 62.
238. Conway, The Taxation of Capital Gains, pp. 122-128.
239. Ibid., pp. 62-63.
240. See above, Ch. 4, pp. 263-264. The Commissioners' discussion was in the context of taxing capital gains, not the inclusion of gifts and bequests in income. Once the latter was added to the proposed tax base, the case for eliminating estate taxes and succession duties was unassailable.
241. Vol. 3, p. 513.
242. Vol. 1, p. 66.
243. Vol. 3, p. 505.
244. Ibid. On the other hand, had the family chosen not to take advantage of the Income Adjustment Account, the additional income arising from the gift or bequest during the same period would have provided substantial compensation for the higher effective rate of tax.
245. Vol. 1, p. 67.
246. Vol. 1, p. 67.
247. Vol. 1, pp. 62, 71.
248. Vol. 1, p. 69.
249. Vol. 4, pp. 26-27.
250. Vol. 4, pp. 26-28.
251. Vol. 4, pp. 29-30.
252. Vol. 1, p. 76.
253. Vol. 4, pp. 77-79, 93.
254. Vol. 1, p. 71.
255. See Vol. 4, Appendix J, pp. 725-731.
256. Vol. 1, p. 72.
257. Vol. 4, p. 730.
258. See the discussion of surplus stripping, above, Ch. II, pp. 55-56, 78-80, 101-104.
259. See above, Ch. 2, p. 101.
260. Vol. 1, pp. 73-74.
261. Vol. 4, p. 38.
262. Vol. 1, p. 76.
263. Vol. 1, p. 73.
264. Vol. 4, p. 39.
265. Ibid.
266. Vol. 4, pp. 40-42.
267. Vol. 4 p. 41.
268. Vol. 4, p. 42.
269. Ibid.
270. Ibid.
271. Vol. 1, p. 81.
272. Vol. 4, p. 43.

Chapter VI: Reaction to the Carter Report

Introduction

The Report of the Royal Commission on Taxation was tabled in the House of Commons by Mitchell Sharp on February 24, 1967, four and a half years after the Commission's appointment. For much of that period the scope of decision-making had narrowed to include the Commissioners, a few key members of their staff, and a small number of tax specialists consulted at the Commission's initiative. Government actors, at both the Cabinet and senior bureaucratic levels, had also played important roles, though chiefly though imposing general limitations on the actions of the Commission. The scope of participation meanwhile appeared to have broadened to encompass any group or individual who cared to submit a brief or attend one of the public hearings in one of several cities across Canada. Although hundreds of briefs were submitted, as we have seen, these had little impact on the major recommendations of the Report.

Toward the end of 1964 and afterward, the calculations and behavior of individuals outside the Commission began to anticipate the forthcoming Report. Walter Gordon had to consider how, as Minister of Finance, and as political strategist for the minority Liberal government, the Commission's recommendations should be dealt with. The Canadian Tax Foundation was also waiting impatiently, having

planned a special tax conference to discuss the Report, and then having had to repeatedly postpone it each time the announced date of release of the Report was set back.

By the time the Carter Report was released to the public, it had already been the object of an intensive study by the Tax Analysis Unit, a special task force set up by Gordon within the Department of Finance. Beginning in the spring of 1965, the Unit acquired access to completed chapters of the Report as much as 18 months in advance of the formal submission of the completed Report. This preview, rather than enabling the government to take expeditious steps to reform the tax system, served as a warning to the cabinet of the political perils of taking any clear and early stand on the Report.

Initial reaction, including that of business, to the comprehensive tax base recommendations was not entirely unfavourable. Most tax professionals whose opinions were reported in the press saw a capital gains tax as inevitable, and some even welcomed the Report. Only the mining and petroleum interests were united and strongly opposed from the beginning.

However, the April, 1967 Conference of the Canadian Tax Foundation revealed, two months after publication of the Report, the overwhelming opposition of the tax practitioners and business spokesmen from every sector. From then on, the public debate was dominated by tax professionals and business executives, especially by those speaking on behalf of the mining and petroleum industries. The strategy of the

forces opposed to the Report was to use events which they controlled -- annual meetings of corporate shareholders, investment announcements (or of cancellations of investments) by corporate executives, industry and professional conferences, meetings of ad hoc pressure groups, and the public release of briefs to the Minister of Finance -- as occasions for making "news".

The content of the anti-Carter propaganda was aimed at undermining the credibility of the comprehensive tax base "package" and arousing fears of a flight of investment capital, which would take with it development projects, jobs and skilled people. Such fears were made more plausible by announcements of cancellation of major investment plans by several mining and petroleum companies and by predictions of wider repercussions by some provincial premiers.

All of this "taxpayer input" gave the Department of Finance more to do, thereby providing additional justification for delay in formulating the government's policy on tax reform. Delay, further study and the government's decision in November, 1967, not to accept the full Carter package signalled at least an interim victory of the anti-Carter coalition.

The Government's Response

During the four and a half years of the life of the Royal Commission, the Diefenbaker government was followed by two successive

governments under Lester B. Pearson, and all three were minority governments. The enthusiastic Conservative pro-business tax reformer, George Nowlan, had long since vacated the Finance portfolio, to be replaced by the Liberal, nationalist, and anti-surplus-stripping, Walter Gordon. Gordon, an enthusiastic tax reformer himself, though not in the sense of either Nowlan, or of the Commission majority, was in turn, replaced on his resignation in November, 1965, by Mitchell Sharp. As Sharp sensed the political winds blowing about the Carter Report, he became reluctant to undertake any legislative action on tax reform.

While the priority and desired content of any potential tax reform programme changed with each new incumbent in the Minister's office, the Commission carried on with its work, feeling now and again, the occasional buffeting of ministerial attention. A product of Walter Gordon's impatience to get on with tax reform was the Commission's agreement to allow staff from Finance to study chapters of the Report as they were completed. This had the dual effect of removing ministerial pressure from the Commission, and of separating for some time, the development of the bureaucratic response from the response at the Cabinet level.

Response at the Cabinet Level:

More than a year before the Carter Report was completed, there were already indications that the Pearson Government was undecided

about what to do with it when it was finally released to the public. Near the end of 1964, Gordon, who was also Pearson's chief advisor on party strategy, recommended that Pearson call an election during the following year.[1] Gordon warned that it would "be most difficult if not impossible... to deal successfully with a host of major issues as a minority government."[2] Fearing that the Carter Commission would "pose some awkward and controversial questions", Gordon preferred a June election in order "to go before not after the Carter Commission report... [was] published."[3]

The Prime Minister, however, decided not to call an election for June. At the end of June, following a meeting of the Liberal National Campaign Committee, Gordon again wrote to Pearson, urging him to call an election for September 27th or October 4th of that year.[4] In support of an election, he offered a number of strategic political considerations, among which was:

> ...the question of the Carter Commission Report which was expected momentarily. I was afraid it might seriously upset the business community. I said, "It is not something I would like to try to handle as a minority government."[5]

The failure of the Liberals to secure a majority following the election of November 8, 1965, in addition to being the occasion for Walter Gordon's resignation, further eroded any inclination the Government might have had to deal with the Carter Report when it was finally made public. Gordon's departure weakened the more progressive elements in Cabinet while demonstrating the strength of its conservative elements. Gordon and his Parliamentary Secretary, Edgar

Benson, were among the leaders of the reformist wing of the Party, which also was reputed to include Maurice Lamontaigne, Guy Favreau, Allan MacEachen, and Judy LaMarsh. According to Gordon, these ministers:

> ...agreed on most policy issues and consequently... had considerable influence in cabinet. As a rule, the Prime Minister, who was instinctively progressive in his approach, agreed with us -- or we agreed with him....[6]

However, the weakening of Gordon's position after the failure of the Prime Minister and Cabinet to support his 1963 budget, undermined somewhat the confidence and solidarity of the progressives in Cabinet. Feeling pressure from "certain sectors of the business and financial communities" opposed to Gordon's policies on foreign ownership of business enterprises in Canada, Pearson had been trying since the fall of 1964 to persuade him to accept another portfolio.[7]

The most prominent conservative members of Cabinet were Mitchell Sharp, Paul Hellyer, J.W. (Jack) Pickersgill, and C.M. (Bud) Drury. After the 1965 election, their ranks were greatly strengthened by the addition of Robert Winters, a veteran of the St. Laurent Cabinet, as Minister of Trade and Commerce. Following his defeat in the Diefenbaker landslide, he became President of The Rio Tinto Mining Company, chairman and chief executive officer of Rio Algom Mines Limited and British Newfoundland Corporation Limited, Chairman of Atlas Steel Company Limited and Preston Mines Limited, Vice-President and Director of The Bank of Commerce, and at least 16 other corporations.[8]

Mitchell Sharp, the new Minister of Finance was more cautious and conservative than Gordon. Both qualities had likely been developed in, and contributed toward his long career in the Department of Finance, and then as Deputy Minister of Trade and Commerce under C.D. Howe. During the latter part of the Liberals' years in the political wilderness, Sharp had been Vice-President of Brazilian Light and Power, a large Canadian multinational firm with utility holdings in Brazil. Gordon found Sharp to be one of his toughest opponents in Cabinet when social or economic reform measures were under discussion. Sharp had repeatedly tried to delay the implementation of medicare, one of the Liberal election planks from 1962.[9]

Given the divergence of members of Cabinet on social and economic policy matters, it is not surprising that they could not agree on what to do with the Carter Report. The Report itself was never actually brought before Cabinet for discussion, though it did approve the procedure for a White Paper on taxation which was later announced by Mitchell Sharp.[10] Although most Cabinet members had little understanding of tax matters, they correctly sensed that the Report would be very controversial and dangerous to the survival of the minority Liberal Government. A White Paper would allow them to postpone taking action on it or committing the Government to a particular position until they had some idea of the public attitude toward tax reform.[11]

The first official indication that the Government had not yet

decided what stand it would take on the Report was given by Sharp in a January, 1967 address to the Canadian Club of Toronto, about a month after the Commission had formally submitted its full Report to the Government. After announcing his intention to table the Report in the House by March, he expressed the view:

> ...that the public and particularly the lawyers and accountants should have some months to read, study and comment upon the report before the government formulates its position on the recommendations.
> That is our intention. Moreover, I hope it will be possible to give the tax experts more than the normal time to look at the various pieces of legislation introduced by the government before Parliament is asked to take final action.[12]

T.C. Douglas suggested in the House that the Report be referred to the Standing Committee on Finance, Trade and Economic Affairs, which could then have served as a forum for parliamentary and public debate.[13] Sharp rejected this procedure in favour of the presentation by the government of a draft bill, which after "a reasonable opportunity for discussion", could be referred to a committee "for discussion when representations could be made."[14] During the next two months, however, as the government was able to estimate the temperature of public reaction, Sharp had second thoughts on the wisdom of responding to the Carter Report with a draft bill, opting instead for a white paper stating the government's tentative position on the issues dealt with in the Report.

Bureaucratic Response: The Taxation Division

Although the Minister of Finance relied on several divisions within the Department for advice on tax policy, including those of Economic Analysis, Federal-Provincial Relations, and International Economic Relations, his primary source was normally the Taxation Division. Growing out of the Office of Taxation Investigation, headed by A. Kenneth Eaton since the 1930's, the Division had traditionally been very small. For some time after the War, it included only Eaton, J. Harvey Perry and E.H. (Ernie) Smith. During the time when the Carter Commission was conducting its taxation studies with a professional research staff of over forty, the Taxation Division still had only half a dozen officers. At this time F.R. (Ray) Irwin was the Director, reporting to Claude Isbister, Assistant Deputy Minister responsible for Taxation, Federal-Provincial Relations, Pensions and Social Insurance.

With its small size and consequent limited degree of staff specialization, the Taxation Division had difficulty coping with the increasingly heavy load placed on it by the sophisticated avoidance techniques of tax professionals, and the pressures from the Department of National Revenue[15] and from outside government to close loopholes, the lobbying activities of business interests and their tax advisors, the representations from tax lawyers and accountants on "technical" matters, and the increasing use of the tax system by Ministers of Finance for purposes of economic regulation.

> much punch in the polling booth. Again and again, the report stresses the advantages to the great mass of taxpayers in the proposed lower rates of personal income tax. This, it is clear, is relied upon as the great selling point -- the one that will make the proposal popular with the masses and hence with the government.[34]

Ben Dworkin, in Tuesday's Citizen, repeated what a number of securities traders had already said in early press reports, that Canada was the last major Western country without a tax on capital gains, and that such a tax had been due for a long time.[35]

John Meyer's column, "It's Your Business", in the Montreal Gazette, provided his readers with some of the most factual and perceptive commentary on the Report. In his column of February 27th, he was cautiously favourable, remarking on the logical consistency of the inclusion of capital gains in the tax base with the Commission's over-riding goal of equity, defined in terms of ability to pay. He also noted the point made in the Report, that the petroleum depletion allowances and tax holidays gave $150 million, mostly to eight companies, and that this was equivalent to four points of the total corporate income tax revenue.[36] The following day, he discussed the "package deal", including capital gains, integration, averaging and the 50 per cent top rates, but observed that:

> 'The Street' fears the possibility, in spite of the Commission's warnings, [that the government] ...might impose the tax upon gains in the stock market without also adopting the accompanying offsets. If this were to happen there is no doubt that the market would be dealt a severe, and unjustified blow.... The temptation to extract only the capital gains tax from this package and to leave the rest is dangerously strong for government, too strong for the Street to ignore.[37]

The slow growth of the Division was not sufficient to enable it to meet the peak loads resulting from periodic challenges in tax policy. As a result, the tasks of analysis and policy development were shifted during such trying times to ad hoc bodies, such as the Ives Commission on the Taxation of Annuities and Family Corporations, the Royal Commission on Co-operatives (both in 1944); the Committee of Four set up in 1960 to recommend, among other things, methods of dealing with the surplus stripping problem; the Carter Commission in 1962; and the three "outsiders" recruited by Walter Gordon in 1963 to prepare a budget within sixty days to reverse the trend toward foreign control of the economy.

Believing the Taxation Division to lack the capacity to analyze the massive Report expected in a few months, Gordon again felt he had to resort to "outsiders".

Development of the Tax Analysis Unit:

As a result of Gordon's pressure on the Commission to deliver the Report by the end of 1964, and convinced by Hartle's argument that an early completion date was out of the question, Carter decided to give the Department of Finance access to the full content of the Report as soon as the chapters had taken final form.[16] The first chapters were not actually sent until May 12, 1965.[17]

Late in 1964, in anticipation of the Commission's Report, Gordon had asked the directors of the Canadian Tax Foundation to supply a list of individuals who could act as consultants to the Deputy Minister. From the three names submitted, Gordon selected James R. Brown, a chartered accountant from Peat, Marwick Mitchell and Company of Toronto, who was hired on an 18-month contract to "review and analyse the Carter recommendations for the Department".[18]

Brown met with Carter in the spring of 1965 and began recruiting his team during the summer and fall. By the spring of 1966, what had become known as the Tax Analysis Unit included nine officers. Six were on temporary contract with the Department: A.E. John Thompson, C.A. from Price, Waterhouse, and a former Supervisor of Tax Structure Studies with the Carter Commission; E.G. Miller; Donald R. Huggett, C.A., of Coopers and Lybrand in Montreal; D.W.V. Dickerson, a chartered accountant and member of the British Columbia bar, with a doctorate in taxation law from the London School of Economics; Richard W. Collins, formerly of the statistics staff of the Carter Commission; John B. Tinker, a tax lawyer with Blake, Cassels and Graydon, and one of the small group who had worked on the final writing of the Carter Report; and Robert Bourassa, who had been Research Director for the Bélanger Commission studying the Quebec tax system.[19] Three others were on loan from the Taxation Division for varying periods: J.B. Smith, a specialist in international taxation; H. David McGurran, who had been working in corporate and international taxation, and had also been seconded from the Department to the Research Staff of the Carter Commission; and C.D. Pierre Bernier, who had also served on the

Research Staff of the Carter Commission.

The preview of the Carter Report which the Tax Analysis Unit had accorded Bryce and his new Minister, Mitchell Sharp, persuaded them that the Royal Commission route to tax reform, far from defusing a potentially explosive issue, had instead made such an explosion seem more likely. Although Sharp's original schedule called for the release of a white paper at the end of 1967 and draft legislation for the following year, the overwhelmingly negative reaction of business and the tax professions to the Report cooled his eagerness to proceed with tax reform. Meanwhile, Brown and the Tax Analysis Unit continued working more-or-less independently on feasibility studies of the Carter recommendations, and on alternative proposals.[20]

By the end of February, 1967, with the long-awaited Report at last in the public domain, tax reform became an issue to be dealt with in the short-run. This implied the merging of the Tax Analysis Unit and the Taxation Division, to effectively process the representations concerning the Carter recommendations which Sharp had invited, continue the analysis of the Report itself, and to prepare a statement of the government's position and eventually, a draft bill. The first official indication of such a move was the announcement of Brown's appointment in March, 1967, as "Senior Tax Advisor", a permanent position created especially for Brown, with a rank equivalent to Assistant Deputy Minister, and responsible for "tax legislation, including the general supervision of the work of the Tax Policy Division and the Tax Analysis Unit".[21]

Reception of the Report in the Press

The Commissioners and their staff had been aware that the Report would have to be "sold" to the government, the politicians, and the voters. The Report was therefore written in non-technical language where possible so that the educated layman could comprehend, and be convinced, by the apparently inexorable logic of the Commission's argument. Highly technical material which was considered essential to a rigorous defence of the recommendations, was put in appendices at the back of each volume.

Anticipating that many tax professionals would denounce the Report, the Commission wanted journalists to derive the bulk of their analysis from a first-hand reading of the Report itself rather than from the comments of tax practitioners. Using the "lock-up", which was customary at budget time, reporters were allowed to examine a 100-page press release summarizing the Report in language suitable for journalistic reporting and the Report itself, several hours in advance of its release to the public. Staff members were present in the lock-up to answer questions, in the hope that the initial reporting might as a result be reasonably factual.[22]

Initial Newspaper Coverage

The Commission's strategy seemed to have succeeded, as the press coverage was reasonably balanced and factual during the initial week following its release. Later on, as opposition from business and the tax professions gathered momentum, the weight of opinions expressed in print shifted decisively against the Report.

The Report dominated the newspaper front pages of Saturday, February 25th, and continued to be a major news item the following week. Much of this early reporting highlighted the themes of tax equity, ability-to-pay, and the rationale for the comprehensive income concept. The headline of Saturday's Vancouver Sun read, "Tax-The-Works Report Would Aid Mr. Average -- No More Dodges Under New Plan", with a sub-heading, "While Lower Wage Canadians Gain -- U.S. Investors and Oil Industry to Pay".[23] In addition to the main story on the first page, there were three pages of reporting on the inside pages. La Presse carried similar headlines: "Pitié pour le contribuable moyen et impôts plus lourds aux societés", with the subtitles, "La Commission Carter croit ainsi réduire les injustices dans le domaine fiscal" and "Le salarié, vainqueur du combat fiscal".[24] The Montreal Gazette's headline was evenly balanced: "Carter Tax Proposals in General Well Received But Plan to Abolish Mine Incentives Criticized".[25]

Other newspaper headlines however emphasized negative aspects of the Report, or portrayed it in an unfavourable light, like the Calgary

Herald's headline, "Market May Get Bearish Over Report", followed by a story which warned that banks, life insurance companies, oil companies, and mines were:

> ...only the leaders in the array of firms whose tax status would be altered, probably for the worse, by the Carter scheme of taxation.... and over all is the great psychological impact of a proposed capital gains tax -- at full rates -- an innovation stoutly resisted from the beginning of Canadian economic development.[26]

The Globe and Mail's story line, "Minority reports call capital gains proposal too harsh",[27] and the Hamilton Spectator's "'Too Stringent' -- Already 2 Disagree",[28] were typical of the prominent coverage given to the two minority reports of Beauvais and Grant. Under the heading, "Quebec Opinion", Monday's Globe and Mail reported that Beauvais thought Quebec would oppose certain recommendations, especially those dealing with collection of income and sales taxes, adding that he felt that those recommendations infringed on the rights of the provinces. Beauvais said that, in general, however, he agreed with the Carter Report despite his minority report.[29] The same issue also reported Carter's interview on the Toronto radio station CFRB, under the heading, "Carter thinks report to be adopted".[30]

Other Toronto papers printed stories in their Monday editions which reflected unfavourably on the Report. The Telegram reported the views of Morton Schulman, Toronto's Chief Coroner, and highly successful financial speculator under the heading, "No new millionaires, says Shulman". The story reported that, while he preferred the U.S. system of a flat rate of 25 per cent on stock held

a minimum of 6 months, he said the capital gains tax would "be a good thing but it ...[would] make a tremendous difference to big money earners in Canada. I made a million but no one else can if the recommendations are accepted."[31] The same edition summarized the early reaction to the Report with the headline, "Carter gets the cold shoulder ...majority business reaction today".[32] Even the Toronto Star, which was clearly sympathetic toward the Report, featured a story by Robertson Cochrane which highlighted and probably exaggerated difficulties of record-keeping for the average taxpayer if the Carter proposals were implemented. While it would mean lower taxes for many, Cochrane admitted, it would also mean more headaches for them at tax time, and more business for accountants and tax consultants.[33]

Columnists:

Many newspaper columnists dealt with the Carter Report during the week following its release. Southam's Charles Lynch correctly perceived the Commission's strategy for selling its Report to the voters and politicians:

> You're going to find something to like about the Carter Report unless you are:
> - a stock market speculator living off capital gains
> - an oil prospector
> - a big expense account operator
> - the owner of an insurance company
> - a provincial premier
>
> ...[although] the Commission said that it had closed its eyes to political implications of its recommendations ...obviously the commission was not that naive, and the report makes clear that those who would be hurt under the proposed new tax structure are those who do not pack

> much punch in the polling booth. Again and again, the report stresses the advantages to the great mass of taxpayers in the proposed lower rates of personal income tax. This, it is clear, is relied upon as the great selling point -- the one that will make the proposal popular with the masses and hence with the government.[34]

Ben Dworkin, in Tuesday's Citizen, repeated what a number of securities traders had already said in early press reports, that Canada was the last major Western country without a tax on capital gains, and that such a tax had been due for a long time.[35]

John Meyer's column, "It's Your Business", in the Montreal Gazette, provided his readers with some of the most factual and perceptive commentary on the Report. In his column of February 27th, he was cautiously favourable, remarking on the logical consistency of the inclusion of capital gains in the tax base with the Commission's over-riding goal of equity, defined in terms of ability to pay. He also noted the point made in the Report, that the petroleum depletion allowances and tax holidays gave $150 million, mostly to eight companies, and that this was equivalent to four points of the total corporate income tax revenue.[36] The following day, he discussed the "package deal", including capital gains, integration, averaging and the 50 per cent top rates, but observed that:

> 'The Street' fears the possibility, in spite of the Commission's warnings, [that the government] ...might impose the tax upon gains in the stock market without also adopting the accompanying offsets. If this were to happen there is no doubt that the market would be dealt a severe, and unjustified blow.... The temptation to extract only the capital gains tax from this package and to leave the rest is dangerously strong for government, too strong for the Street to ignore.[37]

Meyer was doubtful about reducing resource incentives, and noted the difficulty of trying to project the implications of such revolutionary changes. On balance however, he thought it was "a worthwhile gamble".[38]

Most columnists, however, were less impressed with either the Commission's strategy or the substance of its Report. Some wrote about the ideological pre-suppositions of the Report and its implications for the future direction of Canadian society. W.L. Clark, in Saturday's Windsor Star, called the Report a "bitter disappointment" for recommending that the tax burden be simply "spread around", rather than that it be reduced in total along with a reduction in government spending.[39] Lubor Zink, writing in the Toronto Telegram under the heading "Carter concept strictly a welfare state outlook", said there was already too much redistribution and economic nationalism for a developing country like Canada.[40] Fraser Robertson's Tuesday column in the Globe and Mail bore the heading "Carter Report: A Weighty Voice of Dissatisfaction with Business":

> The central point of attack in the Carter Report is upon the profit motive. Simultaneously the belief is advanced that people are more likely to get what they want from governments than from business and businessmen. That is a sharp reversal of the system on which the society and economy of this affluent continent have been raised.[41]

The following day Robertson, predicted that the government would disregard the "package deal" strategy and instead, like it did with the Porter Commission Report, pick and choose which

recommendations to accept. As a warning to those in government charged with making those decisions, he noted the climate of uncertainty in business circles created by speculation about the Report.[42] Pat Carney, in Monday's Vancouver Sun, stressed the disadvantages for middle-income people, including workers, and suggested that people did not value equality highly enough to give up hope of becoming wealthy, or at least economically independent.[43] Readers of the Winnipeg Free Press were told by Maurice Western that implementation of the Carter equity principle, might increase taxes for all above $10,000, or even $8,000, and that the Report was too harsh on foreign investment and the mining industry.[44] R.W. Queen-Hughes told the readers of the Winnipeg Tribune that the comprehensive income principle meant that everything was to be taxed.[45]

Others, while finding the ideas in the Report to be desirable, warned that implementation would be impossible. Jean Autane, writing in L'Action Québec, expressed a widespread view among journalists and editors, that the power of vested interests, including the provinces, would ensure that the Report would simply gather dust in the Archives.[46] Jack McArthur, however, writing in Tuesday's Toronto Star disagreed with the opinion that the Carter tax system was impossible in a federal country like Canada:

> The critics don't address themselves to the question of whether the proposals are bad or good. They just say they are 'impossible' because of divided jurisdiction and jealousies on either side. They are only impossible

> if we convince ourselves they are impossible -- something we seem intent on doing.[47]

Newspaper Editorials:

Of the 80 newspaper editorials in the Commission's file of press clippings published between February 25 and March 1, 1967, 23 (or 29 per cent) were generally favourable to the philosophy and major recommendations of the Report. Sixteen (or 20 per cent) were mixed or uncertain in their views, while a bare majority, 41, were generally opposed. The editorials praising the Report usually cited the goals of equity, ability to pay, and the elimination of tax loopholes and special privileges. Most noted that a large majority of Canadians would have their taxes reduced if the Carter recommendations were accepted, and portrayed a tension or contradiction between the general interest (to be served by implementation of the Carter Report as a package), and special interests which would try to have particular parts of it shelved.

Of 27 editorials which focussed their criticism on the comprehensive tax base, and the contents of which were analyzed, the items most frequently criticized were the taxation of capital gains (9 cases), the threat of "big government" intruding into private life (11 cases) in order to redistribute income (6 cases). Eight said that the complexity and package nature of the proposals required careful study before action was taken, and concerns were expressed in 6 editorials about the riskyness of the proposals, especially regarding the

incentives for capital investment.

Editorial Praise -- Equity, Courage and the Common Good:

The Peterborough Examiner drew attention to the benefits which the Carter recommendations would bring to the great majority of taxpayers, but warned that the government would meet "intense and diverse opposition" from special interests, and would be tempted to implement only the politically popular parts:

> The temptation to do this may be strong as opposition develops. But each year the increasing enlightenment of the electorate makes it less feasible. It will in the end be a foolhardy government which ignores the popular will in this regard. For this is the trump card of the Carter report, that it seeks to benefit all Canadians.[48]

The Toronto Star was less sanguine. In the first of three editorials, entitled, "Lobbyists will menace Carter tax reform", it warned that the current rumblings from business groups were only a prelude to a powerful lobby to get the Report shelved:

> Ordinary Canadians, who stand to benefit, must find voices of equal strength or tax reform will be riddled with exceptions and exemptions to the point of uselessness. For the broad public, the stakes are justice in taxation, better allocation of resources in the economy, and a chance to take part more directly in Canadian industrial growth. The Star supports the central principle of the Report -- the progressive taxation of a comprehensive income base.[49]

The Star predicted that the opposition would come from banks and insurance companies, oil and mining companies, the very rich, and also

"the little interests" such as credit unions, co-ops and labour unions, but hoped that these latter interests would be persuaded by the overall progressive slant of the recommendations, relieving low-income earners. The Star continued to pursue its quarry in editorials the following Tuesday ("Oil men don't need tax gifts from Canada")[50] and Wednesday ("Cheap tax ride for Canada's insurance giants").[51]

The Windsor Star took a similar position, calling for implementation of the Carter package:

> These recommendations have a great potential for both the individual and the country as a whole. The Commission has been courageous. It is essential that the Government also be courageous. It would be most unfortunate if this report were handled on the basis of political expediency rather than on the basis of the national welfare.[52]

Support for this view came even from one of the major business weeklies, the Financial Times, in an editorial entitled, "A test of courage":

> No previous royal commission has presented a Canadian government with so stern a test of political courage as the Carter Royal Commission on Taxation.
> And therein lies the gravest threat to its survival....
> Many of the Carter recommendations are politically attractive. The temptation to adopt them at the expense of the less attractive will be enormous. With a federal election only a year or so away, the temptation may prove to be irresistible.
> It must be resisted. No change at all in the present system would be better than a piecemeal selection of Carter based solely on political palatability.[53]

"It's Politically Unrealistic":

Many newspaper editorials, regardless of whether or not they agreed with the idea of the comprehensive tax base, said that the political obstacles to its implementation were too great. The Montreal Star, in an editorial entitled, "Trouble Ahead for Carter Report", noted the political unrealism of the Commissioners in their insistence on the major recommendations being accepted as a package:

> All or nothing in politics is usually nothing, not because politicians are unwilling to try necessarily, but because no political solution is that simple. There are just too many pressures, too many conflicting interests.[54]

The Hamilton Spectator also agreed that such a fundamental reform, even for a unitary state, was "...usually beyond the scope of elective democracy. There are too many pressures, too many influences, for absolute action."[55] The St. John's Telegram also warned of the political obstacles facing implementation of what they saw as revolutionary proposals.[56]

"The Provinces Will Oppose It":

A major source of those pressures was expected to be the provincial governments, unwilling to allow the federal government to control personal and corporate income taxes. Claude Ryan, in an editorial entitled, "Le rapport Carter: souci de l'efficacité et de la justice mais trop peu du federalisme" praised the Report's accent on

equity and justice and the depth of its research. While favouring the comprehensive income concept, however, he expressed reservations regarding the recommendations on the taxation of co-operatives and caisses populaires, and the failure of the Report to recognize the federal reality of Canada.[57] The latter view was shared by Quebec's L'Evénement[58], Le Nouvelliste of Trois Riviéres (which also noted the dissent of the Commissioners it called the representatives of Quebec and Nova Scotia)[59], Montréal Matin, which feared that the Report would be used by Ottawa against the provinces,[60] and by L'Action, which also opposed the recommendations concerning co-operatives.[61]

The initial editorial in Montréal Matin, was representative of French-language editorials in Quebec:

> ...la Commission n'a pas eu le moindre pensée pour les provinces et, à plus forte raison, pour le Québec. Ce qu'elle propose, c'est un régime fiscal unifié, centralisateur. Ottawa sera le maître incontesté de l'économie et il orientera à sa guise sans que les provinces puissent lever le petit doigt.
> Ces gens ont raisonné en comptables, non en politiques. Ils ont soupesé des chiffres non une constitution. Ils ont fait grosso modo, ajoutant un million ici, soustrayant un million là, ils ne sont pas embarassés de détails de langue, de culture. Comme entreprise de nivellation, il est difficile de trouver mieux.[62]

La Press predicted that the Report would likely gather dust like other royal commission reports, because any attempt to implement it would encounter the opposition of provincial governments, especially that of Quebec. It was most critical of the centralizing effect of the recommendation that Ottawa recover full use of personal and

corporate income taxes, which would be a severe retreat from the energetic demands of the Quebec government:

> Dans son ardent désir d'efficacité, de simplicité et d'uniformisation, la Commission Carter semble tenir peu compte des gains acquis de haute lutte, en ces dernières années par les provinces. Tout en réclamant la part du lion pour l'administration fédérale, elle exige quand même l'établissement d'organismes de consultation. C'est là l'un des paradoxes sinon l'une des contradictions que l'on décèle dans ce rapport.[63]

The editorial compared it unfavourably with the Bélanger Report on the tax system of Quebec, and predicted stiff opposition from the petroleum industry and financial institutions to the capital gains and corporation tax recommendations. While conceding the comprehensive income concept to be excellent in theory, it was potentially difficult in application, including as it did family allowances, strike pay and unemployment insurance payments.[64]

The Montreal Gazette, while somewhat more sympathetic to the Report, shared the pessimistic appraisal of most other Quebec papers on the prospects of the Report being implemented. The Commission's plan would have to overcome the power of entrenched interests and require:

> ...an immense degree of harmony with the provincial governments ...for its successful operation.... This is not a pragmatic approach. The question remains whether a report, to which so much care and original thought have been devoted, may defeat itself by not sufficiently coming to terms with the art of the possible, or the probable. The insistence that the report has to be accepted on the basis of all or nothing, risks everything in aiming for all.[65]

Similar warnings were uttered by the Ottawa Citizen[66] and the Globe and Mail.[67] The latter paper, in the first of several editorials on the Carter Report, entitled "Other roads to tax equity", highlighted the concerns of Beauvais and Grant, especially on capital gains:

> ...their reservations should be the first to be examined. They should be kept at one's elbow while the full report is read, and taken into account along with the Commission's acknowledged awareness of constitutional issues that in themselves could do much to frustrate what Mr. Carter has called the movement 'in gradual and orderly fashion from where we are now to where we should be'.[68]

"A capital gains tax would hurt investment":

Even some editorials which praised the Report for its espousal of equity, justice, ability to pay, nevertheless wondered whether implementation of the recommendations might have an unfavourable impact on capital investment. The London Evening Free Press was typical in its comment that the taxation of capital gains was "controversial indeed, at a time when the country is crying out for domestic capital investment."[69] The Calgary Albertan, while approving of tax equity, questioned the wisdom of removing the tax incentives for the petroleum and mining industries.[70]

The Fredericton Gleaner's editorial emphasized on the argument against taxing risk capital:

> A capital gains tax is a penalty on the use of risk

> capital at a time when the need is for Canadians to invest their own capital in their own enterprises. The Carter plan would deter them.[71]

The editor bolstered his position with the observation that two of the Commissioners had thought that the majority Report had gone too far in this regard.[72]

The Sault Ste. Marie Star, told its readers (incorrectly) that the Report would not have permitted the deduction of capital losses.[73] The Montreal Gazette cited the opposition of the Canadian Chamber of Commerce as cause for concern over the taxation of capital gains.[74] The Globe and Mail opposed the deemed realization of accrued gains on death, and when an heir reached the age of 21. Failing to mention the averaging provisions, the Globe said the proposal would prevent leaving a modest estate to one's children and force the sale of Canadian businesses to foreigners.[75] The Medicine Hat News opposed the taxation of capital gains, yet approved of integration and the removal of estate taxes, two of the features which the Commissioners had intended to off-set the increased burden to the wealthy and to investors arising from the taxation of capital gains. That paper also called for a non-government study of the Report, perhaps by the Canadian Tax Foundation.[76] The Moose-Jaw Times Herald took the opposite position, approving of the taxation of capital gains, but opposing integration and removal of the estate tax.[77] The Winnipeg Free Press, while praising the Report, was uneasy about taxing capital gains, and was opposed to "draconian" resource taxation.[78]

The existing system, which many editorial writers, on the appointment of the Commission, had criticized as chaotic, inequitable, and a drag on the economy, suddenly began to seem not so bad after all. The St. Chatharines Standard labeled the recommendations "comprehensive, revolutionary and risky" and therefore requiring "the most detailed and comprehensive examination to which any proposal has ever been subjected."[79] The editorial claimed that the existing system had encouraged foreign and domestic investment, while the Carter system might not. The writer then called for more tax incentives, which he said, would lead to increased capital investment and result in greater tax revenues.[80]

Ideological critics -- "Freedom" and "Socialism":

Much of the editorial criticism was expressed in terms of diffuse or general values, such as personal freedom, individual initiative, the threat of socialism and the encroachment of the state on private life. It ranged from the gentle rebuke of the Ottawa Journal's story line, "All Gain is Profit -- All Profit is Taxed" under which it expressed opposition to the "unpitying scope" of taxes,[81] to that of the Winnipeg Tribune, which charged that the Carter proposals for increased income redistribution were an attack by the state on the sanctity of the home, property rights, and the rights of individuals.[82]

The Edmonton Journal began by citing British economist Colin

Clark's predictions of adverse effects if government spent more than 25 per cent of private income, and publications of the Canadian Tax Foundation indicating that current government expenditures in Canada totaled 31.5 per cent:

> So it is chilling to learn that the proposed tax revolution would give 'much more' revenue to the federal government. And it is not completely reassuring to know the commission hopefully says that ultimately, tax cuts would be made.[83]

Citing Tax Foundation Chairman Philip Vineberg's predictions of "pain and anguish" in the Report, the editor cautioned that a capital gains tax was

> ...not necessarily justified for Canada with its particular level of development and particular problems....
> And, underlying the revolutionary recommendations on how the government should extract the money it spends and redistributes at such a dizzying pace, are the great basic questions: How big do Canadians wish Big Government to become? What kind of social system do we want?[84]

The Northern Miner saw the Report's "share the wealth philosophy" as an indication of how far Canada had "...wandered along the road to socialism...".[85]

The Calgary Herald conceded that the theme of tax equity was "smart politically" but warned that it would be damaging economically:

> The Carter Report can be based only on the assumption that the government has a better right to spend the people's money than the people have to spend it for themselves....
> The farther and farther the national tax structure goes along the road to confiscatory taxation of personal and

> corporate savings and profits, the closer the approach to Socialism and economic stagnation.[86]

In a similar vein, the Victoria Daily Times, referred to the Report as a "Blueprint for Control", predicting that in spite of promised reductions for lower income earners,

> ...the net reaction of many persons will be a feeling that the governmental net is drawing tighter around them -- that there will be less and less escape from the hand of government on the individual's pocketbook.[87]

Similar feelings were expressed by the Hamilton Spectator,[88] the St. John Telegraph-Journal,[89] the Saskatoon Star-Phoenix,[90] the Kingston Whig Standard,[91] and the Port Hope Guide.[92]

The Guide, while seeing the Report as a threat to Canada's "free society", saw some hope in the dissenting reports of Beauvais and Grant:

> The fact that after all these years of deliberation the Commission is not in perfect agreement should give us pause and should at least prevent the Carter Report from being considered some kind of sacred cow....[93]

Initial Business Reaction

A news item in the Montreal Gazette the Monday following release of the Report observed that most top officials of business were reluctant to commit themselves too strongly over the weekend until it had been thoroughly studied. Meanwhile, many of the first tentative comments were mildly favourable, especially regarding integration and

the sales tax proposals, while the taxation of capital gains was accepted by most business and financial spokesmen as being philosophically distasteful but inevitable. Although the mining and petroleum recommendations received a great deal of criticism from interests in those sectors, widespread business opposition to the Report did not materialize immediately.

The Chamber of Commerce:

Chamber of Commerce representatives whose views were reported in newspapers were mixed in their reactions. Eric Connelly, a chartered accountant and Past-President of the Calgary Chamber, welcomed recommendations on co-ops and credit unions.[94] George Demers, Président du Chambre du commerce de Québec, while approving of general principle of equity, thought that it would be difficult to apply, and the increased tax burdens on credit unions, the reduced incentives for mines, and the elimination of small business rate would be especially hard on Quebec.[95] Paul Ostiguy, Président du Chambre du commerce de Montréal, had been opposed to a capital gains tax, but had changed his mind, in view of the Report's arguments of equity, and the advantages of certainty and consistency.[96] Keith Laird, Q.C., and R. Robert Easton, Q.C., both described by the Windsor Star as "long-time tax advisors to the Windsor Chamber of Commerce",[97] said that the recommendations would help low- and middle-income earners without harming corporations, and would also encourage Canadians to invest more in their economy without hurting American investors.[98]

Manufacturing:

Henri W. Joly, President of the Canadian Manufacturers' Association, and President of B. Houde et Grothe Ltée, a Quebec subsidiary of Imperial Tobacco, was especially pleased about the proposals to remove the sales tax from production equipment, to collect the federal sales tax at the retail level, and to abolish the estate tax and succession duties. Integration "would appear to provide greater encouragement to Canadian investors, and was far better than penalizing non-resident owners by taxation." However, he "regretted" the removal of small business rate, which, without "an equivalent compensation", "could hurt small companies and inhibit their growth."[99] Joly also opposed the proposed taxation of capital gains as being "inappropriate for Canada, since it would discourage the flow of funds into risk-taking capital investment which is necessary for Canada's continuing development."[100]

An Alberta Director of the Canadian Manufacturers' Association, Grant Carlyle, described the Report as "an attempt to remove a number of inequities and anomalies". He thought it was a "good" report and he was "not surprised" at the capital gains tax. "Industries competing with co-operatives will gain some satisfaction that they may become equal."[101]

N. E. Kenrick, Vice-President and Comptroller of Dominion Textile

was also favourably impressed, calling it, all-in-all an excellent attempt to simplify the Canadian tax structure. He particularly approved of the integration and sales tax recommendations.

Finance:

Most securities dealers either accepted the Report philosophically or were, on balance, favourably disposed to the major recommendations. Said O.E. Beeker, Manager of James Richardson & Sons:

> There is going to be some reaction in the stock market to the capital gains tax... but this would only be temporary. A capital gains tax would be a good thing.[102]

Richardson Securities, in a synopsis of the Report which was reprinted on 2/3 page in the Hamilton Spectator under the heading "Carter Report ...and the stock market",[103] regarded it as "a highly constructive and positive move despite mixed reaction in the marketplace over the near term".[104] It expected the effect on the market to be mildly "bullish" for most sectors except for exploratory oils. The possibility of higher insurance premiums and a slowdown of insurance sales might depress that sector. In mining, the attractiveness of stocks was expected to be as great as before to shareholders. Although larger integrated mining companies would pay higher taxes from earnings than non-integrated companies, this was expected to be offset by integration for most middle-income shareholders. However, upper-income shareholders were not expected to

fare as well. Significant improvements were anticipated in the attractiveness of shares for secondary manufacturing. Not enough information was available on banks' inner reserves to predict the effects on that sector with confidence, though the authors of the Richardson Securities synopsis expected them to be helped by increased taxation of credit unions.[105]

William R. Fulton, branch manager of Midland-Osler Securities, noting that losses could be deducted from capital gains, told reporters, "I think we can accept this quietly."[106] Similar thoughts were expressed by members of Toronto's brokerage houses. Ivor Quiggin, head of the Toronto bond department of R.A. Daly, investment dealers, predicted no long-run effects from the capital gains tax.[107] The Ottawa Citizen reported him as saying that capital gains taxes

> ...are something you put up with, like brokerage charges. Obviously there won't be any long-term effect on the stock. After all there has been a capital gains tax in the United States and Britain for years and stock markets there continue to operate with ever-growing investor participation.[108]

Quiggin also pointed out that capital losses would be deductible:

> Since there's a carrot and a stick there, once new measures are accepted it becomes a part of the cost of doing business. Of course no one really wants to see a capital gains tax, but the investment industry knew it was coming. Whether the government implements this particular idea now is really of little consequence -- sooner or later there will be a capital gains tax.[109]

Ewin Ruthven, Manager of the Toronto office of Royal Securities,

favoured the Report and predicted no abrupt change in investor behavior, but added that implementation would require a bold government.[110] W.C. McFadyen, Manager of Nesbitt, Thompson & Co. agreed.[111]

One spokesman for the brokerage houses, E. Paul Henry, research director for Bongard Leslie of Toronto, dissented from the spirit of approval and acceptance among investment dealers. In an investment letter to clients he predicted that the Report would not be implemented in the form of the original package:

> In today's political environment ...we believe the recommendations in the Report involve so much change, are so intricate, and the costs of administering so high, they will never receive carte blanche endorsement by Parliament.[112]

A Greenshields Securities report to its clients, quoted in Ronald Anderson's March 7th column in the Globe and Mail, while not expressing opposition to the Commission's recommendations, noted that:

> ...the far-reaching implications of the Report for federal-provincial relations probably would be the principal difficulty in the way of implementing the proposals -- which the Carter commission had emphasized must be regarded as a package....
> While political realities would seem to militate strongly against the wholesale adoption of the commission's recommendations ...the future development of Canada's tax structure is nevertheless bound to be greatly influenced by the concepts and proposals set out in the Carter report.[113]

Initial reaction on the stock markets was generally pessimistic, as indicated by sharp drops in many stocks on the Monday following release of the Report. The Toronto Star told the news under the red

headline, "Oil mining stock fall after Carter report".[114] The biggest losses were among mines, steel companies with mining interests, oils and insurance.[115] However, the loss of February 28th coincided with a decline on the New York market, and much of the losses were made up the next two days, which some market analysts attributed to a feeling among buyers "that the Commission's suggestions are so sweeping that they may never be put into effect".[116] The fall in stock prices may also have been partially a self-fulfilling prophecy of at least two newspapers which anticipated a decline: The Calgary Herald's headline of February 25 read "Market May Get Bearish Over Report", and a story heading "Market Reaction Likely -- Tax Report Viewed With Caution Here", while the The Globe and Mail on the morning February 27th contained an item headed, "Stocks face impact of Carter proposals".

Spokesmen for the stock exchanges, however, were either favourable or not noticeably worried about the Report. Robert Steiner, Vice-Chairman of Toronto Stock Exchange, told reporters, he felt "somewhat relieved that the recommendations in general do not drop a bomb on the investment community or seriously disturb investor confidence."[117] He agreed that the investment community had long expected such a tax, and it therefore would "not cause any panic in investment circles.[118]

Charles Neapole, President of the Montreal and Canadian Stock Exchanges, said that reaction of Montreal financial interests "n'était pas mauvais du tout."[119] Jack Van Lunen, President of the Vancouver

Stock Exchange was more cautious: a capital gains tax, depending on the rate, was "not necessarily bad".[120] H.A. Walcot, President of the Calgary Stock Exchange thought that the recommendation of a capital gains tax might affect stock prices briefly but that the market would recover in a short time. The idea didn't "come as too much of a surprise to anybody, as indirectly, we have had it for years." He added, however, that it had to be "applied properly and at a fair rate".[121]

Insurance:

Under the heading "Pension scramble expected", the Hamilton Spectator had predicted that the recommended changes in tax status of life insurance policies which double as retirement plans would arouse fierce opposition from the life insurance companies.[122] Initial reaction from industry executives, however, was not entirely unfavourable. W.M. Sanderson, Chairman of North American Life Assurance Company, having read only the Globe and Mail summary in the Saturday edition, agreed with the comprehensive income philosophy.[123] Harry J. Seed, President of Seaboard Insurance, said the proposals respecting life insurance companies probably would not have any great effect, except perhaps on the premiums on some policies, and that it "wasn't wholly unexpected.... A similar type of tax has been in effect in the U.S. since about 1959." He also felt that life insurance firms might benefit indirectly from a capital gains tax: people might be more inclined to purchase annuities, since

they would have to pay capital gains tax on appreciation of stock capital.[124]

Not all insurance spokesmen were sanguine: Robert Reid, President of London Life Insurance Co. said that some recommendations grossly discriminated against policy-holders, and that his company would make representations to government opposing the Report.[125]

The Mining Industry:

When asked in an interview on Toronto radio station CFRB about the protests against removal of mining depletion allowances and the three-year exemption for new mines, Carter said that the logic of the recommendations affecting the mining industry were so clear that nothing could be said against them.[126] Logical as they may have been, the Commission's recommendations on mining aroused the industry into a unified storm of protest which overwhelmed the publicity given to the recommendations themselves.

The implications of the Carter recommendations for the mining industry had featured prominently in the initial newspaper reporting, and although most of the larger companies withheld immediate comment, the industry registered more commentary in newsprint than any other. Certainly, the reaction of the major companies would not have been difficult to guess. Under the headline, "Mines Face Tax Blows" the Hamilton Spectator noted:

> Hardest hit would be eight of the largest companies -- three of them petroleum, and five mining -- which the Commission says have received about 85% of the tax reductions involved though they least needed the concessions.[127]

Monday's Toronto Star, reported the names of the mining companies which had been singled out by investors as being potentially big losers if the recommendations were implemented: International Nickel, Falconbridge, Denison Mines, Cominco, Kerr Addison, and Alcan, as well as steel companies with major mining interests.[128] Wednesday's Globe and Mail mentioned the Steel Company of Canada (Stelco), Algoma Steel and the Dominion Steel and Coal Company (Dosco) among steel companies whose share prices were most affected.[129] The Toronto Star reported that the penny mine and oil stocks appeared to suffer little from investor reaction to the Report, as it had indicated that most of the existing tax concessions were going to large companies.[130]

Opposition was not confined to the major companies, however. According to Paul Goldstein, staff writer for the Toronto Daily Star, the smaller resource firms were "already beginning a tornado of protest". He cited the example of Larry Labow of Labow Mining Consultants, who had:

> ...pumped $500,000 into development work in the last five years.... The tightness of the money market has forced Labow to deal with the big mining outfits and now he finds himself treated like the biggies. He says that the commissioners can't understand the complexities of the mining industry, and their ideas would curtail the provision of development capital. "The Liberal Party will get their brains beaten out if they try to pass

it.[131]

The views of the Mining Association of Canada were first indicated on the Monday following the release of the Report by its Managing Director, V.C. Wansborough, who stressed the negative aspects of the proposals on economic growth.[132] The next day, in a widely-reported statement, the Association's President, J.D. Barrington, said the recommendations would drain risk capital away from mining, cut mineral exploration, retard Canada's growth and weaken Canada's export position. The Report, he asserted:

> ...displays an ignorance of what has led to growth in Canada.... In a frontier economy such as Canada... to lump income and capital together for taxation purposes displays an ignorance of the factors which had led to the expansion of this country not only in mining, but in all basic industries. [If the mining proposals were implemented] ...Canada would be the only country in which mining is a significant industry where provision is not made by way of depletion for the fact that an ore body is a wasting asset ...and that the search for new sources of mineral wealth is accompanied by very high financial risks.... The report completely fails to recognize the vital contribution which the mining industry makes to the national economy by the annual production of over $3 billion of new wealth....[133]

Of the five metropolitan dailies from which the reports of this statement are preserved in the Commission's files, only the Montreal Star reported that Barrington was also head of McIntyre Porcupine Mines, the holding company that controlled Falconbridge Mines. Falconbridge was very likely one of the eight companies which, in 1964, according to the Report, had received 85 per cent of the resource depletion allowances, and one of the four mining companies which had received three quarters of the benefits from the three-year

tax holiday for new mines.[134]

The B.C. and Yukon Chamber of Mines, through its Manager, Thomas Elliot, also expressed its immediate and strong opposition. Elliot warned that British Columbia and the Yukon would be hard hit by removal of the three-year exemption for new mines because "many of the proposed new mines are of the large, low-grade variety that require this type of encouragement in order to plan for their production." Elliot also spoke against the taxation of capital gains:

> Thousands of prospectors and small companies spend years of their lives searching for the one mineral discovery that will make them wealthy. Now the Carter Commission is saying that if a prospector is successful it will treat his reward as income and tax it in full.... It has been said that a person can write off his losses. But how can a prospector write off the years he has been searching ...without a success? Then, again, people who gamble their money on financing mining companies and have a win should be allowed the full benefit of their courage and initiative.[135]

Reginald J. Campbell, Executive Vice-President of Falconbridge Nickel Mines, was reported as declaring that the mining recommendations would lower profits, make mining shares less attractive, and inhibit the opening of new mines.[136] W.R. Roe, President of Kerr Addison Gold Mines predicted that the withdrawal of the 3-year exemption for new mines would tend to dry up sources of exploration money and "make it difficult to finance low-grade propositions."[137]

At the annual meeting of Rio Algom Mines, its President, Robert D. Armstrong, charged that the Carter Report was "based on a number of

false premises and a gross misconception of business and financial realities..." and "...directed at achieving a massive, idealistic and highly unrealistic rearrangement of Canada's economic affairs."[138] He added that the Report paid "no attention to the fact that "Canada is a capital-poor country and that most of its manufacturing industries are not competitive in world markets."[139]

In a speech to the Canadian Club at the Royal York Hotel in Toronto, V.W. Scully, Chairman of the Steel Company of Canada warned of the threat posed by the Carter Report to the company's $100 million investment programme. The Globe and Mail reported Scully's remarks under the heading, "Stelco chief assails Carter experimenters as risk to economy".[140] The company had assumed, said Scully, that the existing incentives would remain in effect when it had committed the funds for the expansion projects:

> Now that the money had been committed, and the facilities in being, it is not at all assumed that our judgement will be vindicated if certain suggestions are ever enacted into law....
> Obviously, in steel, we sink or swim with strong, forward-looking and stable national policies. But it is appalling to think that experimenters may be allowed, using all Canadian industry as their laboratory to disregard the economic realities and to test out schemes likely to invalidate the bases on which an industry such as steel must found its future.[141]

The Petroleum Industry:

With the exception of the three-year exemption for new mines, the petroleum industry was affected by the Carter recommendations in a

similar manner as the mining industry, and its reaction was similarly hostile. Saturday's Calgary Albertan of February 25th, bore the headline: "Report a threat to oil planning", and reported the critical comments of three industry spokesmen: A.F. Beck, Chairman of the Alberta Division of the Canadian Petroleum Association, and President of Canadian Export Gas and Oil, C.O. Nickle, publisher of Nickle's Daily Oil Bulletin, and Jack Pierce, President of Ranger Oil. The consensus was that the Commission had over-estimated Canada's available reserves of crude oil, that the recommendations would encourage American interests to take over the Canadian oil industry, and that Canada would be saddled permanently with high-cost oil. Nickle said that the Report was the complete opposite of what had been hoped for, that is, depletion treatment similar to that of the U.S. He could "...see why reports from royal commissions end up on the shelf for 12 years. With luck this one will join them."[142]

Monday's Calgary Herald featured an almost identical story[143], while Beck's remarks were also reported in the Toronto Star[144]. According to the March 1st issue of the Toronto Star, the Canadian Petroleum Association, representing the major companies, and the Independent Petroleum Association, were already mobilizing opposition to the Report.[145]

Seven weeks after publication of the Report, W.O. Twaits, President of Imperial Oil, attacked it at the annual meeting of shareholders in Toronto on April 18th. His comments were reported in the Globe and Mail together with a photo of Twaits, under the heading,

"Carter Report misguided, deficient: Twaits".[146] He told the 662 shareholders in attendance that the Carter Report was "perhaps the greatest element of confusion and uncertainty in the Canadian economic outlook." In addition to criticizing the proposed removal of depletion, Twaits attacked the value premises and basic assumptions of the Report:

> Should the tax system be dedicated toward dynamic economic growth, generating both physical and social capital, or should it be dedicated toward slicing up the income pie?.... The assumption of a fully mobile pool of capital committed to Canada, which could be shifted readily from one industry to another by tax policy, may be a perfectly practical assumption in the Soviet Union but certainly not where the investor has any choice of opportunity.[147]

This theme was given praise and amplification in Fraser Robertson's column two days later, in which Twaits' remarks on economic growth versus its distribution were quoted. Like Twaits, Robertson attacked what he saw as the redistributive assumptions of the Report:

> In its basic assumption that a dollar is a dollar no matter how it is handled or who has it, the Carter report also seems to imply that in the modern society, equity demands a constant redistribution of wealth by means of taxation, that is, through government. Accumulations of money, either by corporations or individuals, need to be broken up. Presumably the justification of such a system is that money held in large amounts is of no real benefit to most individuals. It is the old robber-baron theory in modern dress.
> Again a real-life picture of how people actually deal with money was presented at the Imperial Oil meeting. A similar picture could be presented by the majority of business companies and is, indeed, being presented with increasing frequency. What the picture shows is that when business handles the money the income pie not only keeps on getting bigger, it also keeps on being sliced

> up into more slices each of which is bigger. The dollar that gets into the hands of a successful company is divided four ways. One part is used, like yeast, to make a new and bigger pie. A second part is distributed to shareholders. A third part is distributed to employees and a fourth part -- a very large share -- is taken by governments which expect citizens to say thank you to them for passing it along to all of us.[148]

On April 19th, the day after Twaits' attack on the Report, Texaco also expressed its opposition, and again, the forum was the company's annual meeting, duly reported in the Globe and Mail.[149] Texaco Canada's President, Frank M. Dawson, warned his listeners that removal of depletion would "likely reduce necessary capital investment in the industry" and would therefore be against the public interest.[150]

On April 20th, British-American Oil joined the growing chorus of opposition.[151] The President of the Canadian subsidiary told those present at the annual meeting in Toronto that it was "dangerous" for the commission to conclude that there was no need to encourage oil exploration because existing production of conventional crude was below 50 per cent of capacity and because the practically inexhaustible reserves of the Athabaska tar sands offered the prospect of synthetic crude at competitive production costs. He warned that that was not the case for exported oil, and, like Twaits and Dawson, emphasized the need for continuing depletion allowances in order to encourage investment in exploration for conventional oil sources.[152]

Other Business Reaction:

The reaction of the resource industries and the financial sector used up nearly all the newsprint devoted to the Carter Report. The scattered comments from other business sectors was mixed. Some opposed removal of the dual corporate tax rate and the proposed inclusion of taxable gains. However, there was no early trend of strong opposition comparable to that in the mining and petroleum industries.

Non-business Reaction

Agriculture:

Only two comments of agricultural representatives are preserved in the Commission's large file of press clippings. James Bentley, President of the Canadian Federation of Agriculture, and Paul-Henri Lavoie, sécrétaire générale de l'Union catholique des cultivateurs, were both reported as being entirely favourable to the Carter recommendations.[153]

Co-operatives and Credit Unions:

All co-op and credit union representatives whose views were reported in the press were opposed to the Commission's

recommendations. John Hallinan, General Manager of the Ontario Credit Union League, was reported by the Globe and Mail as being opposed to the Report, and planning further submissions to government.[154]

Labour:

The few comments of labour union leaders reported indicated only qualified support for the Report. Donald MacDonald, Secretary-Treasurer of the Canadian Labour Congress, approved of the redistributive features, especially the capital gains tax, but opposed the taxing of social security payments. He told the Globe and Mail that the zero rate bracket was set too low, and that co-operative patronage dividends should not be taxed.[155]

Louis Laberge, Président du Fédération du Travailleurs du Québec told La Press that he approved of the proposed reduction in tax burden for small and medium earners and the deduction of costs of workers' tools from taxable income. However, he thought it would make federal-provincial relations more difficult, and wondered what the Report's effect would be on capital investment.[156]

Women's Groups:

The Globe and Mail reported M.J. Sabia of St. Catharines, President of Canadian Federation of University Women and Chairman of

the Committee for Equality of Women; Louise Card, of Neepawa, Manitoba, National President of Canadian Federation of Business and Professional Women's Clubs; and Julia Schultz of Toronto, Executive Director of Council of Jewish Women, as all being in favour of the proposed tax relief for families of working mothers.[157]

The Response From Federal Opposition Politicians

The Progressive-Conservative Party:

The release of the Report found the Conservative Party in the midst of a campaign to elect a Party Leader, and the candidates' views on the recommendations were prominently reported.

John Diefenbaker, who had originally appointed the Royal Commission, and was campaigning to retain the Party leadership, told the Canadian Press he thought the recommendation of a capital gains tax was long overdue.[158] He also favoured abolition of the Estate Tax, but was critical of the removal of the "small business rate", and the Commission's failure to recommend a $500 deduction for property taxes.[159] The Globe and Mail also reported his support for integration and the elimination of the 12 per cent tax on building materials.[160]

George Hees, former Minister of Trade and Commerce, and a candidate to replace Diefenbaker as Conservative Leader, was reported

in the Globe and Mail as saying that a tax on capital gains would be a serious mistake.[161] In a statement issued at the Progressive-Conservative Student Federation meeting in Ottawa, Hees said that the government should reject the capital gains proposal "... so that the process of Canadians owning as much as possible of their development may proceed as quickly as possible."[162] The Ottawa Citizen, however, quoted Hees to have "agreed completely" with the objectives of the Report, and that, the Commission had done a "competent job in its efforts to achieve its objectives by replacing existing tax laws with ones basing taxation on ability to pay...".[164]

Former Justice Minister, Davie Fulton, also a Conservative leadership candidate, had released a statement opposing a tax on capital gains a few days before the Report was released. He told a press conference that such a tax would discourage Canadian investment when it should be encouraged.[165]

National President of the Conservative Party, Dalton Camp, told a Party meeting in Ottawa there was much merit in the Report but that Mitchell Sharp seemed to be hostile to the findings. He thought it deserved careful study by the government and by the Conservative Party, and that its proposals promised a tax formula better than the current tax jungle.[166]

At a speech to a luncheon meeting of the Empire Club in Toronto on March 16th, former Minister of Finance, Donald Fleming, criticized the proposed removal of the three-year exemption for new mines and

depletion; the increased taxation of life insurance companies, the taxation of the business income of charities, and the package deal aspect of the Report.[167] The Report was too radical, involving the "...casting away of much of the expertise and experience gained by ...the Department of National Revenue in administering our existing taxes."[168] Warning that the credibility of the Report rested on the maximum marginal rate actually being lowered to 50 per cent to offset the broadening of the tax base, Fleming doubted whether the government would resist the temptation to keep rates high in order to spend the extra revenue:

> ...The Commission repeatedly has stated this [50 per cent] limit as though it were as final as the laws of the Medes and Persians .... Even if the 50 per cent ceiling were enacted, who can say that succeeding governments may not lay impious hands upon it if the big spenders continue in control of national policy? How well we know to our cost that there is no permanence in tax rates.[169]

Fleming also attacked the proposed inclusion of gifts and bequests, and the family unit concept as "a revolutionary departure from concepts hitherto prevailing in Canada ...all concepts of estate planning are knocked topsy-turvy". The integration scheme, too, was flawed, as it would help shareholders at the expense of bond-holders, thereby distorting debt financing by corporations. He was concerned that "in today's circumstances, the commission has leaned so heavily in favour of the federal government", and thought its treatment of foreign investors would "have a discouraging effect in future on foreign investment.[170] Fleming's remarks, though coming two weeks after those of other prominent Conservatives appeared to have greater

impact, partly from the fact of his former Cabinet portfolio, and also because the consistency and detail of his remarks gave journalists and readers the impression that he had taken the time to read the Report.

Fleming's comments were cautiously praised in a Globe and Mail editorial in the same issue and provided the spring-board for another column by Fraser Robertson attacking the Report.[171] Both the editorial and Robertson's column supported and amplified Fleming's warning that the Carter proposals would give future federal governments the wherewithal to increase spending, thereby wiping out any possibility of significantly reducing tax rates and moving Canada toward greater state intervention in the private sector. In Robertson's words,

> The implication he left with his audience, that implementation of the Carter report almost certainly would be followed by escalation, [of government spending] hardly can be seriously disputed, in view of the history of taxation in this and in other countries....
> Mr. Fleming's concern was not to pick over the report ...but to put before the public a number of very fundamental questions which, taken together, require us first to think of what kind of a country we hope Canada will be and then to ask to what extent the system advocated by the report will contribute to or impede attainment of this objective. For what in essence is of concern is not how money shall be raised, but what powers governments in future should have over the lives of each and every citizen.[172]

The New Democratic Party:

Interviewed in Saskatoon, NDP Leader T.C. Douglas praised the

Carter Report as an honest attempt to redistribute the tax burden according to ability to pay, adding that, "There are a great many wealthy people and corporations who have been getting away with murder."[173] Douglas was especially pleased with the inclusion of capital gains in the tax base and the limits on business expense deductions.[174]

Max Saltsman, Finance critic for the New Democratic Party took satisfaction in the fact that the aim of equitable taxation regardless of source represented "a full endorsement of the position we have always taken to a more worthwhile and equitable approach to income distribution."[175] Saltsman praised the reduced emphasis on sales taxes, higher and more predictable corporation taxes, a "better break" for widows and children inheriting estates, and improved opportunities for Canadian investors, with tax loopholes closed. He expected that the recommendations would "allow provision in our business and financial establishments for more risk-taking."[176]

Initial Provincial Reaction

Most provincial governments, and a number of opposition spokesmen, had something, to say about the Report during the first week of its release. The governments of the Maritime provinces spoke favourably of the Report, while those of Quebec, Manitoba and British Columbia were opposed. The Ontario government was putting out confused signals. The Commission's file of press clippings, however, give no

indications of any initial reaction from the governments of Newfoundland, Saskatchewan or Alberta.

The Maritime Provinces:

Finance Minister, G.I. Smith said he thought the recommendations would do more for Nova Scotia than most other provinces because of its generally lower income level, but that it would be years before the "revolutionary aspects" of the Report were acted on.[177]

Not having studied the Report, Premier Alex Campbell was reported to be pleased at the recommended concessions to lower income earners, and thought that it should generally benefit his province.[178]

The Minister of Finance of New Brunswick, L.G. DesBrisay praised the Report, citing its major goal of establishing an equitable tax system.[179] He noted the similarity of the Carter recommendations to those of the provincial government's municipal reform program: "In both cases, the goal is to reduce the burden on low- and middle-income earners, without reducing incentives to production and investment.[180] He favoured the recommendations on federal-provincial tax sharing, which, combined with the new tax equalization formula to take effect April 1st, should make it clearer to taxpayers which taxes he is paying, and should, in addition, result in lower prices. He added that "everyone" should take advantage of the opportunity to examine the recommendations carefully.[181]

Quebec:

Quebec premier, Daniel Johnson, speaking at a $500-a-plate Union Nationale fund-raising dinner at the Queen Elizabeth Hotel in Montreal, promised to oppose any attempt to centralize powers in a single government. While he did not specifically mention the Carter Report, the story in La Presse pointed out that it would reverse the recent trend toward a greater share of taxes for the provinces by conferring all authority for corporation taxes on the federal government, and giving the latter general preponderance in fiscal matters.[182] The following day, the Minister of Revenue, Raymond Johnson, said Quebec would resist pressure to rely on indirect taxes and was not about to cede the corporate income tax field to the federal government.[183] Jean Noel Tremblay, Cultural Affairs Minister and Associate Minister for Federal-Provincial Affairs, said that if the federal government implemented the Carter Report it would make the provinces tributaries, to be treated like municipalities.

The Report did not receive a much warmer welcome from the Liberal Opposition. Leader of the Opposition, Jean Lesage, told La Presse, "Le rapport Carter est explosif sur le plan des relations fédérales-provinciales."[184] Opposition financial critic, former Secretary to the Bélanger Commission, and former member of the federal Tax Analysis Unit studying the Report, Robert Bourassa told Le Nouvelliste that the recommendations respecting the division of taxing

powers could never be implemented and did not take into account actual government responsibilities and expenditures. He was particularly opposed to the federal control over corporation taxes, and the proposed ceiling of 50 per cent on the provincial share of personal income taxes.[185] Eric Kierans, Member of the National Assembly for Notre-Dame de Grace, President of the Quebec Liberal Federation, and formerly Minister of Revenue, was reported in La Presse as favouring the taxation of capital gains, the reduction of personal income tax rates, and the sales tax recommendations, but opposed to a federal monopoly of control over income taxes.[186]

Among Quebec government officials opinion was generally favourable. According to the Toronto Star, "one spokesman" had said that, even if the recommendations on federal-provincial fiscal relations were rejected, this "did not detract from the value of proposals designed to give the taxpayer a fairer deal."[187] This unnamed official looked forward to a new era in tax policy-making in which inter-governmental co-operation would be essential:

> There is today a new dimension to our fiscal problems. It is that no changes in fiscal matters can really be achieved unilaterally. There has to be consultation with the provinces. Both the Bélanger and the Carter Reports recognize this. One government alone cannot change anything in a taxation field which is occupied jointly with another government.[188]

Ontario:

Provincial Treasurer, Charles MacNaughton told reporters the

Monday following release of the Report, that it was "too complex" for immediate comment, and he would have to await the report of the Ontario Committee on Taxation for "a thorough assessment of the position of this province".[189] However, he did comment on the federal-provincial aspects, saying that Ontario would continue to demand a greater share of federal revenues regardless of the Carter Report.[190]

Premier Robarts said that Ontario had "no objection in principle" to the recommendation that the provinces be given the power to levy indirect sales taxes.[191] While he could not declare himself either for against the inclusion of capital gains in the tax base, he noted that some citizens paid the equivalent of a capital gains tax when the tax collector ruled that a capital gain was a form of income from regular work.[192] On April 20th, Robarts attacked the federal government for its "imaginative spending plans" which it could afford because of "its more comfortable financial position", but which also committed the provinces to greater spending. He criticized the Carter Report for not dealing with constitutional difficulties involved in its recommendations that the federal government have full control over corporate and personal income tax fields while the provinces were left with the sales tax.[193]

On the Monday following release of the Report, Liberal Leader and Leader of the Opposition, Robert Nixon said the provinces should not give up a large share of the income tax field to the federal government, leaving the provinces to rely on the sales tax and

"federal handouts". Apparently unaware that the problem was outside its terms of reference, Nixon criticized what he called the Carter Commission's failure to deal with municipal taxation, which urgently needed reform.[194] The Toronto Star gave its readers a different impression of Nixon's comments, reporting that he was impressed by the Carter Report and its philosophy supporting a strong central government. According to the Star, Nixon said that Ontario didn't need a broader tax base, but should itself relieve the municipalities of the regressive taxes they had to impose on homeowners.[195]

New Democratic Leader, Donald MacDonald, attacked the Carter Report for failing to deal with federal-provincial financial relations, warning that the proposals would reduce provincial revenues. He added, however that the Report vindicated NDP tax policies.[196]

The Western Provinces:

Manitoba Treasurer, Gurney Evans, demanded an immediate federal-provincial conference to discuss tax sharing, expressing his fury over the Carter Commission's recommendation that the federal government cede no more of the income tax field to the provinces:

> All the income tax that's collected here is Manitoba money. They don't abate it to us, we give it to them. And we don't give them too much.[197]

While the Commission's files contain no press reports of the

initial reaction of Premier Ross Thatcher, the NDP Opposition leader, Alan Blakeny, reacted favourably on the basis of press reports. He was especially happy about the recommended comprehensive tax base and relief for low income earners.[198]

Premier W.A.C. Bennett declined comment on the Report until government officials had had a chance to study it.[199] Robert Bonner, British Columbia's Attorney General said the Commission had exceeded its terms of reference in proposing major changes in federal-provincial tax sharing and administration.[200]

Robert Strachan, Leader of the NDP Opposition in British Columbia, was reported to be pleased with the Carter recommendations which, if implemented would "shake up the whole Canadian community". He said it was "obvious that some of the recommendations will not only produce substantially increased revenues but ...will mean a more fair distribution of our national tax burden."[201]

Response of the Tax Professionals

The tax lawyers and chartered accountants, important opinion-leaders on tax policy, had been a decisive factor in the decision to appoint the Royal Commission. Reporters and editors (and eventually, the government as well) were expected to, and did, turn to the tax specialists for "informed comment" during the days immediately following release of the Report.

Initial Reaction:

Although most business spokesmen quoted in newspaper reports were not themselves tax lawyers or accountants they relied on advice from tax professionals employed by or retained by their companies. Tax and financial specialists employed by major accounting and securities firms also advised their customers of the content and implications of the Report. Initial reaction from tax professionals was about evenly divided. Of nine independent tax lawyers and accountants whose opinions on the Report were reported in newspaper clippings in the Commission's files, four generally supported the Report as they understood it, three were more critical than supportive, and two were mixed or non-committal in their opinions. One of the non-committal opinions was that of Ronald Robertson, a tax lawyer with McCarthy and McCarthy of Toronto, and former Director of the Canadian Tax Foundation. Robertson provided a capsule summary of the Report, which, although not clearly critical, would have left many readers with an ominous impression:

> Equity, as this nebulous principle is conceived by the commissioners, is the report's controlling and over-riding theme. Economic effects, customary trade-offs between revenue potential and feasibility of collection all get lower priority. The commission sees income, as it has been redefined and broadened, as the best measure of ability to pay. If one accepts these basic propositions, many of the pieces and individual recommendations readily fall into place from a

theoretical standpoint, although they may be shattering to those affected.[202]

The Toronto Star reported one chartered accountant, Murry Rumack of Rumack, Stern and Co., as being enthusiastically in support of the Report.[203] He singled out for praise the proposed removal of the mining and oil concessions, which had been "too philanthropic", and the integration scheme, which, he predicted, would result in greater dividend payouts and increased cash flow to shareholders. He thought development capital would come easier for new equity and debenture issues, resulting in less reliance on internal financing and allowing more investors to "share the wealth".[204] He also favoured the recommendations affecting the taxation of financial institutions, which "...take away their undue preferences and privileges", and as a result of which the "public has been carrying the load of taxes for too long."[205]

One Toronto corporation lawyer, M. Wainberg had almost unreserved praise for the Report, calling it "a brilliant work" which had "disregarded political party lines and old precepts". Wainberg thought that the taxation of capital gains was "inevitable ...ulitimately, it is for the good of the country. It will eliminate the difficulty of settling what a capital gain is."[206]

One of the best-known tax lawyers, John G. McDonald, author of a text-book on Canadian tax law and of the periodical commentary on

taxation, "McDonald's Current Taxation", was decidedly critical of the Report. The Toronto Star printed sections of the issue on the Carter Report under the headings: "It may pay people to leave the country when they retire"; "Foreigners could be discouraged from lending to Canada"; and "International companies could be caught in an international squeeze play". Under the last of these three headings, McDonald pointed out that removal of the normal exemption granted to foreign business corporations whose head offices were in Canada would hurt such firms as Brazilian Traction.[207] McDonald, who had advocated the taxation of capital gains and the principle of ability to pay sixteen years earlier,[208] had completely reversed his position.

The Commission Spokesmen:

Apart from the initial press conferences, and presentation of the opening address to the special Conference of the Canadian Tax Foundation in April, 1967, Carter did not attempt to get involved in the public discussion of the Report, as he did not consider public advocacy to be a proper role for a former Commissioner.[209] During an interview broadcast by a Toronto radio station, he had been confident that the Report, when carefully studied, would defend itself.[210] Carter's perception of the proper role of ex-Commissioner aside, his failing health by the spring of 1967 made his active participation in the defence of the Report increasingly difficult and eventually impossible.[211] Harvey Perry also assumed a

retiring role until the second Canadian Tax Conference in November of that year.[212]

Much of the burden for the active defence of the Report fell on Hartle, who spent most of the year following its publication travelling from one conference or meeting to another. Geoffrey Conway also toured the conference circuit to counter the barrage of criticism from tax practitioners and businessmen, and several other former staff members of the Commission delivered papers at the two Tax Foundation conferences. The initial reception at these gatherings was invariably hostile, sometimes almost violently so.[213] Conway left some meetings with the impression that the intrinsic merit of the Carter "package" from the point of view of Canadian business had been appreciated, but that this was outweighed by suspicions that the government would implement only those recommendations which increased the tax burden on business.[214]

The April 1967 Tax Conference:

Of all the conferences and meetings devoted to discussion of the Carter Report none were more important for providing an indication of the state of opinion among tax professionals than the two conferences sponsored by the Canadian Tax Foundation, the first in April, 1967 in Toronto, and the second in November of the same year in Montreal. The Foundation had planned a special conference on the Report long before the Commissioners had settled on their recommendations, and had been

forced to repeatedly postpone the scheduled date as the date for the public release of the Report was continually set back.[215] Since everyone in the tax professions had been anticipating the Report, the Foundation did not hold its customary Annual Tax Conference for 1965 or 1966. There seemed little point in saying much about the old tax system when it might soon be fundamentally changed.

More than 1,700 participants were listed in the published Proceedings of the April, 1967 Tax Conference, about double any previous attendance at Foundation conferences. About 40 per cent of those attending were affiliated with legal or accounting firms and approximately an equal number were associated with businesses or business groups. The remaining 20 per cent were mainly from universities, governments, and other institutions in the public sector.[216] The programme listed 71 speakers, most of them familiar names to people in tax circles. Their opinions of the Report, and the opinions of other participants were carried to all important institutions in Canada, either directly through representatives at the Conference, or indirectly through reports carried in the professional, trade, and general media. The participants were fully conscious of their collective opinion-shaping role. As H. Marcel Caron, the Vice-Chairman of the Foundation expressed it in his introductory remarks to the session on corporate taxation:

> I believe this gathering and the Foundation research staff can, and must accept this challenge and offer objective guidance to our political leaders at the federal and provincial government level.[217]

Foundation Chairman, Philip Vineberg, again underlined the importance and responsibility of all the Conference participants as opinion-makers:

> We will all have the necessary obligation towards our country to reach a personal decision as to the way in which we are going to support or oppose these proposals, or otherwise impress our views upon the governing authorities. And with no group more than this one will the responsibility lie in determining the future evolution of the recommendations made by the Carter Report.[218]

When Kenneth Carter delivered the opening address to the largest gathering of opinion-makers in the history of Canadian taxation, he must have been aware of its great import for the prospects of tax reform. Acknowledging that he would "never have a better forum", Carter began by clearing up a misunderstanding of the "package" concept which had been "somewhat overstated" in public discussions.[219] He denied that the Commission had asked that its Report be accepted as 'all or nothing': "that would be not only arrogant but also stupid", since there were about three hundred other recommendations which did not hinge on acceptance of the "package".[220] However, if the main recommendations were not considered together, the resulting incidence of taxation, he warned, "could be most unfair":

> For example the comprehensive tax base, which includes the full taxation of capital gains would, in our opinion, be quite unrealistic if corporations were themselves taxed without adequate relief to the shareholders. Hence the effect of integration was weighed against the comprehensive tax base and it appeared to us to be about in balance. Then again, the lumpiness of some items which would fall into the

> comprehensive tax base when gains were postponed until realized would impose impossible burdens with the existing high rates of personal tax and without an improved system of averaging....[221]

Referring to attacks against him in the press Carter noted:

> Recently I have observed myself to be branded as a socialist, a communist and even a conservative -- that's with a small "c". All I want to say on this score is that my personal ideology doesn't matter one bit, and I know you will all agree that the Report and its recommendations must be considered by themselves without regard to what one thinks about the personal beliefs of one of the Commissioners.[222]

None of the Conference speakers accused Carter of being a communist but several criticized what they saw as an egalitarian bias to the Report and associated it with socialist, communist and totalitarian ideologies. Alun G. Davies, Executive Director of Rio Tinto Zinc Corporation, had this to say concerning the principle of "ability to pay":

> It is essentially a redistributionist, egalitarian argument and I am most surprised that Canadians are expected to swallow it. It is based on the Robin Hood theory of taking money from the haves and giving it to the have-nots. But when the government plays Robin Hood, it keeps a lot of the money to grease the government machine.[223]

Davies continued his attack on the Report in commenting on the "package" aspect of the recommendations:

> The Carter Commission presents Canada with a package deal. To me a package deal like this represents something immoral if not illegal. It is like tie-in sales -- you can't buy what you want unless you also buy what the salesman wants to dump on you. There are aspects of this Report which are good; but as a package deal it purports to put everything into the proper

> slot. It stinks of George Orwell's 1984 and the perfectionist state, arranging everything, forgetting nothing. It is perfect but inhuman.[224]

Most businessmen and tax professionals had long been advocating more and better tax incentives to encourage capital investment, while many taxpayers and tax administrators were complaining of too many loopholes. The Carter Report had, in the same spirit as Leo Eisenstein,[225] perceived one man's socially beneficial tax incentive as being another man's immoral loophole. Davies, in reaction to the Report's ruthless efficiency in closing loopholes, departed from the usual discourse in being less reticent in talking about the virtues of tax loopholes:

> On this point I agree with Professor Kaldor. He once said that there was something to be said for having a tax system with loopholes in it. You had to cater for two types of individual; one who wants to pay all his legal dues up to the hilt as a matter of conscience, another who wriggles at the very thought of paying any tax. Unless you wanted to create unnecessary tensions in the body politic, you allowed some loopholes for the second type. I do not refer to loopholes merely because many of you are accountants and lawyers who would be on the bread line but for your exploitation of loopholes for your clients; loopholes serve a psychological as well as a fiscal need. The Carter Report leaves no loopholes. It has been framed by economists who don't understand how people behave, what makes people tick. It propounds a rounded system which takes care of every situation and has a place for everything. It is the system of the Welfare State, not the expanding frontier.[226]

Another representative of the mining industry, W.B. Dix, Vice-President and Treasurer of McIntyre Porcupine Mines, saw the Report as an ideological document requiring a riposte from tax professionals and businessmen:

> The Report is replete with highly socialistic concepts involving revolutionary changes in the philosophy of taxation and it is the duty and responsibility of Canadians to examine the proposals carefully and to make their views known, particularly in that segment of Canadian affairs in which they have had some practical experience.[227]

The penalty for failure to mobilize opinion against the recommendations was suggested by, among others, R.F. Winfield, L.A. and Vice-President of Finance and Administration for Shell Canada:

> ...there are many areas of the Report, as it applies to the petroleum industry, which need the most careful and critical examination by the public and by government. Anything else would be a gamble of the worst type, and what is to be lost, by way of a slow-down in one of Canada's most important industries and loss of international and general investor confidence, is unknown but practically limitless.[228]

Academic specialists were assigned to speak on aspects of the Report close to their own research interests. Several found themselves in the position of being in general sympathy with the basic thrust of the Report, yet focussing their specific remarks on parts with which they disagreed. This was the plight in which Professor J.S.A. Wheatcroft of the London School of Economics, and a friend of Carter, found himself. Assigned to speak on estates and trusts, Wheatcroft, although an admirer of the Report, had not been fully persuaded by the application of the comprehensive income concept in that area:

> Some of my British colleagues at this Conference have been strong critics of the Report. Most unfortunately I have been assigned to the one part of the Report -- gifts and trusts -- in which I am also a critic. I hope that any criticisms which I offer today on that part

> will not be taken as criticisms of the main recommendations of the Report, which I personally regard as extremely far-sighted.[229]

Robert M. Clark, Professor of Economics at the University of British Columbia, spoke on "Some Effects of the Recommendations for Pension Plans". While professing to admire the Report, and applauding "the obvious influence, at most points, of ...[his] fellow economists..." was however, "unfavourably impressed by the treatment of pensions in a few major points".[230] Clark was one of several critics of the Report to make effective use of wit and verse:

> On the subject of taxes, said Carter,
> Reform is a must! For a starter
> Define income in terms so wide
> That not a cent is left outside,
> Not even the gains made in barter.
> Concerning a man and his pension,
> There are changes too many to mention.
> Encourage him up to a point,
> Then chop him off right at the joint,
> Though inflation will add to his tension.[231]

While acknowledging that his criticisms arose "largely out of differences in value judgments on the role of pensions in our society....", this witty verse from an economist who was not persuaded by the reasoning of his professional colleagues associated with the Commission, added confidence and credibility to the opponents of the Report.

The tax specialists at the Conference who favoured the Report in general, but found it deficient when it came to their own areas of expertise, contributed, notwithstanding their protestations, to the shadows of doubt being cast on the entire Report. What was the

untutored layman to think if many of the experts who had praise for the Report in general, were nevertheless critical of it in the areas where they were the most competent to offer an opinion?

Herbert O. Spindler, C.A., of the Montreal office of McDonald, Currie & Co., probably voiced the ambiguous feelings of many tax professionals who found the Report to be logically compelling yet somehow unacceptable that capital gains should be taxed at the same rates as other income: "It is probably fair, rational and even inevitable. And yet -- somehow it's rape!"[232]

George T. Tamaki, of the Montreal law firm, Stikeman, Elliott, Tamaki & Mercier, had, along with Commissioner Beauvais, been a member of the Committee of Four appointed by Donald Fleming in 1960 to investigate the problem of the taxation of corporate distributions. The conference participants would have agreed that few could have spoken on the subject with greater authority. Tamaki's comments focussed on the differences between the Carter Commission's proposals for taxation of corporate distributions and the modified Committee of Four's proposals supported by Beauvais in his minority report:

> Because the majority of the Commissioners were committed to the idea of a comprehensive tax base with capital gains being taxed at fully progressive rates, they could not accept the Committee of Four proposals -- as modified by the Canadian Institute of Chartered Accountants and the Canadian Bar Association. The basic proposal of the Committee was to levy a once-and-for-all flat 15% withholding tax on dividends. This proposal was, in essence, one of partial integration without a capital gains tax. It is understandable that, having recommended a system of tax at progressive rates on share gains realized by residents as well as on all

> successions outside the family, the Carter Commission felt it could not at the same time do less than recommend full integration which, in effect, abolished corporation tax as such. If the proposal for tax at full progressive rates on share gains and again on successions is not acceptable to the government, the Committee of Four proposals might well have to be reconsidered, as was suggested by Mr. Beauvais who was also one of the Committee of Four....
>
> It is recognized, of course, that as a matter of practical politics, the abolition of corporate tax may not be acceptable as being equitable without some compensating tax on share gains. However, such tax need not be at full progressive rates and there certainly should not be a double tax on the same property on death. At the same time, it is a sobering thought that once the comprehensive tax base is accepted it is possible for a capital gains tax to be introduced without integration -- or full integration to be withdrawn or modified some time later after the introduction of a capital gains tax.[233]

Pat Thorsteinsson had commented on a draft of Conway and Smith's study of the capital gains jurisprudence for the Commission, thereby helping them to "sell" to the Commissioners the idea of taxing capital gains in the same manner as other income.[234] At the Conference, however, Thorsteinsson clearly explained where he and the Commission parted company:

> I have long been an advocate of a form of capital gains tax -- but not this form -- principally because I think the time is long overdue when the taxpayer should cry "uncle" and give up the struggle he is steadily losing over the years in the courts. There is hardly a taxpayer who has gone trembling into the Exchequer Court in a capital gain case who, I think, would not have happily settled for something like 25% -- and there, to my mind, lies the substantial merit of the U.S. system.[235]
>
> ...I should state once again my own bias on the subject. Bias is significant because we are all of us dealing with a set of proposed changes in the tax structure, which are to my mind at this stage almost wholly a question of politics -- certainly not of law.

> The majority Report exhibits a bias in favour of thoroughgoing egalitarianism -- a dollar is a dollar, no matter what its source. That is a viewpoint, a bias if you will, and the fact that it is held by four of the six Commissioners does not make it right, or necessarily any better than a different viewpoint or bias. My own bias is this: in common with Commissioners Beauvais and Grant, I agree that capital gains should be taxed, but on a basis of some preferential treatment that recognizes the significance of incentive in decisions about risk-taking.[236]

John de M. Marler, Q.C., of the Montreal law firm of Coté, Ogilvy, Bishop, Cope, Porteous & Hansard, took exception to the apparent presumption in the Report that one of the principle functions of trusts was for tax avoidance. He quoted the sentence in the Report, "A trust should be regarded as an instrument to be employed for good personal or business reasons and should not be permitted to be used as a tax-avoidance device",[237] and the Commission's comment that, if its recommendations were implemented, it "...should reduce the number of trusts which were created".[238] Marler then described an imaginary playlet in which a young couple planning their financial future realized that they need not resort to the customary vehicle of a trust to avoid estate tax. The scene closed with a chorus of trust company presidents and general managers, chanting in Gilbert and Sullivan style:

> The efforts of our P.R. staff have long since been
> purely promotional,
> Our relationships with husbands and wives have been
> everything else but emotional,
> To preserve their estates was our aim,
> The objective we found full of beauty,
> A target to praise, not to blame,
> Was to fully eliminate duty.
>
> To accomplish this laudable end,
> Indeed, it was almost a must,

> To save tax, yet let the wife spend,
> Could most simply be done by a trust!
>
> In our innocence we thought trusts fine
> And they made for us an honest penny,
> Now we're told, of our object sublime,
> That of trusts there are simply too many.[239]

Marcel Bélanger, C.A., Bélanger, Dallaire, Gagnon & Cie, Québec, former Chairman of the Quebec Royal Commission on Taxation, and one of the Quebec delegates to the Tax Structure Committee, while fully supporting the comprehensive income concept, charged that the Commission had exceeded its terms of reference in making recommendations concerning the federal-provincial sharing of taxes. In any case, he said, the offending recommendations need not be tied to the comprehensive income package. However the chapter of the Report on federal-provincial matters[240]:

> ...threatens to turn public attention away from the basic features of the Report proper. Indeed, this is exactly what is happening, at least in Quebec where press, radio and television commentaries -- and they have been anything but favourable -- dealt almost exclusively with the Report's federal-provincial implications....[241]

Among the speakers at the "Summing-up" session was Joseph A. Pechman, Director of Economic Studies at The Brookings Institute, who had been a partisan of the comprehensive tax base when Carter first discussed tax reform with him in his Washington office in 1963. Probably no one was surprised to hear his unqualified praise for the Report:

> The Commission discharged its responsibilities with distinction. It examined the present system, found it unacceptable on numerous grounds, and produced an

> alternative which -- if adopted -- would make Canada's tax system the best in the world. The Report will undoubtedly take its place among the classics of taxation.[242]

H. Heward Stikeman, Q.C., senior partner in Stikeman, Elliott, Tamaki & Mercier of Montreal, began his attack on the Carter Report by quoting Eisenstein's aphorism that taxes are the result of the group struggle to make other people pay them, then added a Burkean touch to make the process more civilized, and, at the same time, more natural:

> In less blunt language, what really happens, and has happened historically in Canada, is that over the years the politicians and businessman have managed to evolve a more or less workable compromise under which revenue has been raised and the economy going ahead, while giving the politicians largesse to dispense through Parliament. Gradually, a pattern has evolved and Canadian business has shaped itself to get the best treatment under the existing system, consistent with the law. This is not just a question of tax avoidance or evasion. One must remember that during the last fifty years, the same system, with minor refinements, has been in effect in Canada, in the United States, in Great Britain and many other western countries. It is thus a truism that every facet of business conduct is touched, shaped and influenced by the particular tax system. For example business profits are estimated on the footing of how much will be left after known taxes on a known base; capital requirements are forecast within the same terms of reference; capital structures are created with respect to existing tax laws; a large portion of company law has grown up and been shaped by the fiscal influences around it; inventory valuation; scientific research; natural resources; industry planning and incentives, all these have been directly coloured by the tax system in force. Not only this, but each of the facets of business so affected are interrelated in an integrated operation. Likewise, the "personal" taxpayer, as opposed to the "business" taxpayer, over the generations since 1917 has tended to arrange his affairs so as to get the best advantage of the present system. Trusts have been set up, wills have been drawn, investments have been made, family dispositions have been effected and every facet of human financial life has been directed by the good or less good fiscal consequences under the present system.[243]

His message was that an old tax system is a good tax system, and that any reform to such a wide-spread, complex and sensitive equilibrium would clearly have to be carefully thought out and involve a minimum of change, for fear of unanticipated and unjust consequences for a multitude of individuals. Added to this was the dislocation that would result in Canada's business and financial links with its trading partners, as well as the intricate network of tax treaties with many countries.[244] Against any hypothetical benefits to be derived from change, had to be weighed the loss of the taxpayers' and policy-makers' knowledge of the familiar:

> Thus, the first question to be asked is can we afford, this far down the line, to give up all we have learned not only in Canada, but in many other comparable tax jurisdictions, in exchange for a system as yet entirely untried and, what is much more important, a system that inevitably will be subject to the same pressures and forced modifications of economic and political life that have evolved the existing one. In short, we must first ask ourselves, is the exchange worth the cost in terms of dislocation, business uncertainty and all the attendant unpleasantness, and then, if we say that it is worth it, we must also ask ourselves whether the system we will get under Carter will remain itself unaltered, because if it is altered, we are told by its creator, it loses much value. I do not believe either question can be answered in the affirmative.[245]

Those present who remembered Stikeman's address to the 1961 Tax Conference, calling for "a revolutionary approach" to reforming the tax system,[246] would have marvelled at how his appraisal of the existing tax system had mellowed after six years when set in the context of the Carter recommendations.

The Conference participants had been directed, not only to discuss the Carter Report, but also to consider other alternatives to the existing system. Stikeman wanted the path of tax reform to end much closer to the existing system than to the more radical Carter recommendations. The alternative suggested by the Committee of Four (including his partner, George Tamaki, and Emile Beauvais) was a promising option for a more mild, technical fix to the existing system:

> First, I definitely do not think the present Income Tax Act or the system that it typifies is past redemption. On the contrary, I believe that if the time and effort that went into Carter could have been lavished on the present framework, the present structure could well have been salvaged with less dislocation and greater benefits. Even in the most perplexing area, that of corporate surplus distributions, we have had evidence, before Carter started, of a viable solution. The Commission draftsmen rather brushed aside the Report of the "Four Wise Men", or the "Committee of Four", as it is referred to by the Commission, but only because it did not fit their overall thesis.
>
> Second, use some of Carter's ideas apart from the comprehensive income base, such as integration, a portion of the family unit concept through joint returns for husband and wife, deduction of "nothings", and open discussion of budgetary proposals before legislative enactment.[24]

Stikeman suggested combining these changes, (some of them intended by the Commission majority to soften the blow to upper-income taxpayers resulting from the comprehensive tax base) with the continuation of the tax incentives enjoyed by mining companies to other resource industries.

The final speaker of the "summing-up" session was W.D. Twaits, President of Imperial Oil Limited. Twaits had been an advocate of tax

reform before the appointment of the Carter Commission, but was horrified at what the reform process had brought forth. In addressing the Foundation Conference, he was repeating what he had said to his company's shareholders the previous week.[248] He was especially critical of the proposed removal of capital cost allowances during the "pre-earning" stages of resource industry investments, and the removal of depletion, saying that the oil industry already pays more than its share of taxes of all kinds, and that "knowledgeable capital" would be invested elsewhere if adequate incentive were not provided in Canada.[249] Given what amounted to the last word at the Conference, Twaits presented four "basic issues on which the Commissioners' report must be judged":

> 1. Can overwhelming controls proposed for the federal tax gatherer be accepted at the expense of individual initiative, of the human skills which we so urgently require to develop further this country? Are we in effect prepared for the impact of this concept on the ever-increasing number of highly skilled men and women graduating from our expanded educational system, who are now making the decision of how and where to dedicate their talents?
>
> 2. Can we, a nation so utterly committed to international trade, adapt a concept of taxation so much out of line with our international competitors, in trade and money markets?
>
> (3) Can we accept any recommendations without an equivalent study of provincial and municipal tax needs and indeed the whole question of government expenditure by multiple levels in this country? The current opposition of property owners is dramatic evidence of the rising resistance to provincial/municipal taxes.
>
> (4) How do those provinces so dependent on resource-producing industries adjust their policies and how can the pattern of investment be adapted to the sweeping changes without a phase-out over many years?[250]

manner, out of the heat of public debate, presenting in its place a government proposal more amenable to modification as the arguments and pressures of the tax reform debate took effect. In addressing the Queen's seminar, Sharp therefore invited comments and suggestions, not simply on the Carter Report, but also alternative reforms:

> We would like to get as rapidly as possible to the position where it is not the Carter report that is being studied, but the Government's policy statement.[268]

As Thorsteinsson had indicated, Mr. Sharp would have expected a modified tax on capital gains to be a feature of a number of such alternative suggestions. The idea was already contained in the minority reports of Beauvais and Grant. The following week, Ronald Anderson, the Globe and Mail reporter who had attended the Queen's seminar, stated that:

> ...most Canadians are resigned to the probability that a tax will be levied on capital gains. All that is in doubt, judging by informed comment, is the form the tax will take and the rate of the levy.[269]

The Canadian Bar Association:

The Canadian Bar Association appointed a special committee of 14 tax lawyers, chaired by Donald Clark Q.C., of Vancouver, to study the Report.[270] The Vice-Chairmen were W.A. MacDonald of Toronto and R.H.E. Walker, Q.C. of Montreal, with Ronald C. Merriam, Q.C., Secretary of the Canadian Bar Association, as Secretary. Harold Buchwald, a member of the committee, and an active Liberal, used his

Reporting of the April Tax Conference:

The reporting in the Globe and Mail was detailed and accurate in the material presented, although tending to present more prominently the negative thrust of most of the discussions. The April 26th edition covered the first day of the Conference on three pages of the business section under eight story headings, all of them critical of the Report. Under the heading "Would bizarre marriage deals be result if Carter plan adopted?", Marshall A. Cohen, of the Toronto law firm of Goodman & Carr, quipped, "I have visions of fathers marrying their daughters to carry forward the unit."[251] The scathing comments of W.B. Dix, Vice-President and Treasurer of McIntyre Porcupine Mines were reported under the heading, "Endangers Canada market ability, Tax plan seen as competitive snag".[252] The same story also reported the remarks of William E. Haviland, an economist with the Canadian Pulp and Paper Association and the Newsprint Association of Canada, who said that the Report was probably mistaken in thinking that an open economy like Canada could get large amounts of increased taxes from non-residents for nothing: "The risk of provoking retaliation should not be glossed over."[253] On the same page, another heading read "Mining, Oils to bear cost, economist says", quoting G. David Quirin, of the School of Business of the University of Toronto, who called the mining and oil recommandations "the most deplorable of the entire report."[254]

Under the headline "Carter Report: The Great Debate", a full page of reporting featured the following headings:

"Proposals termed too uncertain as basis for oil industry's future"
"$12,000 pension ceiling called much too low"
"Drastic investment policy changes indicated by financial spokesmen"
"Staff problems seen"
"Sales tax accord doubted."[255]

The stories under these headings reported the remarks of 18 Conference speakers, all but 4 of them unfavourable to the Report. Of about 84 column-inches of text, only about 3 column-inches sang the praises of the comprehensive tax base.

The next day's reporting showed a similar amplification of the imbalance of opinion at the Conference. John de Marler's witty playlet was featured at the top of the page, under the heading, "Is there no room for trust between husband and wife?", and introduced with the remark that the participants, "after criticizing various proposals in the Carter report they ended up laughing at it."[256] Other story headings on the same page were:

"Conference divided up to last word"
"Can't centralize taxation: official"
"Economic isolation predicted if Carter proposals adopted"
"Change urged in proposed capital gains tax"
"Sharp aims for legislation on Carter report next year."[257]

The Government's Tax Reform Schedule:

One of the final events of the April Tax Conference was the banquet at which Mitchell Sharp announced that the government would,

after receiving representations from the public, issue a White Paper on tax reform. The White Paper, rather than a draft bill, would be referred to a parliamentary committee, offering an additional opportunity for public debate and representations.[258] It was clear by that time that, while a number of economists and foreign tax specialists held the Report in high esteem, it was very unpopular among Canadian tax practitioners and most businessmen. Mr. Sharp probably knew what to expect when he repeated his invitation for additional public comment on the Report.

After thanking the Tax Foundation for organizing the Conference, Sharp assured his listeners that the government valued their advice "highly", as it did "the promptness with which it ... [had] been given".[259] Sharp, however, declined to express any opinion himself:

> ...I have deliberately undertaken that during the next few months I will not comment on the substance of the Carter Report.... This decision has been taken in order that others will have an ample opportunity to study the Report and discuss it before the government endeavours to come to decisions about it. Any comment by Ministers or leading officials of the government before decisions are reached on it might well be taken as a sign of what the government's intentions are, a signal that might be misleading and even harmful. I recognize that silence on our part at this time runs the risk perhaps that those with particular interests may speak out while no one speaks out in support of the general interest. I feel this risk must be run, however, if taxpayers are to have a fair and proper opportunity to study and react to proposals of a fundamental, even radical character that could affect all of us, rich and poor, throughout the length and breadth of the land. I hope that those who have the general public interest at heart will not hesitate to express their opinions.[260]

Sharp said that he hoped to have legislation passed by the end of

Sharp, but only after taxpayers had had two opportunities to express their opinions, first on the Carter Report, and then on the Government's tentative position on tax reform expressed in a White Paper:

> I hope to be in a position in the autumn to place before my Cabinet colleagues recommendations for major revisions in the main features of the income tax. These recommendations would be made after consideration of the Report and of the comments we have received on it by that time. They would be recommendations subject to revision after they are publicly studied and debated.
>
> I think this first group of government decisions would be incorporated in a White Paper which could contain an explanation of the main proposals we intend to make in regard to the income tax. Such a paper would have to cover some important details in order to make clear how the proposals would work in general and the nature of the solutions that we propose for problems which the Royal Commission has not itself solved. I expect that Parliament will wish to have a committee consider the White Paper. Further details would be incorporated in a draft Bill which we would publish later and which might well incorporate changes resulting from the views we receive in Parliament, from taxpayers, and from the provincial governments which of course have a strong interest in these matters.

Allowing for comment and revision of the draft Bill, there would therefore be three periods for taxpayers to debate tax reform proposals and to make representations to government. Sharp called for written submissions on the Report to be sent to the Department of Finance by September, and that, as far as possible, these might be followed up by oral presentations. Perhaps anticipating his audience, Sharp acknowledged that this did not allow them as much time as they would have liked, and that the process of professional meetings might have to be accelerated. He then invited specific comment on the following Commission recommendations:

1. The inclusion of capital gains in the income tax base and the deduction of capital losses from income subject to tax.

2. The integration of the corporate and personal income tax by means of a gross-up and credit arrangement.

3. The inclusion of bequests and gifts in taxable income, instead of taxing them under separate plans as now.

4. The averaging of income over a number of years for the determination of tax, and other arrangements with a similar purpose.

5. The taxation of the family unit, and the appropriate rates to apply to it, as compared to separate individuals.

6. The exemption from tax of contributions to and earnings on pension plans and other retirement savings plans, from which payments would be fully taxable, and what and how much is to be included in such plans.

7. The expenses to be deductible in determining business and employment income.

8. The application of a single rate of corporation tax to all corporate incomes, and the proposed flexibility to be allowed in charging off all capital costs incurred by small and risky businesses.

9. The proper tax treatment of mines and of oil and gas income.

10. The basis for taxing income of Canadian corporations from sources outside Canada.

11. Finally, how far all these major recommendations are essential parts of a single package and how far there can be variations in what is included and the time of their incorporation in the system.[262]

Sharp acknowledged that the submissions could not possibly deal with all the problems of detail that would arise in discussion of even this partial list of Commission recommendations, and he explained that

the Department had already been examining many of these details:

> We are already aware from the advance study of the work of the Commission made by our officials that there are a great many problems of detail to be solved in carrying out what has been proposed, or possible alternatives. My department and the income tax officials are working on these problems of detail so as to be ready to deal promptly with the decisions which the government intends to try to make later this year, but there is a great deal to be done in translating general ideas into a consistent and workable law. We shall need much help from the comments and suggestions of those with special knowledge and ability.[263]

The tone of the April Tax Conference, and the early submissions reaching the Minister of Finance did little to strengthen any inclination he might have had to reform the tax system along the lines recommended in the Carter Report. In his June 1st budget speech, Mr. Sharp had occasion to comment further on the Report in the House, noting that it "bristles with both technical and policy problems and, need I add political problems".[264]

Mobilizing Opposition to the Report

During the following six months, between the April and November, 1967 Tax Conferences, a propaganda war was waged against the Report at the annual meetings of corporations, especially those in the mining and oil industries, in the newspapers, and at business and professional conferences. Business and the tax professions mobilized to take full advantage of Mitchell Sharp's invitation for comments,

The third week in May, however, a tax management conference, sponsored by the Department of Economics at Queen's University brought defenders of the Report, Douglas Hartle, and Professor S.M. Beck of the Queen's Faculty of Law up against some of its critics. The latter included K.H.J. Clarke, an assistant Vice-President of the International Nickel Company of Canada, R.F. Ruben, President of North Canadian Oils, and Pat Thorsteinsson.

Philip Vineberg told those at the Queen's conference that opposition to the Report on federal-provincial grounds were based on an over-simplification and misreading of the proposals. The provinces were being asked, not to give up taxes, but to accept revenues on a broader base: It would not be hard to persuade the provinces to collect tax on the new base -- in fact it would be hard to stop them."[265] The representatives of the mining and petroleum industries were challenged by H.O. Spindler, C.A. of McDonald Currie and Company of Montreal, to justify their existing tax incentives.[266]

Pat Thorsteinsson predicted that, while a capital gains tax would eventually result from tax reform, it would be at a reduced rate, perhaps similar to the American system:

> I think Mr. Sharp probably expects to sell those modified changes to the business community in part on the very basis that they are less extreme than the alternative of implementing the report recommendations in full.[267]

Part of the government's strategy was to move the Carter Report, which presented the question of tax reform in such an uncompromising

manner, out of the heat of public debate, presenting in its place a government proposal more amenable to modification as the arguments and pressures of the tax reform debate took effect. In addressing the Queen's seminar, Sharp therefore invited comments and suggestions, not simply on the Carter Report, but also alternative reforms:

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column, "The Tax Corner", in the Globe and Mail as a platform for regular attacks on the Report.[271] In one column, Buchwald described the growing opposition to the recommendations, which had "become the Centennial project of a great many":

> Not the least involved are the professional associations, which as organizations, have no special interest or bias to advance, although their members undoubtedly have strong personal views of a philosophical, political or even economic nature. Rather, the Canadian Bar Association, the Canadian Institute of Chartered Accountants and similar groups can formulate their approaches with an intellectual neutrality, concerned only with the intrinsic validity of the report's proposals and their workability.[272]

At the Association's annual meeting in Quebec in early September, Buchwald was one of a three-member panel speaking on the Report. The Globe and Mail printed his warning that implementation of the recommendations would lead to "a dull, grey frustrating society in which foresight, initiative, sacrifice and skill brought no reward, but rather severe penalties."[273]

Ronald Robertson, a speaker on the same panel, was more balanced in his comments, pointing out the the recommendations flowed logically from the Commission's concept of equity as ability to pay. He attributed the hostile reception to the Commission's uncompromising thoroughness in pursuing its concept of equity:

> And when in doubt, tax it, and to hell with the ancient distinctions about capital, income, gifts and so on.... Had the commission been a little more gentle in some of its pronouncements and revealed some of the agonies I feel sure were experienced in reaching some of the conclusions, I suspect there would have been less adverse reaction, or at least more sympathy.[274]

The comments of several other tax lawyers at the Bar Association conference were also reported in the Globe and Mail. Wolfe Goodman of Toronto, while generally supportive of the Report, expressed detailed criticisms of the proposals to include gifts and bequests in taxable income.[275] I.H. Asper, a Winnipeg tax lawyer and active Liberal Party member, called the recommendations "defeatist in their passion for redistribution of wealth through the tax system".[276] Rather than being "content to allow market activities to govern the redistribution of wealth", the Report "was an accusation of failure of the free enterprise system".[277]

On the second day of the conference the Report came under attack from three of the most renowned tax lawyers in the country: Stuart Thom, Pat Thorsteinsson and H. Heward Stikeman. Forgetting that many tax professionals, using the vehicle of Tax Foundation conferences and other avenues of influence, had been pressing for a Royal Commission to investigate the tax system, Thom wondered aloud how tax reform had become entrusted to a body without any political responsibility:

> It would be a very interesting study in itself to examine the reasons that led a considerable part of the public to think that a perfect tax system without fault or flaw could be dreamed up by a group having no political responsibility.[278]

Thorsteinsson claimed that the Commission had erred in mistaking the removal of a disincentive (the proposed full deduction of capital losses) as the substitute for "a genuinely attractive incentive", for without "the pot of gold at the end of the rainbow" there would be no

incentive for business innovation.[279] Stikeman suggested that the Commission's "entire treatment of international income... [was] retrograde and nationally oriented. Robert Walker, Vice-Chairman of the Association's Taxation Committee, said that some of the Carter proposals might lead to a substantial reduction in foreign investment in the insurance business in Canada.[280]

The brief presented by the Bar Association to Mitchell Sharp in the autumn did not oppose the principle of the taxation of capital gains, but recommended that the rate not exceed, or be somewhat lower than, the U.S. rate.[281] The brief recommended the exclusion of gifts and inheritances from the tax base, partly for administrative reasons, but also because their inclusion was not compatible with the Association's model of society sanctioning the inter-generational accumulation of capital:

> A taxing system should, we think, not seriously discourage the formation of private capital for the benefit of one's descendants.[282]

While being more moderately worded than the more colourful comments of some of its prominent members, the brief placed the Bar Association squarely in the camp of the opponents of the Carter proposals.

Canadian Institute of Chartered Accountants:

The Canadian Institute of Chartered Accountants also appointed some of its specialists to a taxation committee to study the Report, express the views of the Institute, and to co-operate with the tax committee of the Canadian Bar Association. The Chairman of the Institute's Committee, L.F. Heyding of Toronto, a senior partner in Peat, Marwick, Mitchell and Co., was reported by the Globe and Mail, as being against the Carter Commission's solution to the objective of equitable taxation.[283] He said that "unsavory tax evasion devices" could be eliminated "without a drastically different tax system", and that the clients of chartered accountants were "not seeking ways to avoid tax -- but they don't want to fall into a tax trap."[284]

The Report was a major item on the agenda of the annual meeting of the Institute, held in September.[285] While the speakers focussed on different aspects of the Report in a more technical than polemical style, the overall slant was decidedly against the Report. The Globe and Mail reported that a panel of chartered accountants had reached a consensus that, if the Carter recommendations were implemented, the number of taxpayer errors would increase.[286] According to G.E. Cronkwright, a partner in Clarkson, Gordon and Co.:

> Despite the Carter commission's creed of equity, the average taxpayer will be so confused by the system that he will be unable to obtain the equity intended for him....[287]

Pat Thorsteinsson predicted that, regardless of what happened to the Carter Report, there would be a tax on capital gains. He urged those who agreed with his contention that "the economy needs the contribution of the few who benefit from capital gains" to oppose the taxation of capital gains at full income rates in favour of a tax at reduced rates:

> You may or may not agree with my compromise position of advocating some tax on capital gains, but I should like to point out to you that there may be some danger that this debate will be lost by default.
> The Government is now considering a highly articulate and well-reasoned proposal to tax capital gains in full. I think it has missed the point and the significance of the effect that will have on investment incentive. If you agree with me, the time is now, very emphatically now, to make your views known in every way that is open to you.[288]

The Institute's brief to Mitchell Sharp registered its opposition to all but two of the twelve sets of recommendations which the Minister of Finance had asked for detailed comments. The chartered accountants were only prepared to agree to more liberal methods for deducting business expenses and to the single rate of corporate tax.[289]

The Economists:

The professional critics of the Report, chiefly lawyers and chartered accountants, sometimes referred to it as an economist's report. While this was denied by Harvey Perry at the November, 1967

Tax Conference,[290] the economists and public finance specialists were generally more positive in their assessment of the Report. Of 35 economists listed in the programmes of the two Canadian Tax Foundation conferences in 1967, 22 generally supported the Report, while only 7 were clearly opposed. Speaking at the end of May, Carter expressed his satisfaction at the favourable reception given his Report by the economists:

> I'm thrilled by the reaction of the economists, since I view the report as an economic document, not a social document. The economists understood the report quickly.[291]

The Canadian Economics Association published a special issue of its journal the Canadian Journal of Economics in which readers who could penetrate the technical language of some of the papers would have gained a generally favourable impression of the Carter Report.[292] However, the special issue did not appear until February of the following year, by which time the tide of opinion had decisively turned against the Report. In addition, the more limited exposure of economists' professional writing to the business and political worlds ensured that their influence on opinion outside the universities would be limited.

One notable exception was the lyrical praise of Richard Musgrave, Professor of Economics at Harvard, whose gothic imagery so captured the fancy of the editor of the Globe and Mail that a choice paragraph was reproduced on the editorial page:

> The Carter Report stands as a landmark in taxation.

> Encompassing six volumes plus numerous research studies, its sheer monumentality and structural logic tower over the reviewer. The spire of vertical equity reaches into the heavens of non-discretionary income; the nave of horizontal equity is sweeping in its purity of accretion; and the transepts of constructive realization and integration complete the unity of Simonesque design. The pilgrim cannot but bow to the architect and craftsmen who created this impressive work.[293]

There was some hidden ironic humour in Musgrave's praise for the "architect", as Douglas Hartle had derived his inspiration directly from Musgrave's writings.

Economists who opposed the Report, largely those working as independent consultants or for corporations, made their views count by getting them published in the newspapers, by assisting in the preparation of briefs to the Minister of Finance, or by assisting groups, businesses or political parties in formulating their positions on tax reform. J.W. Popkin, an economist working for Sun Life Assurance Company of Canada, added credibility to his company's stand against the Carter Report, when, in an address to a meeting of investment specialists of the Canadian Life Insurance Association of Toronto, he said that the Carter Report had lessened the likelihood of business capital spending being stimulated by recent tax cuts.[294] J.R. Petrie, a consulting economist, prepared a critical analysis of the Report for the Canadian Chamber of Commerce.[295] Professor Robert Clark of the Department of Economics at the University of British Columbia, who had delivered a paper at the April Tax Conference critical of the Carter proposals regarding pensions, participated at the Conservative Party's policy conference at

Montmorency Falls, in August, and, along with Toronto accountant, Gerald Townsend, tried unsuccessfully to persuade a policy committee at the Conservative convention to accept the principle of a reduced capital gains tax.[296]

Business Associations:

Summer and fall meetings of business associations brought corporate executives and tax professionals together to voice their concerns about the consequences of implementation of the Carter Recommendations. While some well-known tax professionals, notably Philip Vineberg and Ronald Robertson, defended the Report against what they charged had been ill-informed or unfair criticism,[297] the dominant mood was one of hostility to the Carter Report.

The Canadian Manufacturers' Association devoted much of its annual convention to a discussion of the Carter Report. Carter was there in person to defend his proposals, pointing to the fact that they included some of the ideas put forth in the Association's brief to the Commission, such as the abolition of corporation taxes, its reservations regarding the effectiveness of tax incentives, and the creation of a national sales tax at the retail level; while also acknowledging areas where the Association's ideas were not adopted.[298]

Dan Throop Smith, Professor of Finance at Harvard Business School,

warned that discrimination against income earned by Canadian corporations through foreign subsidiaries would invite retaliation by foreign governments, and make Canada "inattractive for foreign direct investment, with adverse results on its balance of payments and economic growth."[299]

Marcel Bélanger, formerly Chairman of the Quebec Royal Commission on Taxation, who had since joined his provincial government's delegation to the Tax Structure Committee, renewed his criticism of the Report's venture into the field of federal-provincial tax-sharing, a matter beyond the Commission's terms of reference and which should have been left to the Tax Structure Committee.[300] He had high praise for the Report, however, and thought that the provincial governments ought to make concessions where necessary in order to permit the working out of "a coherent system, avoiding double taxation and needless annoyance for their taxpayers."[301]

While they had been prepared to listen to speakers on both sides, the Canadian Manufacturers' Association rejected the major recommendations in their brief to the Minister of Finance.[302] The 96-page brief, submitted on October 4th to Mitchell Sharp by the Executive Vice-President, J.C. Whitelaw, said that a capital gains tax would be "completely inappropriate and unacceptable" in a "capital-hungry country such as Canada".[303] Although the Association had complained of the "double taxation" of corporate income in its brief to the Royal Commission, it was doubtful about the Commission's integration proposal, and opposed to the inclusion of

gifts and bequests in taxable income, which might reduce the amount of capital available for saving and investment.[304] The proposed single rate of corporate tax would hurt small business, and the recommended treatment of foreign-source income "would probably necessitate removal of the corporations to a foreign country, leaving only a small branch or subsidiary operation in Canada."[305]

The Canadian Chamber of Commerce, meeting in Montreal from September 18th to the 21st, heard the Report denounced as "socialistic and potentially damaging to principles of free enterprise."[306] W.H. Flynn, Ontario General Manager of Canadian Industries Ltd., and chairman of the Chamber committee studying the Report, said that, while the Chamber had supported government use of fiscal policy for economic stabilization purposes, it was the impression of a great many people who had studied the Report, that it was "advocating much greater use of federal Government tax and expenditure policies for controlling the economy."[307] C.B. Neapole, President of the Montreal Stock Exchange, reversed his earlier, favourable, opinion[308] and expressed dismay at the seeming apathy of so many people "to what can only be regarded as an apparently unchecked submersion in socialism."[309] Neapole foresaw dire economic consequences resulting from any attempt to implement the major recommendations:

> I can only feel apprehension about the increasing cost of government, the disruption in capital markets, the decline of our appeal to foreign investors and the damage to our ability to compete in foreign markets.[310]

At its closing session, the Chamber approved its brief to Mitchell Sharp, which was the product of the special committee's study of the report. According to Fraser Robertson's column in the Globe and Mail, the Chamber had been "able to call upon a large number of experts to make a concentrated study of each major section of the report..." and the brief had the added credibility associated with the Chamber, which, "had no particular or special interest to defend from change, except the interest of the country at large."[311] The Chamber opposed the Report's integration proposals, thus reversing its pre-Carter position against what it had called the "double taxation" of corporate income:

> In a society which has for many years taxed corporate earnings more heavily than most other sources of income, such a shift as would be caused by integration would be too disruptive and future governments would find it impossible to maintain.[312]

The 55-page brief, presented to Mitchell Sharp on October 6th by Chamber President, W.M. Anderson of Vancouver, also rejected the taxation of capital gains, the inclusion of gifts and bequests in income, the removal of the incentives for the mining and petroleum industries, and the proposed changes affecting insurance companies.[313] The Chamber also feared that the recommendations affecting foreign source income would hurt Canadian businesses operating internationally and warned that

> Some major Canadian companies would have to remove their corporate residences and head offices from Canada to remain competitive and fair to both resident an non-resident shareholders.[314]

The day after the Chamber had approved its brief and two weeks before it was presented to the Minister of Finance, this warning about the proposed taxation of foreign-source income received dramatic support. Speaking at the fall conference of the Financial Analysts Federation in Toronto on September 22nd, A.A. Thornbrough, President of Massey-Ferguson, one of the largest and best known Canadian corporations with foreign subsidiaries, said that, if the Carter recommendations were fully implemented, his company "would be forced to consider seriously a transfer of its head office from Canada...".[315]

Many other businesses and business organizations also opposed the Report, making news in the process, at annual meetings and conferences, press conferences and news releases, and at the presentation of briefs to Mitchell Sharp. The Vancouver Board of Trade, aided by their tax adviser, Jacques Barbeau, a Vancouver lawyer and former Research Director for the Canadian Tax foundation, presented a 30-page brief to Deputy Minister of Finance, R.B. Bryce; "some of his dfficials"; Northern Development Minister, Arthur Laing; Mines Minister, Jean-Luc Pepin; and Revenue Minister, E.J. Benson.[316] The Board representatives argued their case for a reduced tax on capital gains similar to that in the U.S., and opposed most of the other major recommendations, including those dealing with mining and petroleum, gifts and bequests, and integration. In addition to Barbeau, those representing the Board of Trade at the meeting were: J.R. Croll, treasurer of Placer Development Ltd; Robert G. Rogers, president and chief executive officer of Crown Zellerbach

Canada; H. Allan Dunlop, treasurer of B.C. Sugar Refining Co.; William G. Leithead, president of the Vancouver Board of Trade; Clifford Grandison, an economist; and E.L. Harrison, a director of the Canadian Chamber of Commerce and vice-president of British Columbia Packers.[317]

Between May and November, the business pages of the Globe and Mail included statements critical of the Report from the following additional groups and associations, or from speakers at events sponsored by them:

1. The Canadian Petroleum Association;[318]
2. The Canadian Life Insurance Association;[319]
3. The Petroleum Society of the Canadian Institute of Mining and Metallurgy;[320]
4. Society of the Plastics Industry of Canada;[321]
5. The Investment Dealers Association of Canada;[322]
6. The Toronto Junior Board of Trade;[323]
7. The Mining Association of Canada;[324]
8. The Independent Petroleum Association of Canada;[325]
9. The Canadian Export Association;[326]
10. The Investment Dealers Association of Canada;[327]
11. The Retail Council of Canada;[328]
12. The Trust Companies Association of Canada;[329]
13. The Northern Manitoba and Saskatchewan Prospectors and Developers Association;[330]
14. The Canadian Association of Oilwell Drilling Contractors;[331]
15. The Toronto Society of Financial Analysts;[332]

16. The Board of Trade of Metropolitan Toronto;[333]

17. The Co-operative Union of Canada;[334]

18. The Canadian Institute of Mining and Metallurgy, Newfoundland Branch;[335]

19. The Canadian Federation of Agriculture;[336]

20. The Saskatoon Board of Trade;[337]

21. The Toronto and Montreal Stock Exchanges;[338]

22. The National Farmers Union;[339]

23. The Association of Canadian Investment Companies;[340]

During the same period the submission of the favourable briefs of the Canadian Labour Congress,[341] the United Steel Workers of America,[342] and the Ontario Woodsworth Memorial Foundation[343] were also reported. In addition, there were two reports of statements made by Kenneth Carter in defence of his Report.[344]

Submissions to the Minister of Finance

During the summer and fall of 1967, at least nine hundred briefs were sent to the Department of Finance. A sample of 104 of these briefs, collected by Professor W.I. Gillespie of the Department of Economics at Carleton University, contains 39 briefs submitted by companies and organizations in the mining and petroleum sectors. At least 37 of these were in opposition to the Report's recommendations directed toward taxation of the mining and petroleum industries. Eighteen also opposed at least one the major sets of recommendations on the inclusion of capital gains, gifts and bequests outside the

family unit in the tax base, and the integration of corporate and personal taxes. None supported the taxation of capital gains as recommended in the Report.[345]

The same sample of briefs included 24 from the insurance and financial sectors, 16 of which opposed at least one of the sets of recommendations on inclusion of capital gains, gifts and bequests in the tax base, and integration. These sectors were also quite strongly opposed to the Carter recommendations respecting the mining and oil industries, with 10 firms and organizations indicating their disagreement and none registering support.[346]

Looking at the 31 briefs from firms and business associations in the manufacturing, transportation, retail and service sectors, 27 registered opposition to one or more of the proposals on capital gains, gifts and bequests, and integration, and none supported all three sets of recommendations.[347] As with the financial sector, opposition was also quite strong against the mining and petroleum recommendations, with 13 briefs in these sectors stating their disagreement and with none in favour. Three of these were from major steel companies with mining interests: The Steel Company of Canada, Algoma Steel Ltd, and Dominion Foundries and Steel.[348]

Some of the briefs which expressed opposition to major recommendations in the Carter Report came from sources which had initially been reported as being generally favourable. The Canadian Manufacturers' Association, the Canadian Construction Association, the

Toronto and Montreal Stock Exchanges, and the Retail Council of Canada all reversed or modified earlier, more favourable, positions taken by their spokesmen on the Report.[349] While opinion within the national and local Chambers of Commerce had initially been divided, their briefs to the Minister of Finance were solidly against the major recommendations.[350]

Of the 104 briefs for which we have coded information, only two, the Canadian Labour Congress and the United Church's Board of Evangelism and Social Services supported the three major sets of recommendations regarding the comprehensive tax base. The CLC also supported the recommendations on the mining and oil industries, as did its major affiliate with members in the mining industry, the United Steel Workers of America.

Press Coverage of the Anti-Carter Campaign:

The newspapers had been filled with initial commentary on the Carter Report during the first few weeks following its release. Throughout the spring of 1967, the Report was the favourite whipping boy at many corporate annual meetings. While the briefs were presumably being worked into shape during the summer doldrums, tax reform almost disappeared from the news. Beginning in September, the release of many of the completed submissions to the Minister of Finance resulted in another series of news stories condemning the Carter Report. Between September 1st and November 30th the Globe and

Mail contained 69 items on federal tax reform, of which 56 were, on balance, unfavourable to the Carter recommendations. Sixteen of the unfavourable reports originated with the public statements of mining and oil executives.

The coverage in the Globe and Mail during the seven-month period from May 1st to November 30th, 1967 included a total of 119 items on federal tax reform, 75 per cent of which had headings which were clearly critical of the Report or were generally unfavourable in their content, and only 6 per cent of which were favourable. The voices heard most often were those of tax professionals and mining and oil executives: 22 per cent and 19 per cent respectively of all items consisted primarily of reports of their comments on the Carter recommendations. All other non-agricultural business sectors accounted for 18.5 per cent of newspaper items. The voices of organized labour were rarely heard; less than 2 per cent of newspaper items from May to the end of November originated with their public statements. The same was true for agriculture, and the entire non-profit sector which together accounted for only 3.4 per cent of all newspaper items on federal tax reform. The federal government (chiefly the Minister and Department of Finance) accounted for 10 per cent of the stories, the same as for the provincial governments combined. Federal opposition politicians accounted for 3.4 per cent of statements featured in the Globe and Mail on federal tax reform, while editorials and signed columns accounted for another 22 per cent.[351]

The Mining Lobby and the Provincial Connection:

The common denominator among the statements opposing the Report was that its recommendations were not realistic in view of Canada's need for the investment capital required for economic growth. The mining and oil executives' statements were frequently made more persuasive by declaring that specific existing operations would not have been undertaken had the Carter system been in effect, or by the announcement of the cancellation of investment plans, accompanied by the calculated implications for employment in the regions affected. Between May and November of 1967, the following seven firms announced or intimated that plans for expanded activities might not be put into effect as a result of the uncertainty created by the Carter proposals:

Noranda Mines;[352]

Asbestos Corporation;[353]

Conwest Exploration Company;[354]

The Algoma Steel Corporation;[355]

The British-American Oil Company;[356]

The Steel Company of Canada;[357]

Syncrude Canada.[358]

One of the most dramatic statements was made by, R.V. Pavitt, President of Noranda Mines at the company's annual meeting in Toronto, when he announced the cancellation of two copper mining developments in British Columbia valued at $90 million.[359] The story was given the top place on the front page of the Globe and Mail, under the

headline, "Noranda shelves plans, blames Carter Report".[360] Only three days later the same paper reported that Mitchell Sharp would soon be issuing a statement "aimed at restoring confidence in the mining industry which has been shaken by the recommendations of the Carter report".[361]

Noranda's statement was part of a widespread reaction and publicity campaign involving several other mining companies, using annual meetings, announcements of the cancellation of investment plans, and the release of briefs to the Minister of Finance as occasions for making news. J.D. Barrington, who had criticized the Carter Report earlier from his platform as President of the Mining Association of Canada,[362] in his other role, as President of McIntyre Porcupine Mines, told the annual meeting of shareholders on May 3rd, that if the Report were to be adopted in its entirety,

> ...it would be a rapid road to mediocrity, socialism and a police state which would be necessary to enforce its recommendations.
> Surely our governments have not moved so far to the left that they have forgotten that Canada still is a frontier country demanding venture capital, individual initiative, and just reward if we wish to survive and prosper as a whole.[363]

The strong signals emanating from industry spokesmen were beginning to be echoed by the Premier of Saskatchewan, Ross Thatcher, who called the Carter mining recommendations "ill-advised and short-sighted", attributing the deferral of two potash mining complexes in Saskatchewan to uncertainty arising from the Report.[364]

The pressure from the mining and oil industries was sufficiently intense to induce Mitchell Sharp to announce to the House of Commons on May 11, that, in the event that the three-year exemption were withdrawn, it would not apply to income earned before January 1, 1974. In the event that the exemption for prospectors and grubstakers should be withdrawn, he assured the House that it would not apply to amounts received before January 1, 1969 related to properties acquired before January 1, 1968.[365] Immediately, Noranda reversed its stand, announcing that one of the two mines would be opened as originally planned,[366] and the price of Noranda's shares shot up $1.75 to $53.75.[367]

Many mining industry spokesmen were not satisfied with Sharp's announcement. Thomas Elliott, Manager of the B.C. and Yukon Chamber of Mines complained that the uncertainly regarding the exemption had only been removed for three or four years. Companies "should be looking 10, 15, or 20 years ahead, not forced to make decisions based on what may happen three or four years from now."[368] He also said he was concerned that a rush by mining companies to take advantage of the assurance of the exemption might create inflationary pressures in the industry. However a Globe and Mail survey of companies "with important holdings in the region" indicated that Sharp's statement had had "little effect", either because their production plans were already too far advanced, or "the basic atmosphere of uncertainty created by the report continues to be the dominating factor."[369] This uncertainty was attributed to the failure of Sharp to give any assurances about the 30 per cent depletion allowance.[370]

At a meeting of the Federal-Provincial Tax Structure Committee on June 13th, Sharp, accompanied by Edgar Benson, Forestry Minister, Maurice Sauvé, and Minister Without Portfolio, Jean Chrétien, explained the Carter proposals and heard the comments of the provincial representatives.[371] Ross Thatcher, who, in addition to being Premier, was Saskatchewan's Provincial Treasurer, said he would be "happy to see the whole Carter Report scrapped."[372] He added that several of the twelve new potash mines which were "ready to open in Saskatchewan within the next five years" would not proceed unless the mining incentives were maintained.[373] Ontario's Provincial Treasurer, Charles MacNaughton, demanded that tax reform be linked to a new tax-sharing arrangement, something Sharp was unwilling to accept.[374]

At a meeting of the Prairie Economic Council in Winnipeg on June 22nd, Thatcher was joined in his opposition to the Carter Report by Premiers Duff Roblin of Manitoba and E.C. Manning of Alberta.[375] At a press conference, the three premiers released the contents of a joint telegram sent to Mitchell Sharp, calling for a delay in the implementation of any of the Carter proposals until "a full-scale research program" had assessed their economic and social impacts. The telegram listed six basic objections:

- Concentration of fiscal and economic control in the hands of the federal Government to the 'extent that regional development may be circumscribed';

- The possibility of adverse effects on provincial tax revenues and equalization payments;

23 were generally opposed, and the remainder were either divided in their views or not explicit regarding their overall assessment of the Report.

The Canadian tax professionals in private practice were still opposed to the Report: Of 23 practitioners, 10 spoke against major recommendations, 3 spoke in favour, with the remainder mixed or indeterminate. Of ten business executives and tax professionals employed by business corporations and organizations, nine opposed major recommendations, and only 2 supported the Report. These pro-Carter "business" spokesmen were Lawrence E. Coward, Vice-President and Director of William M. Mercer Ltd., securities dealers in Montreal, who supported the proposals for taxing insurance companies,[387] and J. Harvey Perry, who had returned to his position as Executive Director of the Canadian Bankers' Association.

For Perry and others present who had been connected with the Commission, or who sympathized with its objectives and proposals, it was an opportunity for a counter-attack against what many of them regarded as unreasoning but orchestrated attacks on the Report.[388] Perry was the opening speaker at the conference session, "Anatomy of a tax system", and directed attention toward the critics of the Report. He attributed the opposition to the Carter Report to the general lack of familiarity with the task of analyzing a tax structure in depth, and also to the fact "...that is largely the views of the business community that have been expressed." Businessmen, Perry explained, possessed an "extreme tax-consciousness", whereas wage-earners and

- The 'grave consequences' to both regional and national economies through dismantling of tax incentives on resource development;

- The adverse effect which estate and capital gains tax proposals in the report would have on individuals, farms and businesses;

- The implications [of] the report pertaining to foreign capital investment.[376]

Responding to a question from Conservative MP for Ontario, Michael Starr, Lester Pearson told the House of Commons the following day that there was "no ground" for the premiers' fears that the federal government might act with "undue haste" in implementing the Report.[377]

Some provinces were beginning to apply pressure to the federal government on a broader front to get it to disown the Carter Report. Agriculture Minister J.J. Greene encountered criticism of the capital gains proposals, proposed changes in the method of calculating depreciation, and "forcing farmers" to report their earnings on an accrual rather than a cash basis.[378] The communique indicated that "the provincial agriculture ministers are concerned about three recommendations...", suggesting that the public opposition to the Report had spread beyond the Prairie provinces.[379] Ross Thatcher, however, continued to be the most vocal of the provincial opponents of the Report, denouncing it at business gatherings and providing material for news stories.[380]

The pressures on and from provincial governments mounted at the

annual conference of the provincial ministers of mines. Delegates included representatives from all provincial governments except Prince Edward Island, and also of mining associations and companies. According to the Globe and Mail, in camera discussions gave priority to the Carter proposals to tax capital gains and to remove existing incentives to the mining industry.[381] C.E. White of Toronto, Senior Vice-President of Canadian Bechtel, urged the ministers "to pack off the report to oblivion", warning them that, if the Carter recommendations on mining were implemented, mining would "cease to be Canada's fastest growing industry, and to maintain its enviable export record."[382] He hoped that other provincial spokesmen would be as "forthright" in their criticism of the Report as Premier Thatcher, and warned that the supply of minerals was similar to that of food: "There's not going to be enough minerals to go around".[383] V.C. Wansbrough, Vice-President and managing director of the Mining Association of Canada presented the major points in the Association's brief attacking the Report to the provincial ministers. According to the Globe and Mail's account of the meeting, the provincial representatives were "impressed" with Wansbrough's warning that, "if concessions were dropped capital for investment in mining would not remain in Canada but go elsewhere."[384] No unified position opposed to the Carter recommendations emerged from the meeting, however, as Eastern representatives were more "noncommittal".[385]

The November 1967 Tax Conference:

The Tax Foundation hosted a second Conference on the Report, November 18-20, at the Royal York Hotel in Toronto, with the aim of further discussions on the Report. By this time it was clear that the tide of business and professional opinion was strongly against the Carter Report.

R.W. Manning, F.C.A., President of the Canadian Institute of Chartered Accountants welcomed the conference participants with a reminder of the substantial influence of their activities on tax policy formation:

> ...I am sure that one document that has received a lot of study by Mr. Sharp's staff is our April Conference Report. I am just as certain they will be more interested in what is said and reported at these sessions....
> After a period of praise, appraisal and re-appraisal, the time has come for suggesting alternatives -- not only, of course, to the Commission's proposals, but also to the present tax system. It is important to recognize that this Conference is very likely the last opportunity for a distillation of the views of our leaders in accountancy, law, economics and business before the government takes an official position, from which it may not readily move.[386]

The Foundation had made a greater effort to balance the list of speakers with specialists known to favour the comprehensive tax base. Included were J. Harvey Perry and twelve former staff members and consultants to the Carter Commission, making the November Conference more evenly divided than the one in April on the overall merits of the Report. Of 61 speakers, 25 spoke in favour of major recommendations,

23 were generally opposed, and the remainder were either divided in their views or not explicit regarding their overall assessment of the Report.

The Canadian tax professionals in private practice were still opposed to the Report: Of 23 practitioners, 10 spoke against major recommendations, 3 spoke in favour, with the remainder mixed or indeterminate. Of ten business executives and tax professionals employed by business corporations and organizations, nine opposed major recommendations, and only 2 supported the Report. These pro-Carter "business" spokesmen were Lawrence E. Coward, Vice-President and Director of William M. Mercer Ltd., securities dealers in Montreal, who supported the proposals for taxing insurance companies,[387] and J. Harvey Perry, who had returned to his position as Executive Director of the Canadian Bankers' Association.

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consumers who bore a greater tax burden had been "largely silent",[389] What Perry found unacceptable was

> ...an undertone of unwillingness to accept the need for any change at all.... There are forces at work here -- both economic and sociological -- that I have personally found most disturbing. As a result of some of my gloomier reflections I have indeed come to be more concerned about the future of my country than about the future of the Report.[390]

One of the later speakers in the same session was Philip Vineberg, past-Chairman of the Foundation, whose explanation for the opposition looked more to the Report itself and to its authors:

> In the entire history of Royal Commission Reports, none has evoked more constant, almost universally hostile reaction than that of the Royal Commission on Taxation. This seems to be accompanied by a conviction... that the main principles of the Report will not be implemented. If one has to search for a consensus of what has been proven by the appointment of a Royal Commission to reform the tax system, the only thing on which most of us could agree is that you can't reform the taxation system by appointing a Royal Commission for the purpose.[391]

After noting the Commissioners' claims that the majority of taxpayers would pay less under the reformed system, that governments had in the past shown a tendency to overtax, and pointing out the advantages of the Commission's integration proposal and its 50 per cent top marginal rate, Vineberg asked why the Report had not been widely acclaimed:

> It is perhaps a facile assumption to make, and the assertion was made about an hour ago, [by Perry] that all the complaints, or a major portion of them, are to be attributed to the fact that they trespass on vested interests long established. Everyone, of course, is in favour of that part of the Report which taxes somebody

> else and nobody is in favour of that particular part of the Report, damnable that it is, which proposes to tax him. No doubt this equally applies to accountants and lawyers. Their vested interests, though seldom expressed, relate to a vast accumulation of knowledge of the existing system, which represents a hard-won capital accumulation over a lifetime and which this cold blooded Report proposes to demolish without a vestige of capital cost obsolescence factor. This explains part of the reaction. However, many of the adverse briefs have been impressive by any standards. While not always objective, it may be noted that in many instances those who might have had an economic interest in favouring integration have nonetheless indicated their hostility to it as well as to other features.[392]

Vineberg attributed the widespread negative reaction to a wide range of factors: "poor salesmanship" on the part of its defenders in failing to lure the provincial governments with prospects of "vast vistas of taxation which even their most rapacious Ministers of Revenue [had] never previously envisaged"; "widespread disagreement with the economic theory of Henry Simons" (which he compared in vintage to that of Karl Marx); Carter's logic, which, though called French, lacked "the French admixture of love, warmth, and human understanding"; the Report's "preoccupation with inessentials"; the fact that people based their expectations on their future tax positions rather than their present positions, resulting in the Report arousing the anger, not only of the rich, but also all who hoped to be; the Report's lack of consistency with its own principles of neutrality and equity; and resistence to ideas which are unfamiliar "when the path from the present is not clearly laid out".

As at the April Conference, the comprehensive tax base was severely mauled by many speakers. Professor Boris I. Bittker of the

Yale Law School, and a published opponent of the comprehensive tax base, (CTB)[393] pointed out some inconsistencies in the application of the principle in the Report:

> This is only illustrative of the fact that the Carter Report entertains and accepts so many arguments, aside from the CTB principle, for including or excluding specific categories of income that its readers can hardly be blamed if they offer the same or comparable arguments for drawing a very different line. Between the CTB banner and those who are asked to follow it, there is too large a credibility gap to evoke unquestioning loyalty. In the end, therefore, the acceptability of the Report's recommendations must rest on a complex of political, social, and economic judgments, not on any claim of consistency in achieving a CTB.[394]

Harvey E. Brazer of Department of Economics at the University of Michigan, sharply disagreed with Bittker's appraisal, arguing that, if implemented, it would

> ...produce for Canada a tax system which, evaluated in terms of the commonly accepted goals of taxation, would be superior to that of any other major nation in the world. If the Commission's Report is to be attacked in its particulars, that attack should focus on its sins of omission; it is to be faulted, in my view, because it did not go quite far enough in pursuit of the policies demanded by its own principles and precepts.[395]

Brazer, of course, was not a recent convert to the comprehensive tax base. He had played a role in introducing Carter to the idea when the latter was in Washington, and had encouraged Douglas Hartle and the Commission's research staff in their work on capital gains.[396]

Edgar Benson, then Minister of National Revenue and President of the Treasury Board, was the banquet speaker for the November Conference, symbolically closing the initial period of public discussion of the Report, which had opened with Mitchell Sharp's

address on the same topic at the banquet of the April Conference.[397] Aware that many of his listeners had participated in the writing of many of the submissions to the Minister of Finance, Benson took the opportunity to thank them for the briefs and letters which had been "helpful to us in our study of the Commission's Report."[398] Borrowing a phrase from Shakespeare, Benson commented that the authors of the 950-odd submissions had "come to bury the Report, not to praise it."[399]

Benson observed that one of the common themes among the submissions was the argument over the weight and meaning which ought to be given to the "equity" objective. Although he expressed a measure of skepticism with regard to the motivations behind some of the arguments, Benson did take seriously the point frequently made, that "sudden and sweeping change" could have an "inequitable" effect on taxpayers who had planned their affairs under the old tax regime. While acknowledging that "stability is important if individuals and businesses are to plan their affairs sensibly", he pointed out that the need for stability had to be balanced against demands for change arising from the steady erosion of the tax system by talented tax practitioners, and the competing "economic and social goals pressed on us by taxpayers this year."[400]

The second common theme of the briefs related to the difficulties that would result from having a tax system that was "radically different from that of the United States and of other countries with which our economy is inextricably linked."[401] While countering that

even the existing tax system was "different" from Canada's trading partners, he conceded that:

> ...it is true that the proposals of the Royal Commission would give us a system which might be more difficult to reconcile with that of our trading partners than is the existing system.[402]

Benson praised the Commissioners and their staff "for their thorough investigation and analysis of every nook and cranny of our tax system, and for their conscientious effort to give us objective standards by which to judge it".[403] He gave no indication of the government's thinking, beyond saying that it would not implement all the recommendations ("...nobody could be that right"), but that the reformed system would almost certainly "be closer to the system proposed by the Royal Commission" that it was at the time.[404]

Next, Benson announced, would come the views of the provincial governments, and after that the government would "make public a White Paper which [would] set out the general outline of its proposals for tax reform."[405]

Tax Reform on Hold -- The November 1967 Budget:

In his budget speech of November 30, 1967,[406] Sharp referred to "the work we have done within the government", to the representations received, and predicted that the ultimate reform legislation, while being "influenced by the monumental report of the royal commission,...[would] be more in the nature of reforms of the existing

tax structure rather than the adoption of a radically different approach."[407] The "sweeping extent" of the Carter proposals, made it difficult to predict the effects of "sudden changes of this magnitude". He alleged that

> ...the Commission did not give adequate weight to the fact that Canada will need to generate and invest a large volume of savings over the next decade and substantial amounts of foreign capital will be required to supplement Canadian savings.[408]

In an implied reference to the campaign against the Commission's proposals affecting the mining and petroleum industries, Sharp said the recommendations "had caused widespread concern" about their "regional impact".[409] He said that the system recommended by the Commission was "quite different" from that of other countries, particularly that of the United States, with which Canada had an integrated capital market, and "could give rise to economic difficulties, as well as to technical problems in drafting an effective law."[410]

Carter made a statement in rebuttal to Sharp's comments, pointing out that the Commission's proposals would actually move the tax system to a position somewhat nearer the American system that it was at that time.[411] However, the government had been persuaded by the critics of the Report and had rejected the comprehensive tax base and the full integration of personal and corporate income. While denying that he had "killed the Carter report, Sharp explained that the government's decision to base its reforms on the existing system "meant more work for Finance officials, requiring more time before a White Paper

outlines preliminary proposals for reform."[412] The existing target of January or February of 1968 would therefore have to be set back, though Sharp did not suggest a new date.[413]

The Liberal Leadership Race:

It had been rumoured since May that Lester Pearson would probably resign at the end of Centennial year, and on December 12th, he formally announced his intention to step down. As one Cabinet minister after another, including Sharp, declared his candidacy, the issue of tax reform, and a good deal of other government business, was neglected for the politics of the Liberal leadership contest, and after that, for the June, 1968 election.

Tax reform was not a significant issue during the Liberal leadership race. A small group of left-Liberal cabinet ministers, including Edgar Benson, Walter Gordon, Jean Marchand, Larry Pennell and Pierre Trudeau, met at the Circle Universitaire on Laurier Avenue in Ottawa to decide who should run for the Party leadership. Ideology and policy were only indirectly significant in the group's consideration of the electoral chances of each potential leader, not so much in respect to the leader's anticipated influence on policy, but more in terms of their estimated effect on the party's electoral fortunes. They needed someone who could defeat Stanfield, who was ahead in the polls, and it was agreed that Winters, Martin or Turner could not do that.[414] While Trudeau was prepared to support

Marchand, the former CNTU leader thought that his labour union background would hurt Liberal support with business. Furthermore, Marchand argued, Trudeau was more articulate in English, and "smarter".[415]

While discussing a possible candidate for the Liberal leadership, each member of the group knew he was also probably picking his own cabinet portfolio. The defeat of Mitchell Sharp's mini-budget measures in the House Committee while he was acting Prime Minister in Pearson's absence, made it awkward for him to continue in the Finance portfolio. While Benson had considered leaving the Cabinet at that time, Trudeau said that he would not run for the leadership unless Benson stayed. As the current Minister of National Revenue, and a professional chartered accountant, Benson seemed the natural choice for Finance.

Tax reform or the Carter Report were not mentioned by any of the leadership candidates during the campaign. Afraid of dividing the Party, they invoked cabinet solidarity as an excuse for avoiding confrontations over policy.[416] However, Pierre Trudeau's leadership convention victory over Robert Winters, who was generally perceived to be the pro-business candidate, encouraged widespread expectations of a more reformist government, in tune with Trudeau's leadership campaign theme of the "just society". Moderating that expectation somewhat was the early support which Mitchell Sharp gave Trudeau when the Finance Minister ended his own candidacy on the eve of the convention, and the added support of C.M. Drury, who had favoured Sharp.

The leadership race contributed another significant actor to the tax reform debate: Eric Kierans, former Minister of Revenue and then Minister of Health in Premier Lesage's Quebec government, and past-President of the Quebec Liberal Federation, whose concentration on issues had made a favourable impression on many of the convention delegates.[417] Kierans was elected in the Montreal constituency of Duvernay in the general election of June 25th and appointed Postmaster General on July 6th.

Tax Reform and the June 1968 Election:

Of the four national parties which had held seats in the previous Parliament, only the New Democratic Party promised to implement the Carter Report, while the Conservatives opposed any tax on capital gains.[418] There was no groundswell of support for the implementation of the Carter Report and little attention was given by the media to the tax reform issue. The coverage of the speeches of both Trudeau and Stanfield during the final three weeks of the campaign in the the Globe and Mail did not contain a single reference to the Carter Report. One heckler, Donald Mitchell, Vice-President of the Canadian Union of Students shouted through a megaphone, "What about the Carter report?", and was promptly attacked by Conservative Party supporters and hauled from the meeting by police.[419] T.C. Douglas frequently mentioned the N.D.P.'s support for the Carter proposals, and on the final day of the campaign, made news with the

charge that certain industries, including the auto industry, Time, Readers' Digest, the mining industry, banks and insurance companies, were "getting tax favours in exchange for campaign funds."[420]

While Trudeau often spoke of the "just society", it was usually in non-economic terms. When he referred to the distribution of wealth as being unjust or unfair, it was always in regional or international terms. Given the tenor of the campaign activities and rhetoric, the Liberals fought and won the election more on "Trudeaumania", and Trudeau's estimated ability to deal effectively with Quebec's demands for more provincial power, than on anything to do with tax policy or even economic policy. The results of the voting on June 25th could not have been interpreted as a mandate to do anything in the way of tax policy.

However, the election did give Trudeau and his new government a majority of support in the House of Commons, something that had always eluded Lester Pearson. Walter Gordon had repeatedly warned Pearson about the hazards of trying to deal with the Carter Report as a minority government.[421] While the reaction to the published Report bore out Gordon's caution to the full, the Trudeau government was finally in a secure enough position in the House of Commons to take a stand on tax reform.

Conclusion

Mitchell Sharp's announcement during his November budget speech that any reforms would be more a revision of the existing system than a reform based on the Carter Report, signaled an important but interim victory for the opponents of the comprehensive tax base. Shortly after the release of the Report, opinion among tax professionals and businessmen was divided and uncertain, and this was reflected in the newspaper coverage during the first week after publication of the Report. The most frequently expressed opinion on the capital gains proposals was that they were somewhat distasteful but inevitable. Almost as often, the proposals were hailed as essential to an equitable and efficient tax system. Only the petroleum and mining industries seemed united against the Report.

The April Conference of the Canadian Tax Foundation showed for the first time the strength of the opposition to the Report among nearly all tax professionals and businessmen. The critical opinions expressed at the conference were prominently reported, indicating that the Carter proposals were not logically inevitable, that they were more dangerous to business interests than many had first thought, and that the Carter package could be beaten by strong and vocal opposition. The mining and petroleum companies led the way in the campaign, predicting losses of investment capital to activities abroad, and parading the cancellation of investment plans. This widened the front of opposition to prospectors, suppliers, mining municipalities, provincial governments, western Members of Parliament,

and banks looking forward to the opportunity of financing expanded operations.[422] The other sectors also had their own reasons for opposing the Carter recommendations but they were all agreed on their opposition to what they claimed was a radical blueprint for a stronger, more centralized, better-financed, interventionist and egalitarian state. Their common argument was that private capital was less mobile between industrial sectors within Canada than it was across international frontiers. If Canadian governments were to tax private capital more heavily than other jurisdictions, then capital, followed by jobs and trained people, would simply flow to the more favourable tax climate.

The tax professionals, after demonstrating their nearly united opposition to the major Carter proposals at the April Conference acted as resource persons at business conferences and meetings during the summer and fall, lending information, sophistication and credibility to the growing opposition. While there is no published information to positively and systematically link the tax professionals to the more than 900 briefs which descended on Mitchell Sharp, it was widely assumed by the actors in the debate that most were either written by tax professionals or with their advice.[423] Some of the larger corporations had tax specialists on their staffs; many lawyers and chartered accountants had, in effect, advertized their opinions and abilities at the April Conference, the proceedings of which were reported in the papers read by businessmen who were aware that their advice was available for hire.

Strong as the opposition was, it was not united on its objectives or tactics. Ignoring differences on other recommendations, the critics of the Report could be divided into those who were opposed to the inclusion of capital gains on principle, and those who were prepared to accept a reduced tax on capital gains with some reduced compensation for the "double taxation" of corporate income. Pat Thorsteinsson was of the latter group, which was prepared to settle for a compromise on capital gains and corporate-source income. Many adherents of the former position who were knowledgeable in tax matters may have been arguing their case partly out of tactical considerations: that it was wiser to express complete opposition to the proposals in order to be certain to end up in no worse a position than the compromise proposed by Thorsteinsson. Variations of such a compromise were proposed in the minority reports of Beauvais and Grant, by the Canadian Bar Association and the Canadian Institute of Chartered Accountants, and by such prestigeous opinion-makers in the tax community as R.M. Sedgwick, George Tamaki and Heward Stikeman. Tax professionals knew that those capital gains currently subject to tax were assessed at full marginal rates, that is, at rates usually substantially higher than would have been the case under the Carter system, and with no advantages of integration or averaging. They also knew that the Department of National Revenue was becoming more aggressive in assessing income which had once passed for capital gain and was winning its cases in court.

Tactical considerations were also evident in the almost general business opposition to the full integration of personal and corporate

taxes. In spite of the clear benefits to middle-income shareholders, it was understood that the scheme was part and parcel of the full taxation of capital gains. The influence of the tax professionals can be seen here, in that most business spokesmen departed from their long-standing opposition to what they had called the "double taxation of corporate income" in order to avert the threat of the full taxation of capital gains.

The Conservative Party had adopted the more intransigent position of opposing any tax on capital gains, a position urged by Eldon Wolliams at the party convention over the objections of tax professionals like Sheldon Silver, Gerald Townsend and economist, Robert Clark.[424] With the NDP defending the comprehensive tax base, the Conservatives opposing any tax on capital gains and many other Carter proposals, the natural niche for the Liberals, given the spectrum of business and professional opinion, was something which could be presented as a compromise position.

By the end of 1967 there was a widespread feeling in tax and business circles that the critics of the comprehensive tax base had made their point. Sharp's announcement on tax reform during his November, 1967 budget speech was an admission of this, and an acknowledgement that his Department would have to go back to the drawing board.

Notes to Chapter VI

1. "Memorandum to Mr. Pearson on election possibilities", in Gordon, A Political Memoir, pp. 353-355.
2. Ibid., p. 353.
3. Ibid.
4. Ibid., p. 221.
5. Ibid., p. 222.
6. Gordon, p. 177.
7. Ibid., pp. 220, 225, 232. In correspondence with the author, Sept. 16, 1982, Gordon noted that, had not Pearson publicly agreed that he would remain in Finance, he would not have stood for re-election.
8. Directory of Directors, (Toronto: The Financial Post, 1965).
9. Gordon, p. 177.
10. Interview with the Hon. Edgar Benson, Aug. 24, 1982. Cabinet approval of the White Paper strategy must have come after Sharp's remarks in the House (see below) in favour of introducing a draft bill, and before his announcement at the April Conference of the Canadian Tax Foundation that the Government would publish a White Paper. According to Doerr, p. 122, citing a "confidential source, PCO", a Special Cabinet Committee to study the Report was established around this time, its membership including the Prime Minister, the Minister of Finance, The Minister of National Revenue, the President of the Treasury Board, as well as "ten or more other ministers" sitting in the Committee from time to time. However, Mr. Benson, Minister of National Revenue at that time, had no recollection of such a committee. Benson interview. Nor did Walter Gordon, in correspondance with the author, Sept, 16, 1982. Gordon surmised that he was not a member of Cabinet at that time, though he was appointed Minister without Portfolio on January 9, 1967, about a month following the submission of the Report to the Government.
11. Doerr, p. 127; Benson interview.
12. Department of Finance, News Release 67-4, Jan. 9, 1967.
13. House of Commons Debates, Feb. 24, 1967, p. 13497.
14. House of Commons Debates, Feb. 27, 1967, p. 13497; Quoted in Goldenberg, p. 33.
15. E.H. Smith interview.
16. "Bennett to File", Feb. 25, 1964, RG33/65, Vol. 108, "Memoranda to Prof. Hartle from Staff" file. Bennett to Bryce, May 5, 1964, Vol. 143, File 80-5. See above, Ch. 4, pp. 215-219, 231-234.
17. "Sending Draft Chapters to Mr. J. Brown, Department of Finance", Bennett to Harry Wilson, May 6, 1965, RG33/65, Vol. 143, File 80-5.
18. Audrey D. Doerr, The Role of White Papers in the Policy-Making Process: the Experience of the Government of Canada, (Ottawa, Carleton University, Ph.D. dissertation, 1973), p. 125.
19. House of Commons Debates, October 22, 1969, p. 11690; cited in Doerr, p. 132.
20. Doerr, p. 126.
21. Department of Finance, News Release 67-44, Mar. 22, 1967.
22. Conway interview.

23. Vancouver Sun, Feb. 25, 1967.
24. La Press (Montreal), Feb. 25, 1967.
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26. Calgary Herald, Feb. 25, 1967.
27. The Globe and Mail (Toronto), Feb. 25, 1967.
28. The Spectator (Hamilton), Feb. 25, 1967.
29. The Globe and Mail (Toronto), Feb. 27, 1967.
30. Ibid.
31. The Telegram (Toronto), Feb. 27, 1967.
32. Ibid., Feb. 27, 1967.
33. "The 'buck is a buck' backlash", Toronto Star, Feb. 27, 1967.
34. The Ottawa Citizen, Feb. 25, 1967. All press sources during the first week cited here are taken from the Carter Commission's file of press clippings, PAC, RG33/65, Vol. 152.
35. "Canada singular Western haven for those 'Scot-free capital gains", Ottawa Citizen, Feb. 28, 1967.
36. "It's Your Business", Montreal Gazette, Feb. 27, 1967.
37. "Correcting the Imbalances in Present Tax Structure", Montreal Gazette, Feb. 28, 1967.
38. Ibid.
39. "As We See It -- Musical Chairs with Taxation", Windsor Star, Feb. 25, 1967.
40. The Telegram (Toronto), Feb. 28, 1967.
41. The Globe and Mail (Toronto), Feb. 28, 1967.
42. Ibid., Mar. 1, 1967.
43. Vancouver Sun, Feb. 27, 1967.
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45. "Sleepless nights for politicians", Winnipeg Tribune, Feb. 27, 1967.
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47. "Our 'Old Women': Roadblocks to Change", Toronto Star, Feb. 28, 1967.
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49. Toronto Star, Feb. 25, 1967.
50. Ibid., Mar. 1, 1967.
51. Ibid., Feb. 28, 1967.
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53. The Financial Times, (Toronto), Feb. 27, 1967.
54. Montreal Star, Feb. 27, 1967.
55. The Spectator (Hamilton), Feb. 27, 1967.
56. St. John's Telegram, Feb. 28, 1967.
57. Le Devoir (Montreal), Feb. 27, 1967.
58. L'Evénement (Quebec), Feb. 28, 1967.
59. Le Nouvelliste, Trois Rivières, Feb. 27 and 28, 1967.
60. Montréal Matin, Lucien Langlois, Feb. 28, 1967.
61. L'Action, (Quebec), Feb. 28, 1967.
62. Montréal Matin, Feb. 25, 1967.
63. La Press (Montreal), Feb. 27, 1967.
64. Ibid.
65. Montreal Gazette, Feb. 27, 1967.
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133. The Telegram (Toronto); Toronto Star; The Vancouver Sun; The Montreal Star, Feb. 27, 1967; also reported in Montreal Matin, Feb. 28, 1967.
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173. Ibid., Feb. 27, 1967.
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180. "DesBrisay Sees Most Equitable System", Fredericton Gleaner, Feb. 25, 1967.
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183. "Pas de cession de nos prérogatives (Johnson)", Le Soleil (Quebec), Feb. 28, 1967.
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195. Jack Cahill, "Ontario still wants more", Toronto Star, Feb. 27, 1967.
196. The Telegram (Toronto), Feb. 27, 1967; Toronto Star, Feb. 27, 1967.

197. "Other provinces on Carter", Toronto Star, Feb. 27, 1967.
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201. "Bennett, Cabinet Silent on Commission Proposals", Vancouer Province Feb. 25, 1967.
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207. Ibid.
208. See Ch. 2, above, pp. 86-87.
209. Report of the Nineteenth Tax Conference, p. 6. He also delivered the Fourth Henry Simons Lecture at the Law School of the University of Chicago, which was published in the Journal of Law and Economics as "Canadian Tax Reform and Henry Simons", Volume XI, (Oct., 1968).
210. Report of an interview with Carter on Toronto radio station CFRB, The Globe and Mail (Toronto), Feb. 27, 1967.
211. Perry interview, Oct. 23, 1981.
212. See below, pp. 478-479.
213. Hartle, Perry, and Conway interviews.
214. Conway interview.
215. The original date for the special conference had been Nov. 8th-10th, 1965, and was postponed at least four times. Canadian Tax Journal, Vol. 13, No. 4 (July-Aug., 1965), p. 267; No.5 (Sept.-Oct., 1965) p. 349; No. 6 (Nov.-Dec., 1965), p. 460; Vol. 14, No. 1 (Jan.-Feb., 1966), p. 6; No. 4 (July-Aug., 1966), p. 315; No. 5 (Sept.-Oct., 1966), p. 401; No. 6 (Nov.-Dec., 1966), pp.479-481.
216. A registration list, and a biographical list of speakers is included at the back of each Conference Report.
217. Report of the Nineteenth Tax Conference, p. 40.
218. Ibid., p. 435.
219. Carter, Report of the Nineteenth Tax Conference, p. 3.
220. Ibid., p. 3.
221. Ibid.
222. Ibid., p. 5.
223. Ibid., p. 190.
224. Ibid., p. 194.
225. See Ch. 4, above, pp. 201-202.
226. Report of the Nineteenth Tax Conference, p. 194.
227. Ibid., p. 210.
228. Ibid., p. 229.
229. Ibid., p. 168.
230. Ibid., p. 278.
231. Ibid., p. 278.
232. Ibid., p. 348.

233. Ibid., pp. 352-353.
234. See Ch. 4, above, pp. 266-267.
235. Report of the Nineteenth Tax Conference, p. 357.
236. Ibid., p. 359.
237. Report of the Nineteenth Tax Conference, p. 378. (Marler's emphasis).
238. Quoted by Marler, Ibid., p. 379. Marler was referring to Vol. 4, p. 202. See Ch. 5, above, p. 305.
239. Report of the Nineteenth Tax Conference, pp. 379-380.
240. Chapter 38, Vol. 6, pp. 187-217.
241. Report of the Nineteenth Tax Conference, p. 391.
242. Ibid., p. 436.
243. Ibid., pp. 453-454.
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245. Ibid., p. 454.
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248. See above, pp. 411-412.
249. Report of the Nineteenth Tax Conference, pp. 460-463.
250. Ibid., p. 464.
251. The Globe and Mail (Toronto), April 26, 1967.
252. Ibid., April 26, 1967, p. B4.
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281. "Lawyers would amend family unit concept", Ibid. Oct. 11, 1967
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294. The Globe and Mail (Toronto), May 4, 1967
295. Fraser Robertson, "Looking into business", The Globe and Mail (Toronto), Aug. 21, 1967.
296. "Capital gains tax denounced as 'detriment to democracy', The Globe and Mail (Toronto), Sept. 6, 1967.
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302. "CMA assails gains tax proposal", The Globe and Mail (Toronto), Oct. 5, 1967.
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323. "Insurance head assails authors of Carter report", The Globe and Mail (Toronto), July 26, 1967.
324. "Carter tax proposals unsound, mining association tell Sharp", The Globe and Mail (Toronto), Sept. 12, 1967.
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327. "IDA fears tax move may upset securities", The Globe and Mail (Toronto), Oct. 4, 1967.
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339. "Revisions urged", The Globe and Mail (Toronto), Nov. 9, 1967.
340. "Uncertainties feared capital deterrent", The Globe and Mail (Toronto), Nov. 16, 1967.
341. "Most Carter proposals endorsed by CLC", The Globe and Mail (Toronto), Nov. 16, 1967.
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345. Content analysis and tabulations were carried out by one of Professor Gillespie's students, Hal Berndt, in an unpublished paper, "What the Devil's Going on Up There, Anyhow?", (Carleton University, n.d.). Although the content of the remaining two briefs may not have been sufficiently clear, reports in the Globe and Mail indicated that the two organizations, Anthes Imperial, (a manufacturing conglomerate and not a petroleum company) and the Independent Petroleum Association were also opposed to the recommendations.
346. Berndt, "Insurance" and "Financial" tables.
347. Ibid., "Transportation", "Manufacturing/Industry", "Service" tables. Two labour unions, two medical associations, and two non-profit organizations were removed from this sub-sample on the grounds that they did not properly belong within those business sectors.

348. Ibid., "Manufacturing/Industry" table.
349. See above, pp. 401-409.
350. Berndt, "Service" table.
351. The total of all percentages adds to more than 100 due to signed columns and articles which reported the statements of others.
352. The Globe and Mail (Toronto), April 29, 1967.
353. Ibid., May 12, 1967.
354. "Conwest says Carter proposals could mean exploration halt", The Globe and Mail (Toronto), June 12, 1967.
355. "Algoma may halt its ore program if taxes changed", The Globe and Mail (Toronto), Sept. 28, 1967.
356. "B-A submits brief", The Globe and Mail (Toronto), Oct. 28, 1967.
357. "Carter threatens $1 billion outlay: Stelco", The Globe and Mail (Toronto), Nov. 17, 1967.
358. "Fears of tax effects on tar sands cited", The Globe and Mail (Toronto), Nov. 24, 1967.
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361. "Statement by Sharp to allay mine fears is expected shortly", The Globe and Mail (Toronto), May 2, 1967; Bucovetsky, p. 95.
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364. Bucovetsky, p. 95.
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377. "Won't hurry Carter plan, Pearson says", The Globe and Mail (Toronto), June 24, 1967.
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417. The Globe and Mail (Toronto), April 6, 1967.
418. D. Owen Carrigan, Canadian Party Platforms, 1867-1968 (Toronto: 1968).
419. "Student heckler pummelled, thrown out", The Globe and Mail (Toronto), June 18, 1967.
420. Ibid., June 24, 1967.
421. See above, p. 373.

422. The Toronto-Dominion bank was to provide $21 million toward the development of an open-pit mine in the Yukon, which, according to Anvil's President, Kenneth Liever, "would not have been warranted" under the tax regime proposed in the Carter Report. "Anvil Mining reverses view on effects of Carter report", The Globe and Mail (Toronto), Sept. 6, 1967. As Bucovetsky points out, Lieber was over-ruling an earlier statement by his Vice-President, R.V. Markham, who had said that Mr. Sharp's announcement of the extension of the 3-year tax holiday for new mines was not a factor in the company's decision.

423. Perry, Hartle, Conway, Huggett interviews. Benson's remarks at the November Tax Conference suggest that he also was under this impression.

424. "Carter formula rejected -- PC group in favor of capital gains tax", The Globe and Mail (Toronto), Aug. 11, 1967; "'The next election may well be lost on the Carter report' -- Capital gains tax denounced as 'detriment to democracy'", The Globe and Mail (Toronto), Sept. 6, 1967.

Chapter VII: The White Paper Debate

Introduction

The last two Pearson governments had feared the political consequences of taking action on the Carter Report. Accepting the basic elements of the "Carter package" -- the comprehensive tax base and its accompanying off-setting features -- would have sacrificed the Liberal Party's support among the business community. On the other hand, openly repudiating the proposals would have damaged the Party's reformist image and risked losing voters to the NDP. Although two successive Finance Ministers, Walter Gordon and Mitchell Sharp, differed on how the dilemma should be resolved, both were acutely aware of the political hazards they faced. The government could not easily have made concessions from the position defended in the Report, as the Report itself had already anticipated, considered and refuted most objections, thereby handing potent ammunition to potential defenders of the Carter plan for tax reform.

The White Paper, while being about as controversial as the Carter Report it was intended to displace, lacked the logical coherence of the Report and did not divide the country as neatly or clearly into potential winners and losers. It did propose solutions to the issues of equity, efficiency, neutrality and certainty raised in the Report, but presented them more as independent goals: each worthy in itself

and subject to being traded-off against other goals, depending on the value preferences of the electorate, or of those voters who were able to make their preferences count.

The White Paper debate was the crucible for testing the relative political capacities of the groups and interests who had already made their views known in the wake of the Carter Report. In putting forth mere proposals instead of legislation, and calling upon all interested citizens to participate in the discussion of those proposals, concessions to the more powerful interests could be legitimized as the government bowing to the wishes of the people, as interpreted by an independent parliamentary committee. The following account of the White Paper debate demonstrates how investment capital, as represented by corporate executives and assisted by the tax professionals, was able to dominate the participatory process and return the comprehensive tax base to the Economics texbooks from which it came.

Benson's approach to tax reform

Shortly after his appointment as Minister of Finance, Edgar Benson told reporters that he was in favour of by-passing the White Paper process and introducing a draft bill to Parliament:

> I'll have to discuss it with my colleagues, but I think we should decide what we want on Carter and present it to Parliament and see if they approve. A parliamentary committee would study the legislation and invite comment from the public and provincial governments.[1]

Benson believed that publication of a white paper would simply invite the same kinds of comments as had already been made: "I think it's time to decide to do something and do it."[2] He had, after all, criticized the Diefenbaker government in the House of Commons in 1962 for delaying tax reform by appointing a Royal Commission.[3]

The premiers of the Prairie provinces had been pressuring the federal government since June 1967 to go slow on tax reform, as had many businesses and their associations in their briefs to Mitchell Sharp. When Benson announced he would by-pass the white paper stage, he immediately aroused the concern and suspicion of business interests that he might try to force the Carter package through the House. A The Globe and Mail editorial the day following Benson's announcement voiced this suspicion:

> Would Mr. Benson buy the lot? If he would buy parts and not other parts, which parts?
> Implementation of the Carter Report would give Canadians a different country to the one they have known. Mr. Benson cannot expect us to buy such a possibility blind. He must state specifically where he stands on the Carter proposals.[4]

The editorial demanded that Benson state his position openly during an election campaign before introducing legislation, something the Liberals were careful not to do.[5] In September 1968, as Minister of Finance in the majority Liberal government, Mr. Benson confirmed his intention to introduce draft legislation early in the new year, and that the bill would be referred to a committee of the House.[6]

In the meantime, the government introduced what it considered to be more limited and self-contained reforms to the Estate and Gift taxes and to the taxation of insurance companies. In a sense, both the government and many taxpayers saw these changes as rehearsals for the major reform process still to come.

The Estate Tax amendments:

In his first budget speech, delivered on October 22, 1968, Mr. Benson introduced amendments to The Estate Tax Act which exempted completely gifts and bequests between spouses, increased the exemptions for children of the deceased, and increased the levy on transfers between all others sufficient to maintain the overall revenues from the Estate Tax.[7] Beyond the exemption for spouses and children and charitable donations, and a basic exemption of $20,000, the rates on the taxable residual of the estate were to range from 15 per cent, to a maximum of 50 per cent, to be applied at the taxable value of $300,000. The $10,000 exemptions for adult children, and the lack of complete exemption for dependent children, signaled the government's intention not to adopt the family tax unit recommended by the Carter Commission. In addition, the fact that the rate structure was to be based on the size of the estate, and was to be (once the exemption had been taken into account) lower than income tax rates, indicated that the comprehensive income concept had, in effect, been rejected. Mr. Benson pointed out the following February, during a

speech on second reading of an amended version of the bill, that the government had "...considered, but rejected, the recommendations of the Carter royal commission on taxation which would have doubled the revenue from taxation of inheritances".[8]

While it did not represent as fundamental a reform as that recommended in the Carter Report, this aspect of the budget nevertheless sparked a vigorous debate, analagous to that following publication of the Carter Report. Benson announced some modifications in his bill at the end of January 1969, which retreated slightly from the October budget. The major change was the restoration of the basic exemption of $50,000 available under the old Act, instead of a $20,000 basic exemption proposed the previous October. The modification was aimed at estates of $50,000 or less passing to other than spouses or children, and large estates would continue to be subject to the $20,000 basic exemption.[9] In addition, all those liable to tax would be allowed the option of paying in six annual instalments subject to carrying charges at an appropriate rate of interest.[10] To ensure that the transition would not disadvantage anyone, the Department of National Revenue would compute the liability during the transition period according to the rules favouring the estate.[11]

In refusing to go as far as some critics were demanding, and abolish the Estate Tax, Mr. Benson pointed to the fact that it raised over $200 million annually, revenue which would otherwise have to be found elsewhere.[12] He added that, as three-quarters of the tax was passed on to the provinces which had not vacated the field of estate

taxes and succession duties, "One should consider the provincial revenue requirements at this time before engaging in any wishful thinking about the total abolition of death taxes in Canada".[13]

Benson's second point in defence of his amendments to the Act concerned the principle of vertical equity. Confronting some of the more extreme critics of his proposals, Benson said that only about five per cent of Canadians ever paid estate tax and that more than half of revenues were collected from estates valued at over $500,000. The Estate Tax provided some assurance that the wealthy would, at some point, contribute their fair share to the support of the state:

> In Canada, where about seven million persons pay income tax, it is fair that the relatively few who have accumulated the greatest wealth should contribute at death to the common good of our country. They are usually the ones who have benefited most from the collective effort of Canadians to build a strong economic and political system.[14]

Linked to this was Benson's support of progressive taxation on the grounds of ability to pay:

> ...the estate tax is one of our two progressive taxes. I believe in progressive taxation because it puts the burden to pay on the people who can afford to pay.[15]

The Taxation of Insurance Companies:

Benson also introduced in his 1968 budget a revised method of taxing life insurance companies along lines more like those applied to other companies, by including the proceeds of policies in the

policy-holders' personal incomes. The investment income of companies would be taxed at a rate of 15 per cent, to represent a withholding tax to the policy-holder, who, on drawing out the proceeds of his policy, would receive a partial refund to bring the tax down to his marginal rate if the latter was below 15 per cent. However, no upward adjustment would be made for higher-income policy-holders.[16] This differed from the Carter recommendation of attributing the investment income to policy-holders and taxing it at the latter's personal rates, and conceded to the insurance company's objections that the Royal Commission's method would be an "administrative nightmare for policy-holders".[17]

These measures, which went some distance in implementing the detailed recommendations of the Carter Commission respecting the insurance industry, aroused vocal opposition from the insurance companies.[18] The Canadian Life Insurance Association, including top executives from nine major companies, appeared before the Senate Committee on Banking, Trade and Commerce to denounce what it considered a sudden and unjusitfied burden on the industry, and which would impair its ability to compete with other forms of saving.[19]

Following "intensive and helpful discussions ...with representatives of the industry",[20] Mr. Benson introduced modifications which, while retaining the principle of taxation of life insurance company earnings on the same basis as for other companies, softened somewhat the impact on the companies.[21] However, the government did not concede to the companies' demands that large,

before-tax contingency reserves were necessary for the protection of policy-holders.[22]

Mr. Benson and his Department had largely succeeded in their attempt to tax the business income of insurance companies on a basis comparable to that of other companies. However, as two observers of tax reform later noted, the opposition to and the technical complexities of the insurance amendments, (comparatively minor reforms compared to the scope of the Carter recommendations) "may have made the government somewhat cautious in designing its own tax reform package."[23] Robert Bryce confirmed that, although they had "won that battle" the intensity of the opposition to the insurance amendments gave the government a taste of what to expect when the White Paper was released.[24]

The Return to the White Paper Route:

In January 1969, Mr. Benson said that the introduction of a draft bill would be delayed.[25] At this time the Leader of the Opposition, Robert Stanfield, added his voice to those urging the government to produce a white paper rather than a draft bill.[26] Benson persisted with the draft bill strategy, but finally relented by the 6th of February, when Prime Minister Trudeau informed the House:

> ...if there is sufficient argument made strongly for a white paper the Minister of Finance has been telling me that he is prepared to consider the alternative if it appears more helpful to the House and the provinces.[27]

One account of the government's reversal of its position on the process of tax reform argues that this delay was the result of "intense pressure from organized interests and from the provinces against anything which might possibly be seen to discriminate against rapid economic growth...", and the divisions which this pressure produced within Cabinet.[28] A second account suggests that, in addition to political pressures in the direction of a white paper, Benson was also receiving similar advice from J.R. Brown, his Senior Tax Advisor, and other departmental officials, who argued that the administrative technicalities of all policy alternatives had not yet been worked out and that the Department did not have sufficient information to determine the optimum "trade-off" of each of the various proposals.[29] Donald Huggett, a member of Brown's Tax Analysis Unit during its formative period, believes that Brown would have recommended the white paper route over a draft bill because the latter would have required a great deal of work on detailed drafting of legislation, for which they "...just didn't have the horses."[30] A public white paper debate would supposedly supply much of the "information" on political trade-offs, give additional time to work out technical problems and get a draft bill ready for Cabinet approval.[31] Robert Bryce counseled the white paper route over immediate draft legislation on the grounds that the public wasn't adequately prepared to understand and accept major tax reforms:

> Once we got into the guts of it we realized we had to have a white paper. The public just wouldn't have understood it if we had just plunked a bill down.[32]

However, the delay must also be seen in the context of the government's decision, announced in Mitchell Sharp's November 1967 budget, not to accept the comprehensive income concept and the Carter "package" which embodied it. Brown and his officials had been working on the Carter Report and studying various alternatives since 1965, almost as long as the Commission itself had studied the entire tax system and produced its six volume Report. Had the government been planning to base its reforms on the Carter package, there would have been no reasonable excuse for further delay. Sharp implicitly acknowledged this when he told the House that the white paper would be delayed because the government had decided not to base its reforms on the Carter Report, necessitating additional departmental studies.[33]

As Mr. Sharp had already publicly committed the government to the white paper route, and the provinces and business interests were expecting and demanding a white paper instead of legislation, then it is most unlikely that Cabinet could have been united behind Benson's proposed bypassing of this stage. Supporting this view is Mr. Benson's own account that the return to the White Paper route was the result of pressures exerted through the Cabinet, caucus, opposition and interest groups, combined with the pressure of the government's previous position in favour of a White Paper. He recalls Brown's advice however as being for a draft bill rather than a White Paper.[34] By all accounts, the Cabinet had not reached a consensus on tax reform, and the delay and public debate afforded by a white paper seemed to offer an acceptable interim measure.[35] Accordingly,

on February 21st, ten months after his appointment, Benson announced in the House that the forth-coming White Paper would not contain a draft bill.[36]

Preparing the White Paper

The White Paper originated within the Tax Policy Division of the Department of Finance, growing out of the analysis of the Carter Report by Brown's Tax Analysis Unit. Additional analyses of the Carter Report, of the views of provincial governments and of various groups and associations were prepared for the Department on contract by the Institute for the Quantitative Analysis of Social and Economic Policy at the University of Toronto, including Douglas Hartle, who had returned to the Institute after winding up his work for the Carter Commission.[37]

During the early stages, papers were drafted by Brown and Division members, then discussed in frequent Division meetings. Brown's role in shaping the White Paper does not appear to have been a conservative one. On at least one occasion he found that a paper written by Donald Huggett on international taxation "did not go far enough" and re-wrote the paper himself.[38] Once Brown was satisfied with a paper, he defended it before the Tax Review Committee,[39] which was chaired by Bryce, and included Al Johnson, D.S. Thorson, Deputy Minister of Justice, two or three people from National Revenue, Taxation and a couple of "more technical people" from Finance.[40] The Committee

considered over 100 such papers, some of which Bryce took to the Minister's office where Benson's Special Assistants, Peter Farwell and Michael Gillan also played a role,[41] and then to the Cabinet Committee on Taxation. At the levels of the Tax Review Committee, the Minister's office and the Cabinet Committee, the Tax Analysis Unit's ideas of what was equitable and technically feasible were balanced in different degrees with what was politically saleable. No proposal to implement the Carter Commission's comprehensive income concept reached the Cabinet Committee stage since the idea was not considered politically feasible.[42]

The special Cabinet Committee on Taxation, which had been set up after the June 1968 election, and which included Benson, Coté, Donald Jamieson, C.M. Drury, Eric Kierans and two or three other ministers,[43] began to meet frequently between April and October of 1969.[44] Committee members were apparently selected by Gordon Robertson, in consultation with Bryce, Reisman and other senior officials without prospective members being asked whether they wished to serve.[45] Both Bryce and Brown attended the Cabinet Committee meetings, often with one or two staff specialists in particular areas, to assist their Minister in explaining and defending the proposals.[46] Bryce, who saw the Cabinet Committee sessions as part of an educational and persuasive effort, together with Brown, gave the ministers a substantial oral and written explanation of how the income tax system worked and what the issues were.

It was also a process involving controversy with some members of the Cabinet Committee.[47] Eric Kierans recalls the Committee meeting every Wednesday night, with about ten or twelve staff from the Departments of Finance and National Revenue.[48] The staff handed out copies of whatever paper was scheduled to be discussed that evening, most of the Committee members not having seen it in advance. One minister asked, "What am I supposed to do with these?" and was told that his "comments would be taken under advisement."[49] Sometimes papers were criticized, then returned to the Committee in the same form at the next meeting.[50] With the exception of Kierans and Benson, the ministers appeared to understand little about tax reform or economics, and probably had not read the Carter Report.[51] The agenda was controlled by the Department of Finance, and Committee members were inhibited from raising issues which were not dealt with in the paper under discussion:

> ...whatever... paper [was] handed to you: you discussed it as you were reading it and then... officials from the Department of Finance immediately afterwards collected all the papers from the ministers and everybody else and put them back. Those I wanted to retain were retained just by being obstinate about it, but all of this lent an air really of complete incredulity to the whole thing, and I was just amazed that anyone could consider that this was an honest attempt to come to grips with the problems of tax reform. There was no one on that committee with the exception of Jim Brown and Bryce himself who could really discuss the philosophy of what we were doing or could really integrate the overall objectives of what a tax reform proposal was. No one of them would have read Simons or knew anything about Haig or anything like that....[52]

The definition of problems and alternatives had already been accomplished at the departmental committee stage and therefore not much in the way of substantive change was expected at the Cabinet Committee level. If Benson shared any of Kierans' views on tax reform it was with regard to the very limited capacity of the great majority of cabinet ministers to intelligently discuss the issues.[53] Mr. Benson, the Department of Finance, and probably most ministers therefore did not anticipate or look forward to any open-ended Cabinet discussion of tax reform alternatives. When he attempted to re-open significant issues, Kierans found himself a minority of one:

> You could frighten the other ministers as ...five of those seven or eight ministers would have preferred to be on some other cabinet committee ...rather than on this one. So if a deputy minister says, "Well if you do such and so on the taxation of mining, take away depletion allowances, you are going to close down, or the mining industry says that they will close down", well your five ministers really cannot assess that kind of a challenge... so they tend to go along with that, and then the committee has its majority. So you have two guys at the most, let's say, they are quite concerned about it and five guys who are not. Well the five guys aren't going to upset any apple carts.[54]

After approval by this committee, the draft White Paper was submitted to the Cabinet Committee on Priorities and Planning and the Cabinet Committee on Legislation, and finally to the whole Cabinet.[55] Discussion in full Cabinet was more limited, with the Minister of Finance presenting what had already been approved by the

Special Cabinet Committee on Tax Reform. Again, Kierans found himself to be the lone dissenter:

> ...[I was] really quite frustrated because there were people in the full cabinet [who] knew a fair amount of what this was all about, but never raised their voice at all -- and there were people like Allan MacEachen who had an economics background, and there were one or two others who had a sense of fair play and equity and so on but simply didn't raise their voices in defence of a more reform-minded set of proposals....[56]

The burden of defending the draft white paper in full Cabinet was Benson's prerogative as Minister of Finance. With the exception of Kierans, there was little opposition or argument from other ministers, who were not anxious to challenge a minister on his own turf when it "was so clear which way the ...thing was going to go."[57] However, Kierans' opposition was sufficiently determined for Benson to call upon the assistance of Department of Finance officials.[58] Kierans' opposition to what he considered the watering-down of the Carter recommendations had, with the exception of a promise to review the system of capital cost allowances, no appreciable effect on the contents of the White Paper.[59] While the subsequent controversy caused some ministers to think that they had not paid sufficient attention to the debate in Cabinet, their second thoughts were in the opposite direction to that desired by Kierans.

The final drafting stage began in the summer of 1969 and involved

Brown, Bryce (who by this time had formally retired as Deputy Minister, but was staying on as "Economic Advisor to the Prime Minister"), Simon Reisman (the new Deputy Minister), A.S. Rubinoff (Director of the Economic Analysis Division), Thompson, Irwin, and Doug Andison, a lawyer working on contract for the Division. Most of the final drafting was done by Brown and Bryce, when they had most of the Cabinet Committee's decisions in hand.[60] The White Paper, entitled Proposals for Tax Reform[61] was finally tabled in the House on Friday, November 7, 1969.

The White Paper: Proposals for Tax Reform

As with the Carter Report, understanding the controversies which raged around the White Paper presupposes an understanding of the contents and major implications of the government's proposals. Although the order of topics presented here reflects our interest in the comprehensive income concept, this exposition generally follows the headings of the White Paper and compares salient recommendations to those of the Carter Commission.

The Tax Base and Capital Gains:

While accepting the goal of "fair distribution of the tax burden based on ability to pay",[62] and the consequent requirement for an effectively progressive system of income tax, the government believed

that the Carter Commission had "carried some of its arguments to extremes which the Canadian public would not support."[63] The authors of the White Paper made greater concessions than did the Royal Commission to arguments based on economic growth, the need for tax incentives, stability, taxpayer acceptance, and acceptance by the provincial authorities.[64] They refused to accept the comprehensive income concept "in all its splendid simplicity", nor did they accept the opposite contention that:

> ...the distinction between a so-called "capital gain" and an income receipt is either great enough or clear enough to warrant the tremendous difference between being completely exempt and being completely taxable.[65]

The Carter Commission's arguments regarding the need to make the income tax more effectively and uniformly progressive by widening the tax base to include capital gains while lowering the top marginal rates were accepted,[66] as was its argument for the taxation of capital gains on grounds of certainty.[67]

Generally, capital gains would be fully subject to tax, with the following exceptions:

1. Principal residences would be allowed an exemption of $1,000 per year of occupancy, plus maintenance costs, or an arbitrary allowance of $150. A "rollover" provision was included for a taxpayer moving to another location in Canada in connection with a change of job, and who purchased another home within a year from the date of sale.[68]
2. Personal property gains under $500 would be exempt, and a

deduction of $500 or the actual cost, whichever is greater, would be allowed on other such gains. To prevent the claiming of personal consumption expenses as capital losses, no losses would be allowed on depreciable personal property.[69]

3. Only half of gains on shares of "widely-held Canadian corporations", that is companies listed with stock exchanges and those able to meet specified tests regarding number of shareholders, dispersal of ownership and public trading in shares,[70] would be included in taxable income, and half of losses would be deductible.[71] This was defended on the grounds that such companies would then be "on approximately the same footing" as American and British individuals and corporations, and when combined with the proposed 50 per cent credit for corporation taxes paid, would result in little incentive to manipulate transactions to avoid tax.[72] This softening from the position of the Carter Commission, however was offset by the White Paper's proposal to tax such gains as accrued, rather than wait until realization, or bequest, as the Commission had reluctantly recommended.[73] Shares of widely-held corporations would be re-valued every five years, thus reducing the "lock-in effect" that might have arisen from the taxation of only realized gains, and reducing revenue loss and propensity for avoidance or evasion which might accompany postponement.

4. Unlike the Carter Commission, and in recognition of the possibility that "two taxes [Estate and Income] could apply at the same time -- [and]... at a most inconvenient time..." the White Paper proposed that deemed realization not apply at the transfer

of property on the death of a taxpayer, but that it be postponed until the executor or beneficiary disposed of the assets.[74] This was clearly a response to the protests against "double taxation" proposed by the Carter Commission.[75]

5. Rollovers would be allowed in cases where there was a forced realization (such as on receipt of insurance payments), or when there was no underlying change in the beneficial ownership of the assets even though the legal form of ownership had changed. Many rollovers of the latter type would involve widely-held corporate shares, which would be subject to revaluation and taxation every five years in any case.[76]

Personal Income:

The White Paper rejected the Royal Commission's family unit concept and the zero rate bracket,[77] opting instead to raise personal exemptions and add or modify a number of deductions. In agreement with the Commission's comprehensive income concept, unemployment insurance payments, bursaries and scholarships, adult training allowances would be taxable.[78]

The rate structure would also be modified, which, when combined with changes in exemptions and deductions, would reduce the effective tax rate for individuals with incomes under approximately $3,000, and under about $8,000 for a maried couple with two dependent children.[79] By the end of the fifth year of the reformed system,

when the top marginal rate of combined federal and provincial tax had been lowered to 51.5 per cent, those taxpayers who did not suffer as a consequence of the taxation of capital gains would benefit if their income before exemptions and deductions were above about $50,000.[80] This left a substantial number of taxpayers among those with incomes between approximately $5,000 and $40,000, many of them wage- and salary-earners, who would have to pay from about $50 to about $300 more in taxes, even if their taxable income had not been increased by the capital gains or any other proposals.[81]

The Carter Commission had recommended a rate structure that would have reduced taxes for nearly all wage- and salary-earners, regardless of income.[82] The White Paper however, in not adopting the comprehensive income concept to the extent proposed by the Commission, was not able to recommend as generous a reduction in rates for middle-income earners. Also, the government's expectation of a higher level of revenue requirements since the Commission had considered the question put an additional constraint upon the authors of the White Paper.[83]

"Corporations and Their Shareholders":

The income of closely-held corporations would be taxed on a flat rate of 50 per cent, with full credit to the shareholders so that the final tax to the shareholder would be levied at his personal rate. Under certain conditions, the shareholders of the closely-held

corporation could elect to be taxed as a partnership, allowing the corporation to pass the liability on to its shareholders.[84]

Widely-held corporations would pay a flat-rate tax of 50 per cent, with a credit of half the taxes actually paid to be extended to the shareholders and credited against personal tax on cash or stock dividends.[85] Under the existing system, the 20 per cent dividend tax credit benefited shareholders of all corporations which were not classified as "tax exempt", regardless of whether or not those corporations had actually paid enough tax to cover the dividend tax credits claimed by the shareholders.[86] This was also available to foreign corporations resident in Canada, a privilege which the White Paper proposed to remove over a period of five years.[87] As with the integration scheme proposed by the Carter Commission, the refundable tax credit would have the effect of taxing individual shareholders at their personal marginal tax rates rather that the flat corporate rate initially paid by the corporation. However, unlike the Carter recommendations, this would affect only half of the corporate tax paid by widely-held corporations.

Generally, inter-corporate dividends would continue to be tax-free, though the government would end the existing practice whereby Canadian shareholders benefited from the dividend tax credit even though the dividends arose out of income received from corporate holdings abroad which had never been subject to Canadian income tax.[88]

The existing three-year exemption for new co-operatives would be removed, and the computation by which co-operative profits could not be reduced below 3% of capital employed through the deduction of patronage dividends would be tightened, with the minimum set at a rate comparable to the interest rate currently paid on government bonds.[89] On the grounds that credit unions and caisses populaires were "in real competition with other financial institutions", they would be treated in the same way as co-operatives, and be allowed the same deductions for doubtful debt reserves and market liquidity reserves as banking institutions.[90]

Business Income:

In addition to the changes discussed under the previous headings, the White Paper proposed the following changes:

1. "Nothings", that is, capital expenses such as business "goodwill" would be deductible according to specific rules, since the associated capital gains would henceforth be taxable.[91] This was in accord with the Carter recommendations.
2. Regulations respecting depreciation allowances would be tightened to prevent tax postponement and avoidance.[92] The White Paper appeared to be going beyond the Commission in attempting to prevent tax avoidance in this area.
3. While not specifically referring to the Carter Commission, the arguments in the White Paper made it clear that the government had accepted the Commission's findings regarding the ineffeciency of

the existing mining and petroleum incentives. The White Paper proposed the phased removal of the three-year exemption for new mines, to be replaced by a system allowing rapid write-off of the capital invested so that no tax would be paid on income from a new mine until the cost of the initial investment had been recovered.[93] Percentage depletion would be replaced by "earned depletion", to be allowed at the rate of $1 for every $3 of expenditures on eligible exploration and development costs of mineral deposits in Canada, and which would not include the cost of acquiring mineral rights.[94] The existing percentage depletion available to non-operators, shareholders depletion, and the exemption of proceeds received by prospectors and grubstakers, would all be removed, on the grounds that their existence had rested on the justification that each had represented compensation for the non-deductibility of capital expenditures or capital losses.[95]

4. Professionals would henceforth have to compute their income on an accrual basis to prevent postponement of tax compared with other businesses. This would not apply to farmers and fishermen, however. For livestock farmers, their entire herds would be considered as inventory, and any gains accrued and realised after commencement of the system would be taxable.[96]

5. In another implicit acceptance of a Carter Commission recommendation, the investment income of non-profit social, recreational and service clubs, societies and associations would become taxable.[97]

6. Trusts, which under the existing system paid tax according to the

personal rate schedule without the personal deductions, would generally be taxed in the same manner as corporations. This change was intended to prevent the postponement and reduction of tax through use of trusts, and to put trusts on the same tax basis with corporations with which they, in some cases, competed.[98] This also reflected the philosophy of the Carter Report.

"Taxing International Income":

The White Paper approached the taxation of international income with the objectives of preventing international tax avoidance and of continuing to "attract the foreign capital essential for [Canada's] development and to open up further opportunities for Canadian exporters...".[99] While not wishing to provide tax incentives to attract foreign capital, or to put obstacles in the path of Canadians investing abroad, the government intended the system of credits for tax paid by Canadian corporations to provide an incentive for Canadians to invest in the domestic economy.[100] The White Paper recognized that "going international" was necessary for Canadian companies to compete effectively with foreign companies, and that it was

> ...in Canada's interest as a substantial capital-importing nation to maintain an international climate hospitable to the unrestricted flow of capital across international boundaries.[101]

The White Paper rejected the philosophy of the Carter Commission, that all corporations, including those with operations abroad, should

election expenses.[123]

Hartland Molson C.A., (listed as "Independent" in the Parliamentary Guide) was Chairman of Molson Breweries, Vice-President and Director of the Bank of Montreal and Canadian Industries Limited, and Director of Canadian Corporate Management and Sun Life Assurance Company and Canadian Industries Limited, all dominant corporations.

One Senator, David A. Croll, Q.C., did not fit the corporate mould of most of the other Committee members. A former Mayor of Windsor, he had been fired as Minister of Labour from the Ontario Cabinet by Premier Mitch Hepburn for siding with the auto workers during the General Motors strike in Oshawa.[124] Once appointed to the Senate in 1955, he assumed what the author of a recent study on the Senate called a "social investigator" role.[125] However, Senator Croll stands out as an exception from the Banking and Finance Committee's elite membership and pro-business orientation.

Operation of the Senate Committee:

The Senate Banking Committee held public hearings in approximately the same manner as the Commons Committee on Finance, Trade and Economic Affairs.[126] However, given the number of corporation lawyers among its members, they were in a better position than the Commons Committee members to understand the technical complexities of the subject matter. The author of one study noted, perhaps with some

length interest whenever the ratio of shareholder debt to equity ratio exceeded three to one.[106]

In order to prevent "leakage" from the tax system, the White Paper proposals respecting the taxation of gains associated with closely-held corporations required that non-residents also be taxable on such gains. It was proposed to enforce compliance by placing a "back-up" obligation on the purchaser by issuance of "certificates of compliance" on the transfer of private company shares.[107]

"Co-ordination with the Provinces":

The White Paper implicitly rejected the Royal Commission's philosophy on fiscal federalism, that the federal government should have full control over the personal and corporate income taxes, while guaranteeing the provinces a share of the revenues. Arguing that since the spending activities and revenue requirements of both levels of government were difficut to predict, the White Paper said that it would be unwise to specify the constitutional division of taxing powers, but agreed that governments at both levels had to make further efforts to harmonize "spending and taxing policies if the interests of the taxpayer are to be protected."[108] The continuation of the existing system of federal collection of provincial personal and corporate income tax was proposed, with the provincial personal income tax being expressed as a percentage of the federal tax and each province being free to vary its own percentage. The proposed system

of integration would have been greatly complicated had each province's share of the corporate income tax varied, and therefore the White Paper proposed a uniform 50 per cent corporate rate with a standard abatement for the provinces.[109]

The substantial bargaining power of the provinces to levy their own personal and corporate taxes was discretely acknowledged in the observation that the Ontario government had, in its White Paper on the Reform of Taxation, indicated an intention to institute its own personal income tax system. In remarking on the Ontario government's objectives of controlling the desired degree of progressivity through use of tax credits, and to increase its revenue from the personal income tax, the White Paper expressed the federal government's willingness to discuss a tax credit system even though it would "greatly complicate the tax return and the collection administration". What the authors of the White Paper wanted to show was that "the achievement of Ontario's purposes [and perhaps those of other provinces] may not require a separate income tax system."[110]

It was hoped that any provincial legislation required would be enacted before the end of 1971, when the federal legislation was expected to come into force, and that the provinces would either have the federal government collect their share of the personal and corporate income taxes or make their own taxes consistent with the federal system. In order to encourage the provinces to change their income taxation systems in harmony, the White Paper proposed to "guarantee provincial revenue against unforeseen reductions in the

aggregate yield of the revised personal and corporate income taxes for a period of several years."[111]

"Impact on Revenues and the Economy":

The White Paper estimated that, on the assumption of zero economic growth, the new tax system would bring in about 1.5 per cent more revenue than the existing system in the first year, and (as transitional provisions were phased out and as capital gains became increasingly subject to tax) about 5 per cent more in the fifth year.[112] It was expected that there would be a moderate reduction in private saving, and that the rate of capital investment by closely-held corporations and the mineral industries would be reduced, though the latter might be off-set by increased saving through pension funds, mutual funds, and other factors.[113] The government anticipated that these changes could be adequately regulated through appropriate monetary and fiscal policies.[114] As far as international capital flows were concerned, a modest net inflow was anticipated.[115]

The Parliamentary Arena

The White Paper was referred to the Senate Standing Committee on Banking Trade and Commerce on November 19th, 1969, and to the House Standing Committee on Finance, Trade and Economic Affairs on November

28th.[116]

Membership of the Senate Committee:

The membership of the Senate Standing Committee on Banking, Trade and Commerce would have been a good start on the Who's Who of Canadian monopoly capital. Twenty-two of its members held a total of 165 corporate directorships, with the entire Senate accounted for a total of 220.[117] Nine were members of what Wallace Clement called the "corporate elite", meaning they held one or more directorships in "dominant" corporations as defined in his study of the Canadian Corporate Elite.[118]

The Senate Banking Committee included 18 lawyers, 16 of them Queen's Counsel. The 9 elite members each held directorships in a variety of economic sectors, such as finance, insurance, mining, manufacturing and communications, indicative of the high degree of interlocks between corporate sectors which Clement had reported.[119] The Committee as a whole accounted for 11 directorships on the boards of banks and trust companies, and of 8 mining companies. The following brief profiles will illustrate how their interests transcended the interests of any particular industry to collectively encompass that of monopoly capital as a whole.[120]

The Committee's Chairman was Salter Hayden, Q.C., a tax lawyer and Senior partner in the Toronto firm of McCarthy and McCarthy,

Vice-President and Director of Atlantic Sugar Refineries, a director of the Bank of Nova Scotia (both dominant corporations), and director of at least 17 other corporations.

Lazarus Philips, Q.C., Vice-Chairman of the Committee, was senior partner in the Monteal law firm of Phillips, Vineberg, Goodman, Phillips and Rothman. Also a tax lawyer, he had served as Chairman of the Board of Governors of the Canadian Tax Foundation in 1952, was a member of the Executive Committee of the Board of Governors as late as 1964, and a participant during 1953 on the Joint Taxation Committee of the Canadian Bar Association and the Canadian Institute of Chartered Accountants which travelled annually to Ottawa to discuss the budgetary tax amendments with the Minister of Finance. In 1970 he was Chairman of Domco Industries, Vice-President and Director of the Royal Bank of Canada, and sat on the boards of directors of at least 12 other corporations, 8 of them dominant.

John Black Aird, Q.C., Liberal National Treasurer until July 1968,[121] was a partner of the Toronto law firm of Edison, Aird and Berlis, and Vice-President and Director of Algoma Central Railway. He was a member of the board of directors of at least 9 corporations, including the Bank of Nova Scotia, and Consolidated Bathhurst Limited, (both dominant) as well as being on the Board of Governors of Upper Canada College.

George Percival Burchill (Liberal) was a director of Bathurst Power and Paper, Montreal Trust and New Brunswick Telephone, all of

them dominant or subsidiaries of dominant corporations. He was also Director of several local New Brunswick companies and President of George Burchill & Sons, a local lumber company.

Eric Cook, Q.C., (Liberal) was a Director of the Bank of Montreal and at least two other corporations.

Paul Desruisseaux, Q.C. (Liberal), in addition to being a lawyer and member of the Canadian Bar Association, was also an editor, publisher, broadcaster and a Governor of the Quebec Chamber of Commerce. He was Chairman of Melchers Distilleries, and Chairman, President or Vice-President of several television, cable, film distributors and publishers, including Telegram Printing and Publishing. He was also Director of The Royal Bank of Canada, Canadian General Electric, (both dominant) and others, for a total of 23 corporations.

Louis P. Gélinas, a Liberal fund-raiser,[122] was a Director of the Mercantile Bank and of four dominant corporations: Seagrams, John Labatt, and Canada Permanent Trust, Canada Cement Lafarge, as well as sitting on the Boards of at least 19 other corporations.

Louis Giguère, in addition to being Vice-President of Campeau Corporation (dominant), was Director of Denison Mines (mid-range) and at least two other corporations. Senators Giguere, Gélinas, Aird, and fellow Committee member Harry Hays, were or had been fund raisers for the Liberal Party. It was customary among both major parties to ask corporate lawyers and businessmen with extensive contacts in the corporate world to solicit donations for party administration and

election expenses.[123]

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The Senate Banking Committee held public hearings in approximately the same manner as the Commons Committee on Finance, Trade and Economic Affairs.[126] However, given the number of corporation lawyers among its members, they were in a better position than the Commons Committee members to understand the technical complexities of the subject matter. The author of one study noted, perhaps with some

irony, that Senate Committee hearings "were conducted in business-like fashion, the issues and problems being understood at the outset by the Senators and witnesses alike."[127] Another study concluded that Senator Hayden and the Committee's senior advisor, Arthur W. Gilmour:

> ...carefully staged the hearings to provide the maximum opportunity for those who benefit most from the existing tax system to explain why this is really the best of all possible worlds and that only by providing tax concessions to every possible business group can our economy survive.[128]

Gilmour was senior partner in the Montreal office of Clarkson, Gordon & Co., former Montreal Director for Income Tax and Succession Duties for the Department of National Revenue, and author of Gilmour's Income Tax Handbook.[129] The Globe and Mail quoted from Gilmour's briefing material to the Committee on the White Paper which showed his contempt for the Government's proposals for integration, elimination of the dual corporate rate, "removal" of tax incentives to the extractive industries and other incentives, and to tax dividends from foreign subsidiaries of Canadian corporations. Senator Phillips was of a like mind on these questions.[130]

Not surprisingly, business interests took full opportunity of the sympathetic platform offered by the Senate Committee to voice their objections to the White Paper proposals. There was little pretense of the Senate Committee providing an impartial forum: nearly all the witnesses heard were representatives of corporations and business groups. The questions were both asked and answered by people who shared common assumptions regarding the need for government to provide

a favourable "tax climate" to maintain "business confidence".[131]

The Senate Committee's Report:

The Senate Committee's report rejected the philosophy of the White Paper, recommending in its place a number of incremental changes in the existing tax system.[132] The Senators did not accept even the White Paper's compromised version of the comprehensive tax base, arguing instead that capital gains should, in general, be taxed at the lower of 25 per cent or the taxpayer's personal rate. They suggested that short-term, speculative gains be taxed as ordinary income, as under the existing system. There would be more generous provision for "rollovers", that is, tax-free re-investment of capital gains under specified conditions. Unlike the White Paper, the Senate Committee wanted no deemed realization on gifts or bequests, or when the owners left Canada, thus making the tax on capital gains largely voluntary for the tax-wise and the well-counselled. In spite of the substantially symbolic effect of the Senators' version of the taxation of capital gains on the inter-generational transfer of wealth, they nevertheless recommended the abandonment of the estate tax field to the provinces.

The distinction between widely-held and closely-held corporations was rejected, as was the proposed scheme for integration of corporate and personal taxes. They proposed modifying the existing dividend tax credit to vary from 25 per cent to 15 per cent, depending on the

amount of dividends received. The general corporate tax rate would be 50 per cent, with a rate of 35 per cent for the first $35,000 of business income earned by small corporations.

The Committee's report did not reject every idea in the White Paper. It agreed that marginal rates of tax were too high on large incomes, proposing that the top rate be reduced to 50 per cent and that the rates on middle incomes not be increased over existing rates.

Given the predominance the representatives of corporate capital among the Committee's members and witnesses alike, the very conservative content of the Committee's report should have surprised no-one. Even the Globe and Mail, which had been very critical of the Carter Report and of the White Paper, refused to take the Senate Banking Committee or its report seriously:

> ...the banking committee has turned in a sorry performance. Canada has been 10 years in search of basic tax reform, and all that these senators feel that they can endure is some minor tinkering in some areas where the inequality is patently obvious -- such as the lack of a capital gains tax. The whole purpose of the white paper was to find a fair system of taxation for Canadians. The banking committee has devoted itself to shoring up privilege.[133]

As events turned out, the Senate Committee's report had less influence on the final tax reform legislation than did the House of Commons Committee on Finance, Trade and Economic Affairs. This does not imply, however, that the role of the Senate Committee was simply that of an unsuccessful exercise of the business "lobby from within".

The publicity generated by the Senate hearings contributed to the more general propaganda effort of business interests waged against the White Paper, which presented the impression that virtually all well-informed people opposed the government's proposals. Added to this was a variant of the "good cop - bad cop" routine, where the reactionary nature of the Senate report made that of the Commons Committee look progressive by comparison. The Government, in shaping its draft legislation more in the image of the Commons Committee recommendations, could appear to be taking a more progressive, reformist position and also appear to be giving what it called "participatory democracy" a chance to work.

Membership of the House of Commons Committee:

The Standing Committee of the House of Commons on Finance, Trade and Economic Affairs included eleven Liberals counting the Chairman, Gaston Clermont, and the Vice-Chairman, Alastair Gillespie, five Conservatives, two New Democrats, and two members of the Ralliement des Créditistes. While not able to boast of business connections as impressive as those of its sister Committee in the upper chamber, the membership nevertheless included a majority of businessmen, lawyers and accountants. Twelve, (60 per cent) were business owners, managers or corporate directors. Alastair Gillespie (Etobicoke) had the most impressive business credentials, with a Master's degree in Commerce, Vice-President and Director of Canadian Corporate Management Co. (listed as "mid-range" by Clement) and director of 7 other

corporations. Seven other businessmen Committee members were members of the local Chamber of Commerce or Board of Trade, or of the Canadian Chamber of Commerce. In addition, there were 4 lawyers and 2 chartered accountants, one of the latter, Liberal Aurelin Noel (Outrement), a former member of the Canadian Tax Foundation's Board of Governors.

Most of the Liberals on the Committee were elected for the first time in 1968 and were considered to be new but promising backbenchers. Barnett Danson (York North) was President of the Danson Corporation, and a member of the Board of Trade of Metropolitan Toronto. Robert Kaplan (Don Valley), a lawyer, member of the Canadian Bar Association and the Canadian Tax Foundation, was a former legal advisor to the Canadian delegation at the United Nations. Fernand LeBlanc (Laurier), was a chartered accountant in the firm Leblanc & Gagnon, a member and former Treasurer of the Montreal Chamber of Commerce, a member of the Businessmen's Association of Plateau Mount Royal, and President of Caisse Populaire St. Denis. Pat Mahoney (Calgary South), a lawyer and business executive, was a past-President of the Canadian Construction Association, Vice-President and Director of the Stampeder Football Club, former member of the Executive Committee of the Canadian Football League, Director of Chinook Holdings, member of the Calgary and Canadian Chamber of Commerce, the Law Society of Alberta and the Canadian Bar Association. John Roberts (York Simcoe), educated at the University of Toronto, Oxford, and the Ecole National d'Administration in Paris, had been a foreign service officer for the Department of External Affairs and Executive Assistant

to the Minister for Forestry and Rural Development. Ross Whicher (Bruce), listed his occupation as that of businessman, and Jacques Trudel (Bourassa), had been Sales Manager with the Heinz Company and a member of the Montreal Board of Trade and the Quebec Food Retailers' Association. The Committee Chairman, Gaston Clermont, was a Thurso, Quebec, businessman and member of the local Chamber of Commerce. All the Liberls except John Roberts were therefore businessmen, lawers or chartered accountants, not the kind of governing party representation likely to cast a jaundiced eye upon arguments for lower taxes on business.[134]

The Conservative members included three parliamentary veterans: Marcel Lambert (Edmonton West), Hugh John Flemming (Carleton Charlotte), and Robert McCleave (Halifax-East Hants). Lambert was the Conservative finance critic, a lawyer with the firm of Emery, Jamieson, Chipman, Sinclair, Lambert & Agrios, member of the Edmonton Chamber of Commerce, former Parliamentary secretary to the Minister of National Revenue, and former Speaker of the House of Commons. Flemming had been Premier of New Brunswick and Minister of National Revenue in the last Diefenbaker government. He was Director of Flemming & Gibson Limited, a building supply company, a member of the Advisor Board of Montreal Trust, and a Director of Seven-Up Sussex Ltd. Robert McCleave was a lawyer, member of the Nova Scotia Barristers Society, and a former Parliamentary Secretary to the Minister of Public Works. The Tory ranks were completed by two newcomers to Parliament: Gordon Ritchie (Dauphin), a medical doctor and member of the Canadian Medical Association; and Cliff Downey

(Battle River). All five were ideologically conservative, as one student of the Committee's activities observed, they were "deeply committed to the virtues of small enterprise, individual initiative, private property ...[and] opposed, from the start, to the philosophy of the White Paper."[135]

Two New Democrats sat on the Committee: Max Saltsman (Waterloo), a former alderman of Galt and the party's finance critic; and John Burton (Regina East), an agricultural economist, a long-time CCF-NDP activist, former member of the Canadian Brotherhood of Railway, Transport and General Workers, former Director and Secretary of the Melville Co-operative Association, and a former member of the Saskatchewan government's Economic Advisory and Planning Board. Both men were committed to tax reform along the general lines recommended by the Carter Commission.[136]

The Ralliement des Créditistes was represented by C.A. Gauthier (Roberval), the owner of a furniture business and funeral parlour, former Mayor of Mistassini, member of the Board of Caisse Populaire Mistassini, and of the local Chamber of Commerce; and by Henri Latulippe (Compton), owner of "La Maison Henri Latulippe et Propane Gaz Plant" and of a Cable TV network in Megantic, President of "Megantic Furniture" and a former alderman. The Créditiste members did not play an active role in the work of the Committee, and had very little influence on its Report.[137]

The dominant social category represented on the Commons Committee

was clearly that of business, with that of tax professionals second. The co-operative sector, including credit unions and Caisses populaires, was represented by a Liberal, a New Democrat and a Créditiste. Organized labour was represented by only one former union member. There can be little doubt, therefore, that by virtue of its composition, the Commons Committee was predisposed to view business representations less critically than a committee more representative of Canadian taxpayers.[138]

The Commons Committee Staff:

Unlike some members of the Carter Commission, and many members of the Senate Standing Committee on Banking and Commerce, most Commons Committee members knew little about the technical aspects of taxation.[139]

Early in the proceedings, Max Saltsman argued that professional staff be assigned to the different party groups on the Committee, while Mr. Clermont insisted that all staff report to the Chairman.[140] Given the Liberal majority on the Committee, the views of the Chairman prevailed, although staff members did advise individual Committee members on an informal basis.

Ronald Robertson, former Director of the Canadian Tax Foundation, was retained to head the Committee's professional staff of fifteen lawyers, chartered accountants and economists from a list of persons

nominated by the Committee members. Among them were Gwyneth MacGregor, Robertson's colleague at the office of the Canadian Tax Foundation, frequent contributor to the Canadian Tax Journal, and Editorial Director for the Carter Commission. Another was Marshall A. Cohen, a corporate tax lawyer with the Toronto firm of Goodman & Carr, who was later to join the Taxation Division of the Department of Finance to assist in drafting the 1971 tax reform legislation and eventually to become Deputy Minister of Finance.

The staff began to assist the Committee during February and March 1970, after the Departmental witnesses had been heard, and after the major decisions on Committee procedure had been made.[141] Unlike the Carter Commission, where Douglas Hartle arrived during the formative stage in the Commission's life, and was able to exercise a dominant role in the use of its professional staff and its relationship to the public hearings, Robertson and his staff were clearly the servants of the Committee and of its Chairman. The Committee staff analyzed briefs and suggested questions to be put to witnesses, prepared background papers for the Committee members, and discussed issues informally with individual members who sought their advice. There was no independent research comparable to that of the Carter Commission against which to verify the testimony of witnesses.[142] This mode of operation increased the likelihood of the Committee's report being more a distillation of the briefs and hearings than a logically coherent approach to tax reform.

Activities of the Commons Committee:

Before beginning its hearings, the Committee listened to a full-day's briefing on the White Paper by members of the Canadian Institute of Chartered Accountants. The material was drawn from the Institute's "White Paper Course", prepared for its members, and from briefing material drawn up by the major accounting firms to inform their corporate clients on the content of the White Paper. The briefing team consisted of Eric Ford from Clarkson and Gordon, David Timbrell from McDonald Currie, Robert D. Brown from Price Waterhouse, and Douglas Sherbaniuk, a specialist in tax law and Director of the Canadian Tax Foundation. Sherbaniuk had been a senior staff member of the Carter Commission and wrote one of its studies on the concept of income,[143] and Timbrell had consulted for the Commission and authored one of the two studies sponsored by the Commission on taxation of the mining industry.[144] During the following months, Brown and Timbrell were to appear before the same Committee in support of their corporate clients.[145]

The Committee also attended the March 1970 Tax Conference sponsored by the Canadian Tax Foundation.[146] As the Conference was devoted specifically to a discussion of the White Paper, it served as a "crash course" on taxation and tax reform for the relatively untutored Committee members and exposed them informally and at an early stage to the views of many tax professionals.

The Public Hearings of the Commons Committee:

Witnesses were questioned only by Committee members, who frequently ignored or misunderstood the advice of their staff.[147] In contrast to the rigorous questioning of witnesses before the Carter Commission, points tended more often to go by default to the witnesses appearing before the Commons Committee. For example, Donald Huggett, who had left the Department of Finance to return to his practice with Toppers Lyman, was defending the submission of the Montreal Board of Trade before the Committee. One question, which he felt sure had been suggested by the Committee's staff, caught him by surprise, forcing him "to wriggle and back-peddle".[148] However, to his relief, the aggressive line of questioning was not followed-up by the next Committee member to be given the floor, thus letting him and his clients off the hook.

The hearings began near the end of January with appearances by Edgar Benson, Robert Bryce and the Senior Tax Advisor, James R. Brown.[149] Bryce and Brown also appeared before the Committee on four subsequent occasions the following April.[150] During the initial interview with the senior Finance representatives, Bryce responded to questions concerning the difference between Canadian and American tax levels and the concern over a "brain drain" if middle-income earners were taxed too heavily, by suggesting that professionals might be able to compensate for a heavier tax burden by increasing their pre-tax incomes. He also said that the White Paper proposed not to tax accrued property gains on succession, notably in

the case of closely-held corporations, "a most radical change compared with the Royal Commission report...".[151]

From the point of view of the Department of Finance, the appearance of its representatives before the Committee was "an educational process", so that Committee members at least understood the White Paper before they questioned other witnesses.[152] Some were slow to accept the lesson, however, and Mr. Benson and his officials "had to defend it to some members."[153]

To offer additional opportunities for participation in the hearings, the Committee divided itself into two sub-committees and toured the country to hear submissions from interested members of the public.[154] However, in deciding to go on tour, the Committee effectively ruled out the possibility of inviting specialist testimony (that is, specialists not representing paying clients before the Committee) -- there simply wasn't enough time to hear all of the witnesses in various parts of the country who wanted to appear before the Committee, let alone invite others. The two sub-committees began their respective tours before all briefs had been received; nor were the briefs analysed in terms of how representative their authors or groups concerned were of Canadian taxpayers.[155]

Hearings therefore were not scheduled in such a way as to ensure that all legitimate interests were represented,[156] with the result that a large number of well-organized business interests were heard by the Committee to the relative exclusion of the poorly-organized. Two

observers of the tax reform process, commenting on the domination of the hearings by business, noted that the Committee proceedings "occupy 3 feet of shelf space and illustrate every conceivable special interest argument for favoritism in the name of the national interest".[157] Other studies reached similar conclusions regarding the lack of balance in the distribution of interests submitting briefs to, and appearing before, the Committee.[158] Best represented were the business and professional groups standing to lose the most from implementation of the White Paper proposals, and a fortiori, the Carter recommendations. Their briefs -- prepared at great expense by tax professionals -- were long, detailed, technically sophisticated, attractively packaged and professionally presented.[159]

The Commons Committee received 524 briefs and heard 211 witness groups. The voices of businessmen were heard most often by the Committee: 141 of the witness groups, two-thirds of those heard, represented businesses, business associations, and groups dominated by business representatives.[160] "Big business" was over-represented, even in proportion to the total business representation among the witnesses groups: 22 witness groups were direct representatives of "dominant" corporations or their affiliates, and an additional 10 were in the "mid-range" category, for a total of 15.2 per cent of all witness groups. All other businesses, medium and small, were represented directly by 66 witness groups, or 31.3 per cent of the total. The largest single category, 33.2 per cent, of witness groups were business associations: 70 of which succeeded in presenting their views orally to the Committee.

Often the spokesmen for such groups were themselves senior officials of major corporations. K.E. Steeves, who appeared before the Committee as Vice-President, Finance and Treasurer of Bethlehem Copper Corporation (a "mid-range" corporation), also was among the witnesses representing the British Columbia Mining Association and the Mining Association of Canada. J.M.P. Kelly, Q.C., the sole witness on behalf of the Campeau Corporation (a dominant corporation, of which he was a Director), also represented the Canadian Institute of Public Real Estate Companies. The six-man delegation from the Independent Petroleum Association included B.B. Rombough, who also appeared in his capacity as Treasurer and Director of Home Oil (a dominant corporation) and its parent, Cygnus Corporation. There were many such instances of corporate economy of representation.

The mining industry was represented at the public hearings by 24 witness groups (11.4 per cent), with an additional 9 briefs submitted in written form only.[161] In addition, several Chambers of Commerce from regions and municipalities where mining was a dominant factor in the economy also spoke on behalf of the industry.[162] Petroleum was also well-represented, with 15 witness groups (7.1 per cent), and an additional 15 written briefs submitted. As with the mining industry these figures do not include local Chambers of Commerce and other groups and businesses (such as the pipeline and chemical industries) which linked their fortunes to the petroleum industry.

The tax professionals were well-represented: nine individual

practitioners and professional associations appeared before the Committee. In addition, most of the corporations, business groups, and some of the non-business groups, were assisted by tax lawyers or accountants. It was common knowledge among participants in the tax reform process that many, and perhaps most of the briefs were written by or with the advice of tax professionals.[163]

Few corporations or business groups appeared before the Committee without the assistance of at least one tax professional. A comparison of the list of witnesses appearing before the Commons Committee with persons attending Canadian Tax Foundation conferences allows one to identify many of the tax professionals among the Committee witnesses. In addition, professional consultants are frequently identified in the text of the testimony. For purposes of analysis, we will define a subset of tax professionals, called "tax advocates", those persons who attended at least one of the two major Canadian Tax Foundation conferences of 1967 dedicated to the discussion of the Carter Report and who also appeared before the Commons Committee examining the White Paper. These "tax advocates" are not exclusively tax professionals in the sense of deriving most of their income from dealing with tax matters. Nor do we assume that they were more extreme in their views than other participants. However, they had demonstrated a sustained interest in tax reform (and probably commitment to one position or another) over a two-year period and almost certainly possessed an acknowledged level of competence in the subject in order to argue a point of view before a parliamentary committee. Comparison of the three lists yields a set of 152 individuals, listed in Appendix

"A".[164]

Forty-three percent of these "tax advocates" were chartered accountants, and another twenty per cent were lawyers.[165] Eighteen percent were senior officers or directors of the 113 dominant corporations, and hence members of the "economic elite" as defined by Clement. This figure, however, greatly understates the proportion of the "tax advocates" linked to monopoly capital, since a total of 82 persons (or 54 per cent of the "tax advocates") were linked in some manner, (either as directors, officials or hired consultants) to dominant or mid-range corporations. The latter percentage indicates that a majority of the "tax advocates" were linked with dominant or mid-range corporations, but still understates the real influence of "big business", since it does not include the representatives of associations which were themselves dominated by very large corporations.

A few examples will illustrate this point. The delegation of the Canadian Manufacturers' Association included the following individuals linked to dominant corporations:

-- K.O. Fowler, a chartered accountant working for Texaco in Edmonton;

-- A.D. Laing, an employee of DOFASCO, who appeared before the Committee two weeks earlier on behalf of his company;

-- John G. Lees, an employee of Aluminum Securities, controlled by Alcan, and who appeared before the Committee two weeks later in support of the latter corporation;

-- D.A. MacIntyre, a chartered accountant working for Imperial Oil, was a member of the CMA's Taxation Committee and Chairman of its "Subcommittee on Corporations and Their Shareholders".

Thus all four "tax advocates" on the nine-member CMA delegation were linked to monopoly capital. It is also noteworthy that it was the mining and petroleum sectors of big business that were represented on a delegation of manufacturers.[166]

The four-man delegation of the Vancouver Board of Trade included Derek H. Parkinson, a chartered accountant with Price, Waterhouse, and who is included in our list of "tax advocates". Parkinson also appeared on behalf of MacMillan-Bloedel (a dominant corporation) and in addition, was among the representatives of the Council of Forest Industries of British Columbia. Another "tax advocate", A.H. Zimmerman, Vice-President and Comptroller for Noranda Mines, in addition to appearing on behalf of that dominant corporation, also represented, as a member of its Executive Board, the Canadian Pulp and Paper Association, and the Canadian Potash Producers' Association. Most industry associations, local chambers of commerce and boards of trade had at least one representative from a dominant corporation, and, depending on the degree of concentration of the particular industry, some had several. At the extreme were the Canadian Bankers' Association and the Steel Industry of Canada which were effectively monopolized by monopoly capital.

What at first might be mistaken for a frenzy of interest group

activity, each industry and corporation pursuing its own ends, on closer examination resembles more a loose coalition of business spokesmen with extensive cross-cutting interests. However, this does not resemble the pluralist concept of cross-cutting interests and group membership, which is supposed to moderate socio-political cleavages and provide a basis for democratic and consensus-oriented politics. Instead, it is the cross-cutting of different sectors of corporate capital, and the consensus of different fractions of capital to the exclusion of labour, the unorganized and the underprivileged.

The officers and directors of dominant corporations who participated on the delegations of business associations provided an important element in the cementing of the various business interests. Harold M. Griffith, President and Chief Executive Officer of Stelco, and one of the "tax advocates", was also a Director of two other dominant corporations: Canadian General Electric and the Toronto Dominion Bank. Thus the interests of mining, basic steel production, manufacturing and finance were united in one articulate and impressive spokesman. A variation of the same phenomenon is that of another "tax advocate", David S. Holbrook, Chairman and President of Algoma Steel, Director of Canada Steamship Lines, the Royal Bank of Canada, Dupont, and Dominion Bridge (all dominant corporations) plus one mining corporation. This cross-cutting phenomenon spanned, not only industrial sectors but also included cultural, charitable and political organisations. "Tax advocate", W.O. Twaits, one of the primordial agitators for tax reform in the early sixties, and one of the most vociferous critics of the Carter Report,[167] in addition to

his well-known role as President of Imperial Oil (a dominant corporation which submitted one of the most comprehensive and technically impressive briefs) was also a Director of the Royal Bank of Canada, Vice-Chairman of the National Industrial Conference Board, a Governor of the University of Toronto and member of the Economic Council of Canada, the Advisory Council to the Minister of Industry, Trade and Commerce, the Canadian-American Committee, the Canadian Economic Policy Committee and the British North American Committee.

A second unifying element was provided by the tax professionals, primarily the tax lawyers and chartered accountants. Many were officers and directors of the dominant and mid-range corporations as well as members of their respective professional organizations and of the Canadian Tax Foundation. Most of the others were partners in independent professional firms which did business with large corporations.

A few examples of the "independent" tax professionals among the "tax advocates" will illustrate how a small number of tax professionals may encompass a world of corporate diversity. J. Kerr Gibson, Senior Partner in the firm Clarkson, Gordon and Co. did not sport any corporate directorships but appeared before the Commons Committee three times: as a consultant for the Mining Association of Canada, as a member of the Taxation Committee of the Toronto Board of Trade, and on behalf of George Weston Limited (a dominant corporation). Philip F. Vineberg, Q.C., partner in the Montreal firm of Phillips, Vineberg, Goodman & Co., became familiar with the

Committee members as he spoke on behalf of the Quebec Bar, the Association of International Business Corporations (which included eight corporations, four of them dominant or mid-range: Massey Ferguson, Seagrams, Aquitaine, and Rio Tinto Zinc), the Association of Canadian Distillers and the Canadian Association of Real Estate Boards. Vineberg was also a director of two dominant corporations, Seagrams and Edper Investments, as well as of eleven others. Robert D. Brown, a chartered accountant with Price Waterhouse in Toronto, and a renowned specialist on the taxation of the mining industry, appeared on March 17th with the delegation of the Canadian Institute of Chartered Accountants briefing the Commons Committee members on the White Paper, and on June 1st while presenting the Institute's own views, then on behalf of McIntyre Porcupine Mines at the end of May. P.N. Thorsteinsson, appeared before the Commitee as Tax Advisor to Syncrude, a consortium which included the dominant petroleum companies, Imperial Oil and Gulf Oil. Later that summer, Thorsteinsson assisted delegations from Interprovincial Steel and Pipe, Western International Hotels, and Woodward Stores. John Godfrey, Q.C., a corporate lawyer with the Toronto firm Campbell, Godfrey, Lewtas & Co., chief fund-raiser for the Liberal Party,[168] and later a Senator, appeared before the Commons Committee as President of the Canadian Mutual Funds Association. He was president of four corporations, on the boards of Montreal Trust (a dominant corporation), two mines, and thirteen other companies. Altogether, 57 such "independent" professionals (37.5 per cent of the "tax advocates") represented one or more corporations or business associations before the Commons Committee. Fifteen of these

practitioners appeared on behalf of corporations or associations in the mining or petroleum sectors.

Tax professionals also assisted some of the few non-business groups which appeared before the Committee. Other professionals, including doctors, dentists, teachers, engineers and architects, were reasonably well represented at the Committee hearings, accounting for 21 individuals, professional firms and associations.

Few spoke on behalf of the millions of taxpayers who might have hoped to benefit from tax reform. Of the latter, not many would have had the opportunity to develop the necessary capacity to critically assess the arguments in the tax reform debate, nor would they have possessed the resources to hire experts to compose briefs and to argue on their behalf before the Committee. The Committee considered inviting public finance specialists, who might have been expected to fulfil a quasi "public defender" role, but, as we have seen, it rejected this for lack of time.[169] The Committee's time was short because of the large number of groups, businesses and individuals who demanded and were granted a hearing. As a result of the decision not to limit the allocation of Committee time devoted to hearing other groups in order to free time for invited specialists to testify, the overall balance of representations to the Committee was grossly out of proportion to the composition of the population which would be affected by any reform measures.

Agricultural interests were represented by 8 witness groups, and 6

groups spoke on behalf of co-operatives and credit unions. Employees were represented by only 6 organizations (2.8 per cent of all witness groups), including the Canadian Association of Social Workers, the Canadian Labour Congress, the Canadian Teachers' Federation, the National Hockey League Players' Association, the Public Service Alliance of Canada and the Saskatchewan Wheat Pool Employees' Association. Two remaining non-business categories of witnesses were the non-profit, voluntary and charitable organizations, of which 11 appeared before the Committee. Public sector organizations, including the federal departments of Finance and National Revenue, provincial government delegations, school boards, universities and hospitals accounted for 12 witness groups.[170]

Content of the Briefs and Hearings:

The majority of briefs and witness groups opposed the integration scheme for corporate and personal taxes, the elimination of the "small business incentive", the removal of special treatment of extractive industries, the taxation of business entertainment expenses, the 5-year deemed realization of capital gains on widely-traded shares,[171] and the "high rates" on the $10-25,000 income brackets.[172]

The common argument of practically all briefs and testimony opposed to the White Paper was that the proposed reforms would retard economic growth by reducing financial incentives for people and

corporations to take risks by investing their savings.[173] More subtle versions of the argument did not oppose the goal of "equity" tout court, but explained that in order to give the less advantaged sectors of society their due the economy must generate more wealth to be re-distributed, and this could only be achieved by creation of a "favourable tax climate".[174] This theme was repeated time after time by opponents of the White Paper in statements to the press, in briefs, at business and professional meetings, and in the parliamentary committee hearings.

As was the case with the propaganda campaign following publication of the Carter Report, this message was repeated most frequently and most urgently by representatives of the mining and petroleum industries. A long series of pessimistic statements by corporate executives, warning that the proposed increase in the tax burden on mining and oil companies would result in reduced investment and a corresponding reduction in economic activity and employment, appeared in newspapers during the ten months following release of the White Paper and during the spring and summer in the form of briefs to the parliamentary committees.[175]

Few groups supported tax reform, either as defined by the Carter Report, or in terms of the White Paper. The Canadian Labour Congress, the Canadian Welfare Council, the Public Service Alliance of Canada, and the Vanier Institute of the Family, were among the few groups which said that the White Paper did not go far enough to implement the progressive recommendations of the Carter Commission.[176]

The Erosion of the White Paper Proposals

Given the lack of balance among the forces participating in the white paper exercise and the declared openness of the government to persuasion, an erosion from the initial position of the White Paper was unavoidable. While the theatre of participation was still going on in the parliamentary committee rooms, most of the actual concessions were being made in the executive arena.

Provincial Opposition to the White Paper:

As co-habitants with the federal government in the income tax condominium, the provinces were among the most influential actors in the debate over the White Paper. While the specific issues of contention were sometimes technically complex and subtle, the general tenor of provincial reaction was that the White Paper proposals would harm provincial economies and provincial government revenues. The provinces used press r[illegible], speeches at business, professional and party gatherings and [illegible]l-provincial meetings to propagate their views. In addition, Ont[illegible], New Brunswick and Saskatchewan presented oral submissions to the Commons Committee, and Alberta, Manitoba, Quebec, Nova Scotia and Newfoundland sent written briefs.[177]

The controversies between the federal government and that of

Ontario were the most intricate of all. Initial reaction by Ontario Treasurer, Charles MacNaughton, was that the proposed system of increased personal exemptions was not progressive enough in terms of its impact on low income recipients many of whom did not pay income tax and could not therefore benefit from deductions and that Ontario therefore favoured a system of refundable tax credits.[178] The other major item of contention, MacNaughton warned, was the planned increase in revenues for the federal government, which he said the provinces would need in order to shift municipal taxation away from property and other regressive taxes, "particularly for those groups who have not shared fully in the economic advance of recent years."[179] MacNaughton said that he was satisfied with the taxation of capital gains as proposed, adding that "the present tax-free status of capital gains [was] an obvious source of inequity and distortion...."[180]

However, as the pressure of business interests and tax professionals mounted against the White Paper, Ontario's opinion hardened. During the Ontario Conservatives' Annual Meeting Premier Robarts said, "I would rather have a capital gains tax, ...then there would be no need for death duties",[181] indicating opposition to Benson's recent amendments to the estate tax. Perhaps unaware of any contradiction with his Treasurer's earlier statements regarding the progressive virtues of tax credits, Robarts declared that the lack of federal imagination manifest in the failure to extend tax deductions for such items as mortgage payments and municipal taxes was "one of the reasons Ontario considered going into the income tax field itself."[182] The following week, MacNaughton announced that

Ontario's study of anticipated revenues revealed that the White Paper proposals would generate more than $1 billion additional revenue annually after five years, rather than $630 million estimated by the federal Department of Finance. At the end of January, Ontario Mines Minister Alan Lawrance attacked the White Paper proposals for reforming the system of tax incentives for mining companies, removing the dual corporate rate, and retaining the taxation of inheritances.[183]

Then, in a February 10th speech to the Financial Executives Institute in Toronto, Premier Robarts criticized as "inequitable" the proposed form of capital gains taxation, preferring in its place the American system which exempted homes and allowed concessionary rates on long-term gains.[184] The five-year re-valuation scheme, he denounced as "unconscionably harsh and damaging...", "administratively unwieldy", an invitation to evasion, and a hindrance to efforts to increase Canadian ownership of the economy.[185] The combination of the capital gains tax and the removal of the dual corporate rate "could spell the end of the small business developed by individuals, which has been the well-spring of our success and strength through more than one hundred years...".[186] He described as "confiscatory and punitive" the White Paper proposal to tax capital gains as well as gifts and inheritances.[187] The federal government, he charged, stood to gain $1.3 billion in revenue from the proposed changes: "Never in Canadian history, except in wartime, has such a tremendous tax increase been proposed or implemented...".[188] Robarts' speech took up about a third of the front page of the Globe and Mail, under

the headline: "White Paper called damaging: Economy could be retarded by tax plan, Robarts claims". Directly underneath was a photo of Benson defending his White Paper at a large meeting sponsored by the Toronto Star. The abuse heaped on Benson's proposals at that meeting by small business advocate, John Bulloch, though more extreme in tone, was not so different in substance from the criticism of the Ontario Premier.

Robarts' attack on the White Paper further heartened the forces opposed to Benson's tax reform proposals. As Keith Sandford, the Canadian Construction Association's taxation officer (and one of our "tax advocates") told a meeting of the Association in Edmonton, "If Robarts says no, it will have to be changed."[189] The Ontario Premier repeated his criticism of the White Paper while dining in the supportive company of 200 top financial executives in the candle-lit ballroom of the Toronto Granite Club.[190] Benson's riposte was a challenge to the Ontario Liberals to defeat the Robarts government at the next election.[191] While the Ontario Liberals gave Benson a sympathetic hearing in a discussion of the White Paper, the Party was uncertain and divided in its views on tax reform.[192] Ontario's opposition to the major White Paper proposals continued to make news until June, when the provincial government presented its views to the Commons Committee.[193]

While approving of the increased personal exemptions (though smaller than those allowed by Quebec), Quebec's Finance Minister Mario Beaulieu opposed the proposed elimination of the dual corporate

rate.[194] Liberal Opposition Leader, Robert Bourassa told a Montreal Junior Board of Trade audience that, as Premier, he would defer application of Quebec's share of the capital gains tax for several years in order to stimulate investment. Although he considered a tax on capital gains to be just and equitable, he had "to consider all aspects of the economic situation in Quebec."[195] When the time came for Quebec to present its views to the Commons Committee, that Province had a new Liberal government, and Robert Bourassa's indulgence for tax concessions to stimulate investment enjoyed the authority of the Prime Minister of Quebec.[196]

None of the other provinces expressed clear support for the White Paper and most opposed the proposals on mining taxation, the 5-year re-valuation of widely-held shares, and the dual corporate rate. Saskatchewan's Liberal Premier Ross Thatcher was the first to voice provincial opposition to the White Paper,[197] and continued to be the most extreme and vocal of the provincial critics. Thatcher singled out the increase in the tax burden on "middle class people", the taxation of capital gains and the changes in the incentives for the mining and petroleum industries.[198] On emerging from a mid-December conference with provincial finance ministers and treasurers in Quebec City, Benson said the provincial objections to his proposals centred on the taxation of corporations "big and small", the five-year re-valuation scheme for shares of widely-held corporations and the reduction of incentives for the resource industries.[199] However Benson emphasized that the federal government was not firmly committed to its proposals: "...we will change anything in the white paper if

we can be convinced it should be changed."[200] He repeated such protestations of flexibility many times during the nine months of the White Paper debate as he went from one hostile reception to another.

At the February 1970 meeting of Finance Ministers and Provincial Treasurers, Nova Scotia's Finance Minister called for replacement of personal deductions by refundable tax credits, thus joining the Ontario government and the federal New Democratic Party on that issue.[201] He also feared that "have-not" provinces like Nova Scotia might not share adequately in increased revenue from corporate taxation, since relatively few shareholders resided in such provinces.[202]

Alberta, in a brief which had previously been presented to Benson, expressed strong opposition to the whole philosophy of the White Paper, endorsing instead the business view of pro-growth and free enterprise.[203] Saskatchewan expressed similar views to those of Alberta.[204] New Brunswick wanted a lower rate structure for the proposed tax on capital gains, more generous treatment for small business, and lower rates on middle incomes. The general tone was pro-growth, like the other provinces.[205]

The participation of provincial governments in the Commons Committee hearings added more weight to the already imposing opposition to the White Paper, and to any tax reform of a progressive nature. The Committee's Report said that the provinces' submissions reflected:

> ...for the most part what the Committee has found to be the general view of many Canadians from whom it has heard, namely that at this stage of Canada's development economic growth is regarded as having a higher priority than the degree of equity sought in the White Paper. The succinct phrase "too far, too fast" perhaps best sums up the tenor of the views of most of the provincial governments on the White Paper proposals as a whole, in particular on taxing capital gains.[206]

Benson Responds to the White Paper's Critics:

Mr. Benson never ceased to emphasize that the proposals in the White Paper were simply that, promising, "If Canadians... put forward ways in which proposals could be improved the government will be quick to adopt them."[207]

Only five days after publication of the White Paper, Mr. Benson stated in Vancouver that he did not think any downward revisions in capital cost allowances were merited, even though a study of the system was promised in the White Paper because of criticisms that the allowances were too generous. Benson's remark was quoted by Derek H. Parkinson (a "tax advocate") at the March 1970 Tax Conference and taken to constitute a commitment that past concessions in this area would not be removed. As Eric Kierans later observed, this "quick and easy capitulation" strengthened the hope and resolve of opponents of the White Paper.[208]

At the end of November, during the debate on a motion to refer the White Paper to Committee, Benson tabled in the House of Commons two

modifications affecting the application of capital gains tax to bonds and mortgages.[209] The limit to the government's flexibility, said Mr. Benson, was the achievement what it saw as the primary goals of tax reform, first "a fair distribution of the tax burden based on ability to pay", and secondly, a tax system which "interferes as little as possible with economic growth and productivity."[210]

As with the Carter Report, reaction to the White Paper was about evenly mixed at first, then the balance shifted in favour of the critics of major proposals. Almost all business and professional critics denounced the proposed five-year revaluation of widely-held corporate shares and the closely related distinction between widely-held and closely-held corporations. "It's a question that comes up everywhere I go", Benson acknowledged to a meeting of the Institute of Chartered Accountants of Ontario.[211] Most seemed to feel that the distinction was arbitrary or "artificial" (an odd adjective, since practically everything in the world of taxation is the product of social convention). Frequent objections were that owners of closely-held corporations would be deterred from offering shares on the stock market, thereby inhibiting small Canadian-controlled corporations from expanding, preventing Canadians from purchasing shares in foreign-controlled corporations, and possibly forcing the sale of Canadian-owned corporations to foreigners. It was frequently pointed out that an owner of controlling interest in a widely-held corporation might have to sell a portion of his shares in order to pay the tax on unrealized gains, thereby losing control of his company. The chief complaint here lay

in the government's intention to tax unrealized gains in the market value of corporate shares, something not recommended even by the Carter Commission except as a goal for the indefinite future. Calculations of hypothetical tax liabilities, (based on historical stock values which rose rapidly in a no-capital gains tax regime and probably also reflecting increased values due to hoarded surpluses) were used by I.H. Asper, in his regular newspaper column to make it appear that the real rate of corporate tax would be in excess of 60 per cent.[212]

Benson's response to these objections was to submit a departmental paper to the Commons Committee, examining possible implications and alternatives if periodic revaluation were dropped.[213] Prominent among the alternatives was deemed realization of capital gains on death, the proposal recommended by the Carter Commission majority and opposed so vehemently by most of its critics. Some tax professionals were attracted to this alternative, provided that the estate tax were eliminated or at least its rates sharply reduced. Many tax professionals had agreed with Beauvais' and Grant's minority reports, that the Carter recommendation to tax gifts and bequests as ordinary income and, at the same time, deem realization of capital gains on gift or bequest was "double taxation".[214]

Closely linked to objections to the distinction between closely-held and widely-held corporations were criticisms of the two corresponding modes of full and partial integration. There was no consensus on the alternative, but a majority of business and

professional spokesmen appeared to be leaning toward removal of the closely- or widely-held distinction, replacement of the integration proposal by some minor change in the existing dividend tax credit, usually accompanied by a reduction in the weight of tax on capital gains.

Another area of controversy was the White Paper proposal to remove the 21 per cent rate of tax on the first $35,000 of corporate income. This proposal spawned Toronto businessman, John Bulloch's Canadian Committee for Fair Taxation, which denounced this provision and most of the rest of the White Paper as a revolutionary socialist document, and as a plan for the expropriation of small business and the entire private sector.[215] The proposals for taxation of capital gains, the increase in tax rates for "middle-income" earners, combined with the removal of the dual corporate rate and the 1968 Estate Tax amendments, were held out as evidence that the government was trying to confiscate the resources of the middle class.[216] A member of Bulloch's group, Irving Rosen, a chartered accountant with the firm of Rosen, Ezrin & Co., former member of the Smith Committee to study Ontario's tax system, and one of the "tax advocates", told an angry crowd of nearly 3,000 in Toronto's Royal York Hotel that many small businessmen in the $10,000 a year bracket would face tax increases of far more than $300.[217]

Another member, London Insurance Executive, Colin Brown paid about $23,000 to run full-page ads in Canada's major dailies attacking the White Paper and asking readers to send coupons opposing it to their

members of Parliament.[218] In an interview with the Globe and Mail's social columnist, Zena Cherry, Brown accused Trudeau and Benson of being socialists, citing as proof some quotations from Trudeau's writings.[219] While admitting that he was not himself a tax expert, the dangers posed by the White Paper had been pointed out to him by "people who are experts in the field... chartered accountants, tax lawyers, and bankers."[220] Price Waterhouse had done the figures in his ad which argued that the government had "cooked the books" in its comparisons of Canadian and American tax levels.[221] The ads sparked enough support for Brown to organize another anti-White Paper lobby group, the Committee For Fair Taxation.[222] Partly as a result of the efforts of these two anti-White Paper groups, at least 26,000 letters were received in Benson's office in the Department of Finance, from November, 1969, to June, 1971, plus coupons in the "bushel loads".[223] Not all letters were opposed to the White Paper but over 6,000 of Brown's coupons were received, and some members of Parliament received as many as 1,500.[224]

Such groups represented one extreme of the spectrum of opposition to the White Paper proposals. Tax professionals and business executives quoted in the press tended to separate themselves from what they considered to be hysterical reactions, yet opposed some of the same proposals with more reasonably-sounding arguments. Toronto lawyer, Marshall Cohen, speaking to a meeting of the Canadian Fruit Wholesalers Association in Montreal, defended some aspects of the White Paper, particularly integration, and warned his listeners that a tax on capital gains and removal of the dual corporate rate were

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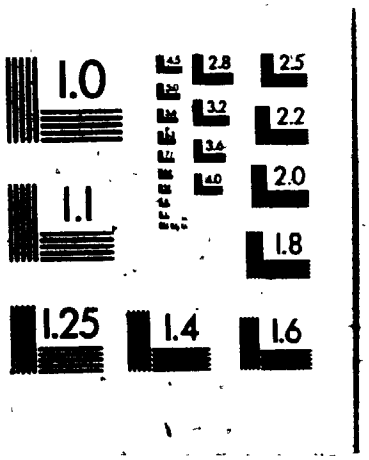

inevitable.[225] Cohen, while maintaining that "There's nothing unfair or unreasonable about a capital gains tax, criticized the five-year revaluation plan as "wrong" and responsible for the "over-reaction" of taxpayers.[226] Shortly afterward, Cohen was to be retained as a specialist advisor to the Commons Committee studying the White Paper.[227] A.J. Little, partner in Clarkson and Gordon, told a Queen's University seminar on tax reform that the Canadian Council for Fair Taxation had adopted a completely destructive approach and was promoting hysteria throughout the country.[228] Little advised Benson to take a more gradual approach, beginning with a capital gains tax no higher than 25 per cent, then, as revenue came in from the tax on captal gains, reduce the burden on those with low incomes. The removal of the dual corporate rate should be deferred until 1972, and then introduced with the commitment to replace it with an alternate incentive to small businesses. "Five-year revaluation", he said, "won't work and has to go, and with it should go the distinction between widely-held and closely-held corporations."[229] Little also thought that business entertainment expenses should be deductible, that averaging provisions should be more generous, that there should be joint returns for husband and wife, and that the three-year exemption for new mines should be restored.[230] Wolf D. Goodman, partner in the Toronto law firm Goodman and Carr and one of the "tax advocates", told a meeting of the Advertising and Sales Club of Toronto that the removal of the split corporate rate would hurt only those incorporated small businesses which paid high executive salaries and left $35,000 or less in the company for growth, that is, companies whose owners were deliberately taking advantage of the low rate.[231]

He said that the closely-held, widely-held distinction should be scrapped however, and doubted the workabilty of the five-year valuation scheme.[232] Lancelot J. Smith, former Chairman of Ontario's "Smith Committee" on taxation, denounced the "emotional" and "irresponsible criticisms" of the White Paper. He urged the government, however, to tax only half the gains on all forms of property and to abandon what he called the "giveaways" in the proposals, particularly the five-year deemed realization of widely-held shares. He recommended instead deemed realizaion at death, combined with a substatial reduction in the weight of estate taxes.[233]

One of the early supporters of the White Paper was J. Harvey Perry, Executive Director of the Canadian Bankers' Association, and former member of the Carter Commission. In an article published in The Canadian Banker and reported in the Globe and Mail,[234] Perry summarized the contents of the White Paper and assessed it against the Carter Report. Perry's cautious remarks on the White Paper had not been cleared with his banker employers and caused one of them to demand that he be asked to resign.[235] The other bank presidents were not prepared to take such drastic action, and it was agreed that Perry would remain as Executive Director, but that he should leave taxation (his area of recognized expertise) to the bank presidents.[236]

The bankers were quick to rectify the damage wrought by Perry's observations on tax reform. E.H. Heeney, President of National Trust

of Toronto, (and one of the "tax advocates") told the annual meeting of shareholders that:

> ...any changes in taxation of our middle income group which would make it more attractive for them to live in another country should be the concern of all Canadians. We should be equally concerned with any taxes that result in a further reduction of personal and corporate savings in this capital-hungry country.[237]

G. Arnold Hart, chairman of the Bank of Montreal, told the Bank's shareholders at their annual meeting that:

> Incredibly, we have a situation where Canadians are being invited to submit to higher taxes, not to pay for programs they have asked for, not even for programs that have been put to them in an election platform, but just because the Government makes a bland assertion that it will need more money and therefore proposes to write itself a blank cheque on the collective bank account.[238]

The very similar opinions of other bank executives found prominent display in newspapers. Bank of Commerce Chairman, N.J. McKinnon told the annual meeting of shareholders that "both the economic consequences of the proposals of the white paper and the principles that underlie them constitute a threat to the Canadian economy and to the people of this nation" and warned of higher interest rates, devaluation of the dollar, depressed living standards for low income groups, and "a general debility of the entire Canadian economy".[239] The address of W. Earle McLaughlin, Chairman and President of the Royal Bank of Canada to shareholders at the annual meeting on January 8, 1970 was printed as a half-page ad in major newspapers, about half of which was an attack on the White Paper's supposed bias against saving and capital accumulation. He singled out the increased burden

on "middle and upper income groups", the capital gains tax, the five-year valuation of corporate shares, and the "artificial" distinction between closely-held and widely-held corporations, all of them to be opposed as (he repeated four times) "taxes on capital accumulation ...when capital is so sorely needed".[240]

Similar statements were made by Bongard Leslie and Co. in their December investment letter,[241] by Harold F. Kerrigan, President of Crown Trust (who also attacked the mining and petroleum proposals)[242] and by Conrad F. Harrington, Chairman and Chief Executive Officer of Royal Trust.[243]

The March 1970 Tax Conference, dedicated to discussion of the White Paper and attended by the Commons Committee, probably sealed the fate of the five-year revaluation proposal, and of the distinction between types of corporations upon which it rested. Practically all speakers not associated with the production of the White Paper who had something to say about these items favoured their withdrawal.[244] Although nearly half of the 47 speakers were either generally favourable or not decidedly opposed to the major proposals in the White Paper, this group included mostly economists and tax professionals who were either linked to the White Paper or the Carter Report, or were university faculty members. Looking only at private sector tax professionals -- those working for corporations, for private-sector associations or in professional firms -- none unequivocably supported all major elements of the White Paper and about two-thirds were opposed.[245] Ten of the 47 speakers -- none of

whom were clearly in favour of the major proposals, although only four were solidly opposed -- were also on our list of "tax advocates".

While few supported the major proposals in the White Paper, the centre of gravity of professional opinion had shifted somewhat from that prevailing in the wake of the Carter Report. A majority of tax specialists speaking at the March 1970 Tax Conference were prepared to accept the idea that capital gains should be taxed, though they quarrelled with the degree of taxation and the method of imposing it.

Out of the almost universal condemnation of the proposal to revalue shares of widely-held corporations every five years, the alternative of deemed realization at death (effectively killed in the reaction against the Carter Report) began to breathe life once more. The context had changed, however: the White Paper was not proposing to bring gifts and bequests into income in the fashion of the Carter Report, and the Estate Tax had already been "reformed". Several speakers at the Conference proposed that deemed realization at death replace the discredited five-year revaluation plan, but that it be combined with the elimination of gift and estate taxes, along with a reduced rate for all capital gains. The integration proposal, also linked to the distinction between types of corporation found little favour compared with some form of dividend tax credit.

The combined weight of professional opinion would have been difficult for any politician to ignore. The federal Conservatives were quick to learn from professional criticism in articulating their

own opposition to major elements of the White Paper, with their Leader, Robert Stanfield touring the country denouncing the increase in tax burden on middle income earners and small business, the failure to provide more generous relief to the poor, the proposals regarding the taxing of corporate capital gains and the taxation of gains on owner-occupied homes. Stanfield also repeated the charges made by financial executives that the proposals were inflationary.[246] The settings for his speeches were (like those of Benson and Robarts) business and professional meetings and banquets, party fund-raising dinners and meetings, and press conferences.

While defending his proposals against what he charged were ill-intentioned interests bent on continuing their exploitation of existing loopholes, Benson always maintained that the legislation would be different if the critics could show better ways to achieve the objectives of tax reform which he had set out at the beginning of the exercise. Occasionally another member of the government or of the Liberal Party would go on the offensive in support of the White Paper. Prime Minister Trudeau denounced the coupon-mailing campaigns to a fifty dollar-a-plate Liberal dinner in Toronto.[247] Most Cabinet ministers however did not feel they understood the White Paper well enough to risk defending it.[248]

Faced with overwhelming opposition on some proposals, Mr. Benson was preparing for strategic retreats well in advance of the parliamentary reports. In a January 6th address to the Canadian Club in Toronto, Benson admitted "Some things in it simply won't

work".[249] While refusing to specify which parts wouldn't work, he did single out which proposals were receiving the most criticism,[250] and, as we have seen, conceded that there might be some problems in the five-year valuation proposal.[251]

At the Tax Foundation Conference at the end of March, Robert Bryce said that the "core proposals" were that personal and corporate taxes be integrated and that capital gains be taxed. The intention was to design a "leak-proof" system, and the government was prepared to make modifications but it was "most desireable ...to preserve the core of the system and adjust other elements in the integrated framework."[252] Benson told a meeting of the Canadian Wholesale Drug Association on April 28th that the Department of Finance was studying ways to provide incentives to new, small businesses with[illegible] continuing the dual corporate rate.[253] Speaking to a Sudbury Chamber of Commerce gathering the same day, Benson said that making provincial mining taxes deductible from income when computing federal taxes was "an idea worthy of consideration."[254]

One of the proposals attracting critical fire was the integration of personal and corporate income, which was perceived by tax professionals as being closely linked to the taxation of capital gains and to the elimination of the dual corporate rate. Accordingly, as in the debate over the Carter Report, those opposed to the taxation of capital gains usually opposed integration. As R.D. Brown, chartered accountant with Price, Waterhouse & Co. explained to a meeting of the Tax Executives Institute (an association of tax administrators in

major corporations and financial institutions) that the most critical issue would be the integration of personal and corporate taxes: "If the Government gives way to a large extent on its proposals in this area, the whole thrust of the white paper will be blunted and major modifications are likely to be made all the way along the line."[255] Although on our list of "tax advocates", Brown took a moderate position, predicting that, although there would be some reduction in economic growth and savings, business would adjust and most people would think tax reform worth the cost.[256]

In a letter to the Commons Committee dated June 11th, Benson introduced a schedule of declining rates applied to the White Paper proposals in the event that they were to be enacted without modification.[257] Modifications which would "substantially reduce the amount available for prospective tax cuts" were being considered by the government, hinting of more concessions to come.[258] This, combined with a refutation of Ontario's revenue estimates a week later,[259] put to rest the controversy over the projected revenues of the proposed tax system, allowing attention to focus more on demands for changes affecting the structure of the tax system.

Appearing before the Committee on August 5th, Mr. Benson said that, while he would accept modifications in the White Paper, three objectives should not be compromised: a capital gains tax, a shift of the income tax burden away from low income-earners, and the elimination of tax loopholes.[260] Permitted by the Commons Committee to question Benson, Robert Stanfield tried unsuccessfully to get

Benson to announce a retreat on the 5-year revaluation of corporate shares, the treatment of small business, income averaging, the capital gains tax on the sale of personal property, and on the taxation of the extractive industries.[261]

Benson's White Paper was not firm government policy and therefore the limits on the behaviour of Liberal Committee members and Members of Parliament were comparatively relaxed. As the extent of opposition to the White Paper became evident, the positions of the Liberal members of the Committee began to diverge. John Roberts and Gaston Clermont defended the White Paper throughout. Barnett Danson and Robert Kaplan, while generally favourable to the White Paper, were more ready to acknowledge the validity of various criticisms.[262] Alastair Gillespie, Patrick Mahoney and Ross Whicher were more often impressed by some of the objections raised by the business and professional critics in the areas of capital gains, integration, small business, and the tax burden on the middle income group."[263] Gillespie told a meeting in February, 1970 of the Ontario Retail Lumber Dealers Association that he had reservations about the White Paper's distinction between types of corporations, the five-year revaluation of corporate shares, and the effects the proposals would have on small business and middle-income groups.[264] During the initial questioning of Department of Finance officials in April, he suggested that, because continuing inflation would increase tax payments, the "less progressive the tax system is made, the better."[265] In May, he disagreed with the proposals to tax capital gains on houses and personal property and wanted to see all capital

gains taxed in the same way with a top rate of 25 per cent. Like most business and professional critics of the White Paper, Gillespie also favoured the existing dividend tax credit system over the integration proposal.[266] While questioning Benson during the latter's appearance before the Committee on August 5th, Gillespie asserted that one national interest which the tax system ought to serve was the development of more multi-national corporations, something not promised in the White Paper.[267]

As with the Liberal members of the Commons Committee, Liberal MP's who were not on the Committee, where they publicly departed from the White Paper, did so in the same direction as most of the business and professional critics. Hyliard Chappell (Liberal, Peel South) was reported in the Globe and Mail as saying that the white paper did not mention incentives and warned about going "too far on the well-meaning but destructive road to socialism."[268]

Lobbying the Minister of Finance:

Private consultations in the Minister's office were a prime focus of interest for many groups.[269] The names of members of Cabinet committees was confidential, encouraging lobbyists to direct almost all their attention to Benson.[270] Benson, of course, would have been the prime target even had they known the other Cabinet Committee members, since the Finance Minister is generally understood to have the overwhelming influence in determining tax policy. On at least one

occasion another minister was approached by one group when it had been told that the concessions they desired were strongly opposed by the Minister in question.[271] When Benson was not available, groups met with departmental officials who avoided being drawn into the debate: "Nothing more than an indication that a group's position had been heard, understood and noted could be given."[272]

The most effective lobbyists were from the mining companies, some of whom had told provincial premiers and Finance officials in Ottawa that certain projects would not go ahead unless the mining proposals were withdrawn. "Some real tough hombres" from head offices in the U.S. came to Ottawa to point out that Canada did not have a monopoly on iron or other minerals.[273] The same message found its way to provincial capitals and was especially effective in Quebec, where newly-elected Premier Bourassa, under pressure to fulfil his election promise of 100,000 new jobs,[274] told the June, 1970 Federal-Provincial Conference of Finance Ministers in Winnipeg:

> Several expansion plans, entailing in total several hundred million dollars, have been postponed or -- so we are told -- are likely never to materialize because of the implications of tax reform.... Quebec cannot afford to lose promising investments in this fashion.[275]

Bourassa's government was in turn regarded by the federal government with more sympathy than some of the other provincial governments demanding similar concessions. Benson went to Montreal on August 6th to listen to Bourassa's argument that several projects were "up in the air" over the uncertainty and timing of tax reform.[276]

The implications of the White Paper's mining proposals for Iron Ore of Canada's plans to build a new pelletizing plant at Sept-Iles in Quebec were discussed by the federal cabinet. Eric Kierans opposed any concessions, arguing that Iron Ore was bluffing and that the company had no choice but to build a new pelletizing plant if their ore was to be of sufficient concentration to be competitive internationally.[277] With most of the cabinet unable to assess Iron Ore's threat, and Mr. Benson arguing for the concessions, the issue was decided over Kierans' objections.[278] In a letter to the provincial premiers on August 26th, Benson said he was prepared to widen the definition of expenditures which would qualify for an "earned depletion" allowance to include processing costs and costs associated with the expansion of existing mines, and to reduce the federal taxes on the mining and petroleum industries from 40 per cent to 25 per cent. This would, according to Mr. Benson, "give the provincial governments the opportunity to bring the taxation of mining profits into line with taxation of profits in other industries...."[279]

In the same letter, Mr. Benson explained why he was not waiting for the reports of the parliamentary committees before making the changes in the White Paper proposals:

> Uncertainty on this subject may be causing the postponement of important projects, particularly in some of the slow-growth regions where the federal and provincial governments are attempting to spur economic activity through other programs.[280]

There was also the forthcoming federal-provincial conference beginning September 17th at which strong pressures for concessions on at least the mining proposals could have been expected from most of the provinces. In an editorial the following day, the Globe and Mail attributed Benson's concessions to provincial pressures resulting from "over $1 billion worth of new projects... [which had] been hanging fire awaiting some clarification from Ottawa", plus the fact that a delegation of Japanese mining company executives, under the sponsorship of Japan's Ministry of International Trade and Industry, was arriving that weekend to meet with Cabinet ministers and senior officials in Ottawa, Ontario, Quebec and British Columbia, and with four major mining corporations.[281]

The immediate industry response to Benson's announcement was mixed. Although Syncrude and the Mining Association of British Columbia were looking for further concessions, most mining and steel executives surveyed by the Globe and Mail were anticipating expanded production and employment.[282] Major beneficiaries mentioned in the Globe and Mail's reporting were: Québec Cartier Mining, a wholly owned subsidiary of United States Steel which was planning a major expansion of properties in Québec; Stelco, which would benefit through its iron mining subsidiaries and in the fact that its planned steel-making facilities on Lake Erie would be eligible for depletion allowances; Dofasco, which was in a similar position to Stelco; Inco; and also mining projects in British Columbia in which Japanese interests had major investments.[283]

The Commons Committee Report:

At the end of the Commons Committee's hearings, it met with its staff in camera for a day to obtain their views on what the Report should contain.[284] In addition, there were private meetings involving Liberal Committee members and Benson,[285] at one of which, Clermont asked the Minister what he would like to see in the Report.[286] The Report was approved by a vote of 10 to 2, with the Liberals voting in favour, the New Democrats against, the Conservatives abstaining, and the Socreds absent.[287]

The Committee said that its Report was based on three principle conclusions:

> 1. That the tax load now borne by lower-income Canadians be reduced....
> 2. That in principle capital gains should be taxed and that the revenue base be expanded in other ways.
> 3. That preservation of an economic climate favourable to growth must be a central consideration of Canadian tax policy. In order to maintain this climate, it is necessary to ensure that those who have acted in good faith in the past are not retroactively penalized. This applies particularly when this past activity has been in the direction of the objectives sought in the proposals.[288]

Although it had listed economic growth as the third objective, the Report, in stating that it was "especially concerned that full consideration be given to the effects of tax reform on economic growth",[289] implied that it was really the foremost objective.

The Commons Committee Report generally followed the White Paper as

far as personal exemptions, deductions and income averaging were concerned.[290] It recommended that the 50 per cent marginal rate begin at $30,000 of taxable income, as opposed to a 51.2 per cent top rate cutting in at $24,000 of taxable income proposed in the White Paper. This was a minor concession to critics (from both left and right) who charged that rates proposed in the White Paper were too high on "middle-income" earners in comparison to higher incomes. The proposed top rate was raised to 60 per cent, cutting in at $60,000 of taxable income.

As expected, the Committee Report discarded the government's distinction between closely-held and widely-held corporations and the proposed five-year revaluation of corporate shares. Capital gains should be taxed only when realized and only half of gains should be included in income and half of losses deductible. In addition, the Committee recommended that there be no deemed realization on gifts and bequests to a spouse, although assets transferred to others would be subject to valuation for capital gains. The Committee also recommended that the impact of the Estate Tax, a frequent target during the White Paper debate, be softened by exempting the first $150,000 and broadening the rate brackets so that the 50 per cent rate applied at $800,000. These were substantial concessions to the majority of professional and business critics.

The Report endorsed the concessions made by Benson to the mining and petroleum interests in August, with some additional minor concessions affecting rules for calculation of depletion allowances.

There were few changes affecting international income with the exception of an extension for an additional three years of the exempt period for tax-free dividends from foreign affiliates, and a grandfather clause to exempt from tax, dividends from projects begun by 1975 and which had been spared foreign tax as a result of incentive legislation in the host country.

The Minority Report:

The New Democratic Party was initially opposed to the White Paper, on the grounds that it did not go far enough to implement the Carter recommendations. However, as the avalanche of business opposition to the government's proposals became apparent, the New Democrats decided that they had better attempt to salvage something in the way of tax reform by supporting the White Paper.[291]

In addition to opposing the majority Report of the Committee, the NDP also issued their own minority report and held a press conference to present the party's position on the White Paper proposals.[292] Saltsman told reporters that although the White Paper proposals were "...an improvement over what we now have, [they] continue to be unfair in their treatment between those whose income stems from wages, salary and pensions, as compared to those whose income arises from investment." Unlike the Committee majority, the NDP members believed that "economic growth and prosperity are, to only a minimal extent,

influenced by the tax system."[293] Though "well-written and well-thought out", the minority report had "absolutely no impact whatsoever on later events."[294]

Conclusion

The Standing Committee hearings were an important part of what was actually the third public debate on tax reform since the Carter Report was published in 1967. As with the previous debates, nearly all the talking was done by tax professionals, business and pro-business lobby groups. Even the government's defence of its proposals was carried out in front of business and professional audiences, those people who stood to lose most from the White Paper's plan to extend the tax base to include capital gains. Fairly typical of the government's attempts to sell its reform proposals to the public was Benson's address to Calgary Liberals at a $50 a plate fund-raising dinner a week following the release of the White Paper. Upon hearing that the increase in the tax burden would be only $17 at the $10,000 income level and $177 at the $15,000 income level for a married man with two children, an angry voice shot back, "You're not talking to that kind of audience".[295]

Having committed itself to the idea of using a white paper to involve the "public" in making tax policy, the government had no choice but to take the parliamentary committees and their hearings seriously. Although Benson was in a position to influence, perhaps control, the content of the Commons Committee Report, the overwhelming

weight of the submissions could be ignored only at the cost of the credibility of the parliamentary committee system and of the government itself. The Carter Commission, while not ignoring the submissions presented to it, had rigerously cross-examined witnesses in the hearings and submitted the written briefs to staff scrutiny to verify their internal consistency and to test them against information obtained from other sources. Having finally adopted a philosophy of taxation at arms-length from the submissions, the Commission's Report then referred back to a number of the submissions from an independent and critical perspective.

As the government had the means to control the workings of the House committees, and had the achievement of the Carter Commission to emulate if it so chose, one must assume that the option was open to it to fashion the Finance Committee in such a way as to permit the Committee to conduct a critical enquiry into what most Canadian taxpayers really wanted out of tax reform, while, at the same time, educating the public to understand the White Paper proposals. The Committee's failure to use its professional staff to full advantage, to solicit independent specialist testimony, to form a "pro-reform" majority to include the two NDP members (who did, after all, agree with many of the government's proposals), and its acquiescence in allowing business lobbyists to monopolize the public hearings, all support the conclusion that the Committee was used by the government to conduct a graceful retreat from the recommendations of the Carter Commission.

The rhetoric of "participatory democracy" fitted in well with such a scenario: It would have been politically costly for the government to openly concede to business pressure not to implement the Carter recommendations. The government came close to such a concession at the end of 1967, as indicated in Mitchell Sharp's budget speech of November 30, 1967.[296] Mr. Benson's indecision over whether to produce a draft bill or a white paper signaled continued division in Cabinet on the substance and the strategy of tax reform. The political merit of the white paper route was that it promised to preserve much of the reform-minded and populist image of the new Trudeau government by appearing to place it on the side of tax reform and also appearing to be asking "the people" to decide for themselves what sort of tax reform they wanted.

At the same time, the White Paper, and Benson's repeated assurances to business and professional audiences that the proposals were subject to change in the light of taxpayer criticism, were a signal for mobilization to those who stood to lose from a tax system reformed along the lines of the White Paper. As David Lewis later expressed it, "The release of the White Paper was the first offer in a complex negotiation."[297] "Big business", and businessmen who tried to appear small to the tax collector by spreading their holdings over many small corporations, had all they needed to sustain a concerted campaign against the reform proposals: a very substantial tax incentive; the wherewithal and opportunities to retain expert assistance and to propagate their views; and the promise of success in the government's commitment to alter its plans in light of public

criticism and of the parliamentary reports.

There was no comparable counter-mobilization from the approximately three million taxpayers at the low end of the income scale which the White Paper predicted would benefit from the government's reform proposals. This was partly as result of the failure of the White Paper to go the full distance with the Carter Commission majority in recommending the comprehensive tax base, thus earning only a reluctant and belated support from the New Democratic Party and organized labour. In addition, these pro-tax reform forces did not enjoy the analytical and propaganda resources available to the business and professional opponents of tax reform. Most academic tax specialists found it difficult to wax enthusiastic over what they regarded as a flawed and weaker cousin to the Carter Report.

Of at least equal importance, is the assymetry of the tax incentives facing the opposing sides in the debate: the high-income investor stood to lose many thousands of dollars annually, while most wage- and salary-earners could hope to gain at most only $131, and some skilled workers would actually lose a few dollars.[298] For most taxpayers, therefore, the monetary incentive to make the effort to become informed was not great, and for the majority of working people not accustomed to discussing the finer points of capital gains and capital cost allowances, the effort required would have been substantial. It is not surprising that Mr. Benson did not have to run gauntlets of angry workers in order to try (unsuccessfully) to persuade gatherings of businessmen and professionals of the need for

tax reform.

In spite of the efforts undertaken by the government and by opponents of the White Paper to communicate their ideas to the public, an opinion poll taken two months after release of the document indicated that only 52 per cent had even heard of it.[299] A special poll commissioned by Colin Brown in June, 1970 indicated that, after more than seven months of "public debate" the percentage of respondants aware of the White Paper had only increased to 57 per cent.[300] Of these, 48 per cent "disapproved" of the White Paper, while only 30 per cent "approved". As one would expect, the level of awareness was higher in Western Canada, among upper and middle-income groups, executives and professionals, and was lowest among lower income groups and labour.[301] In defending his reform proposals Mr. Benson often referred to the "silent majority" who would benefit from tax reform. Many were silent, the polls suggest, out of ignorance of the government's proposals.

In addition, many lower-income people, while being aware of the existence of the White Paper, and possessing perhaps some vague idea of its content, might have been confused regarding its significance for the interests of people in their general situation. Given the normal lack of technical sophistication among people subject to low marginal rates of tax deducted at source, one would expect many of the lower-income earners, intended by the government to benefit from its proposals, to accept at face value much of the propaganda directed against the White Paper. This would tend to be more so, if the

attacks were repeated frequently by many critics who appeared to speak with some authority on the subject. As we have seen, this was, indeed, the general character of the White Paper debate.

Given the composition and mode of operation of the parliamentary committees, their reports would have had to reflect in some measure the weight of testimony before them. In the case of the Senate Committee, this consideration could only have reinforced the senators' pro-business instincts. This would also have been the case for the Conservative members of the Commons Committee, and for some of the Liberal members as well. For the Liberal members, however, such an inclination was countered by a reluctance to oppose the government's proposals, which, although not established policy, were linked nevertheless to the prestige of the government. Only the two NDP members were strongly committed to a version of tax reform at least as progressive as that proposed in the White Paper. It is not surprising therefore, that the exercise in public participation supposedly performed through the Committee hearings worked to further modify the tax reform agenda in favour of a small and privileged minority of Canadian taxpayers and foreign investors.

The behaviour of the Senate Standing Committee on Banking, Trade and Economic Affairs was, throughout the White Paper episode, entirely consistent with its social composition. The composition and dynamics of the Commons Committee were more complex, however. Although weighted in composition toward the business and professional classes, the ambiguous constraints and loyalties of the Liberal members and the

presence of two New Democratic Party members made the outcome of its deliberations more problematic. Other studies of the workings of this Committee and of its meaning for the concept of "participatory democracy", have treated the influence of the government on its party's members on the Committee as one of several factors limiting the approximation to participatory democracy which was achieved.[302] While one would expect the constraints exercized by government on its backbenchers, in general, to be a factor limiting genuine public participation in policy formation, this does not appear to have been the case for the White Paper debate. The "public participation" which the parliamentary committees nurtured was confined to the top veneer of society. What government-imposed limitations the Liberal members may have felt on their freedom of action would simply have limited the extent to which they could concede to the demands of this tiny proportion of the Canadian electorate.

Some participants in the tax reform process have noted that the behaviour of the Liberal members of the Commons Finance Committee, and hence the Committee itself, may have been influenced by the consideration of their future prospects with the government.[303] It would appear that the government was not disappointed with the Committee's report, as five former Liberal members had been appointed as parliamentary secretaries by 1972,[304] and Robert Kaplan had become Chairman of the Finance Committee. Three members who had played a major role in drafting the Report, Danson, Kaplan and Gillespie, later joined the Cabinet.[305] In a recent interview, Mr. Benson confirmed that he was pleased with Gaston Clermont's conduct of

the Committee's work on the White Paper.[306]

The great political value for the government of the apparent independence of the Commons committee was that, in listening to the complaints against the White Paper and in recommending changes, the government could make a graceful retreat from tax changes it would not have dared to put into a budget, or have survived, had it been so foolhardy. The Department of Finance and Mr. Benson were anxious to avoid the débâcle of Walter Gordon's first budget, which unsuccessfully attempted to introduce a narrower range of changes.[307]

Mr. Benson agreed that the Committee did allow a graceful retreat on some points, but that the whole logic of the white paper process necessitated concessions from the government:

> You couldn't possibly start from the position you hoped to end up at. Some concessions are essential because the whole rationale was to consult the people. If no concessions were made, the process would lack credibility.[308]

However, when it came to the mining provisions, such a graceful concession was not open to the government. Mr. Benson felt he had no choice but to write to the provincial premiers five weeks prior to the Commons Report, in order to "clear up" the uncertainty generated by the White Paper and allow long-term mining projects which hinged on the tax system to go ahead.[309] The force majeure of large-scale capital investment could not pause to allow the fig leaf of parliamentary etiquette to be put into place.

A number of factors affecting the operation of the Commons

Committee, notably the late arrival of the staff and its marginal impact on the questioning of witnesses, the decision to tour the country and not to invite independent specialist testimony, and the partisan divisions within the Liberal-controlled Committee, all contributed to making the hearings ineffective in extending the scope of participation beyond the customary circle of businessmen and professionals.[310]

Of more enduring significance are socio-economic factors and the characterics of the existing tax structure,[311] which account, not only for the narrow scope of participation in the White Paper debate, but also for the same phenomenon noted in previous chapters in the contexts of the placing of tax reform on the political agenda and in the campaign to discredit the Carter Report.[312] The historical legacy of the imposition of a tax system with nominally high, progressive rates combined with significant exemptions, incentives, loopholes and ambiguities was the development of a high degree of tax consciousness and competence among taxpayers in the high income brackets. Anyone expecting to have to pay 81 cents out of the next dollar he received had a powerful incentive to look for a way to avoid the tax, or to hire someone else who had already travelled what Eisenstein called the "highways and byways of tax avoidance." A growing fraternity of tax practitioners, nurtured by the tax structure and the fees of willing clients, developed the professional institutions, networks and influence which enabled it to shape the tax system on which it depended. Even the chief protagonist of the White Paper, referring to spreading investments through a number of small

companies in order to take maximum advantage of the 21 per cent rate of corporate tax, told the Ottawa Chartered Accountants Association, "A lot of us, including myself a long time ago, make our living trying to do this."[313]

To the tax professionals, participation in the formation of tax policy was a democratic right, a professional obligation, and for many, an occasion for earning another honest dollar. As we have seen, they did participate and with clearly perceptible results. By October, 1970, however these results were only provisional, consisting of two parliamentary committee reports and several undertakings by the government to modify certain White Paper proposals. It was widely expected that the end of tax reform would see a capital gains tax, but not the taxation of unrealized share gains, and perhaps a reduction in the Estate Tax. The fate of integration was still uncertain.

As the government prepared its draft legislation, the economy slipped into a recession. Then, the hostage-takings by the Front de Libération Québécois in Montreal diverted public attention away from tax reform, while providing a dramatic demonstration for those arguing that tax incentives were essential to restore prosperity and to promote social stability.

Notes to Chapter VII

1. "Seeks early action on Carter -- Benson plans fundamental tax changes in first budget", The Globe and Mail (Toronto), April 24, 1968.
2. Ibid.
3. House of Commons Debates, Oct. 23, 1962, p. 863; cited by Doerr, p. 129.
4. "The financial facts, please", The Globe and Mail (Toronto), April 26, 1968.
5. See above, Ch. 6, pp. 487-488.
6. House of Commons Debates, Sept. 16, 1968, p. 51.
7. Department of Finance, "Notice of Ways and Means Motion -- Income Tax Act and Estate Tax Act", Oct. 22, 1968; House of Commons Debates, Oct. 22, 1968, p. 1913.
8. House of Commons Debates, Feb. 5, p. 5180; "Text of a speech by the Honourable E.J. Benson ...", Department of Finance, News Release, Feb. 5, 1969.
9. House of Commons Debates, Jan. 30, 1969, p. 4929; Department of Finance, News Release 69-12, Jan. 30, 1969, p. 2.
10. Ibid.
11. Ibid.
12. House of Commons Debates, Feb. 5, 1969, p. 5179; Department of Finance, News Release, Feb. 5, 1969, p. 2.
13. Ibid.
14. Ibid.
15. House of Commons Debates, Feb. 5, 1969 p. 5179; "Text of a speech by the Hon. E.J. Benson ...", Department of Finance, News Release, Feb. 5, 1969; E.J. Benson, "Budget Proposals on the Estate Tax and Gift Tax", Department of Finance, News Release No. 69-12, Jan. 24, 1969.
16. "Statement by the Minister of Finance ...", Department of Finance, June 24, 1969.
17. Ibid.
18. Meyer Bucovetsky and Richard M. Bird, "Tax Reform in Canada: A Progress Report", National Tax Journal, Vol. 25, (Mar: 1972), p. 18;
19. Senate Standing Committee on Banking, Trade and Commerce, Minutes of Proceedings and Evidence, June 18, 1969.
20. "Budget Proposals -- Income Tax Act", Department of Finance, News Release, April 28, 1969.
21. "Statement by the Minister of Finance to the Standing Committee of the Senate on Banking, Trade and Commerce Concerning Income Taxes on Life Insurance Companies", Department of Finance, June 24, 1969.
22. Ibid., p. 10.
23. Bucovetsky and Bird, p. 18.
24. Bryce interview.
25. House of Commons Debates, Jan. 21, 1969, p. 4547.
26. House of Commons Debates, Jan. 21, 1969, p. 4547-8.
27. House of Commons Debates, Feb. 6, 1969, p. 5213; quoted by Edward

S. Goldenberg, Parliamentary Committees and Policy Formation: A Case Study of the Role of the House of Commons Standing Committee on Finance, Trade and Economic Affairs in the Process of Tax Reform in Canada, (McGill University, MA thesis, 1971), p. 38.

28. Goldenberg, p. 38.
29. Doerr, p. 131; Goldenberg, p. 40, encountered the same explanation but called it "face-saving".
30. Interview with Donald R. Huggett, Montreal, May 3, 1983.
31. Interviews with F.R. Irwin and E.R. Smith both support this interpretation.
32. Bryce interview.
33. See Ch. 6, above, pp. 486-487.
34. Benson interview.
35. Doerr, p. 130; Goldenberg, p. 38.
36. House of Commons Debates, Feb. 21, 1969, p. 5797; Doerr, p. 130.
37. Statement by the Hon. Edgar Benson, Minister of Finance, House of Commons Debates, Oct. 22, 1969, p. 11690.
38. Huggett interview.
39. Thompson, Orchard and Huggett interviews.
40. Bryce interview.
41. House of Commons Debates, Oct. 22, 1969, p. 11690.
42. Benson interview.
43. Kierans and Benson Interviews. Additional names given by Mssrs. Kierans and Benson did not coincide, suggesting one or both men were confusing participation in the Committee discussion with that in full Cabinet.
44. Doerr, p. 132.
45. Kierans interview, Dec. 5, 1983.
46. Thompson, Orchard, and Bryce interviews.
47. Ibid.
48. Kierans interviews; Kierans, "Problems of tax reform", Canadian Taxation Vol. I, No. 4 (Winter, 1979) p. 23.
49. Kierans interview, April 28, 1983.
50. Ibid.
51. Ibid.
52. Ibid.
53. Benson and Kierans interviews.
54. Ibid.
55. Doerr, p. 132.
56. Kierans interview, Dec. 5, 1983.
57. Ibid.
58. Kierans interview.
59. Ibid.
60. Interviews with current and retired Department of Finance officials.
61. (Ottawa: Queen's Printer, 1969), is hereafter referred to as the White Paper.
62. Ibid., p. 6.
63. Ibid.
64. Ibid., p. 7.
65. Ibid., p. 36.
66. Ibid., p. 37.
67. Ibid., pp. 37-38.

68. Ibid., pp. 38-39.
69. Ibid., p. 39.
70. Ibid., p. 52.
71. Ibid., pp. 41, 53.
72. Ibid., p. 41.
73. Ibid., p. 41.; See Ch. 5, above, pp. 288-289.
74. White Paper, p. 42
75. See the discussion of Beauvais' and Grant's minority reports, Ch. 5, above, pp. 339-341, 345-349.
76. White Paper, p. 43.
77. Ibid., pp. 14-15.
78. Ibid., pp. 17-18.
79. Ibid., Table 4, p. 27, and Table 6, p. 29.
80. Ibid., Tables 4-9, pp. 27-32.
81. Ibid.
82. Royal Commission on Taxation, Report, Vol. II, Appendix I. The Report acknowledged that the rate schedule for unattached individuals "would result in modest tax increases for individuals at the bottom of the scale whose taxable income would not be increased by our other proposals." Vol. II, Ch. 11, p. 201.
83. White Paper, pp. 8-9.
84. Ibid., pp. 48-49.
85. Ibid., pp. 50-51.
86. Ibid., p. 47.
87. Ibid., p. 57.
88. Ibid., pp. 54-55.
89. Ibid., pp. 57-58.
90. Ibid., p. 58.
91. Ibid., pp. 60-61.
92. Ibid., pp. 61-63.
93. Ibid., pp. 65-66.
94. Ibid., pp. 66-67.
95. Ibid., pp. 67-68.
96. Ibid., p. 68.
97. Ibid., p. 69.
98. Ibid., pp. 69-70.
99. Ibid., pp. 71-72.
100. Ibid., p. 72.
101. Ibid.
102. Ibid., pp. 73-74.
103. Ibid., p. 74.
104. Ibid., pp. 74-75.
105. Ibid., pp. 76-77.
106. Ibid., p. 78.
107. Ibid., p. 78.
108. Ibid., p. 80.
109. Ibid., p. 82.
110. Ibid., p. 83.
111. Ibid., p. 84.
112. Ibid., pp. 85-87.
113. Ibid., p. 93.
114. Ibid.
115. Ibid., p. 95.

116. A Special Joint Committee had been created the previous July, but was criticized by the New Democratic Party for including Senators with many corporate directorships and hence with conflicts of interest. Although the criticism was not explicitly accepted by the Government, the mandate and existence of the Joint Committee expired at the end of the Session. Goldenberg, p. 49.
117. Robert J.L. Gardner, The Politics of Reform: Class Interests and Tax Reform in Canada, 1960-1971 (Hamilton: McMaster University, Ph.D. Thesis, 1984) p. 825.
118. Wallace Clement, The Canadian Corporate Elite, (Toronto: McLelland and Stewart, 1975), pp. 172-173, 400-428. Clement lists a total of 384 "dominant" (having assets of greater than $250 million and income of over $50 million) and "middle-range" (over $50 million in assets and $10 million in sales but not meeting the criteria for dominance).
119. Ibid., pp. 159-164.
120. Unless otherwise indicated, information concerning the affiliations of parliamentary committee members is drawn from the Parliamentary Guide of the appropriate year, supplemented with information from the Financial Post Directory of Directors.
121. K.Z. Paltiel, Political Party Financing in Canada, (Toronto: McGraw-Hill, 1970) p. 35.
122. K.Z. Paltiel and J.B. Van Loon, "Financing the Liberal Party, 1862-1965", in Committee on Election Expenses, Studies in Canadian Party Finance (Ottawa: Queen's Printer, 1966), p. 192; Reginald Whitaker, The Government Party: Organizing and Financing the Liberal Party of Canada 1930-58, (Toronto: University of Toronto Press, 1977), p. 198.
123. Joseph Wearing, The L-Shaped Party, pp. 58-64; Paltiel, Political Party Financing in Canada, pp. 33-35; Whitaker, The Government Party pp. 196-206.
124. Noted by Colin Campbell, The Canadian Senate: A Lobby from Within (Toronto: Macmillan, 1978), p. 48.
125. Campbell, pp. 19-21.
126. The Commons Committee hearings are discussed below, pp. 551-564.
127. Doerr, p. 202.
128. Gardener, p. 829. Doerr, p. 202, describes Hayden as "an outspoken and strong defender of private business interests and who was opposed to many of the White Paper proposals."
129. "Tax reform hearings to start Wednesday", The Globe and Mail (Toronto), Jan. 24, 1970, p. 2.
130. "White paper proposal assailed as Victorian, ruthless and inept", The Globe and Mail (Toronto), Mar 5, 1970, p. B5.
131. This was observed by Gardner, pp. 829-831, and is consistent with the more general observations of Campbell, pp. 10-19.
132. Senate Standing Committee on Banking, Trade and Commerce, Report on the White Paper Proposals for Tax Reform Presented to the Senate of Canada (XXth Report, 1969-70 Session).
133. "The servants of privilege", The Globe and Mail (Toronto), Oct. 2, 1970, p. 6.
134. Goldenberg, p. 54, offers this assessment of the Liberal representatives: "What can be said without fear of contradiction

is that an outpouring of excess radicalism would have been surprising from the Liberal members of the Committee." C.E.S. Franks, "The Dilemma of the Standing Committees of the House of Commons", Canadian Journal of Political Science Vol. 4, No. 4 (Nov.-Dec., 1971), p. 476, called the members from the two major parties on the Committee "mainly small 'c' conservatives."

135. Goldenberg, p. 54.
136. Ibid.
137. Goldenberg, p. 56.
138. This conclusion is shared by Goldenberg, p. 56.
139. Goldenberg, p. 56; Bryce, Huggett, Robertson and Kierans interviews.
140. Standing Committee of the House of Commons on Finance, Trade and Economic Affairs, Minutes of Proceedings and Evidence, Jan. 15, 1970, pp. 12:68 - 12:73; Goldenberg, pp. 60ff.
141. Goldenberg, p. 129.
142. Bucovetsky and Bird (p. 21) believe that the Committee staff was inadequate to critically assess the briefs and testimony, whereas Goldenberg (p. 129) concludes that the Committee simply didn't make effective use of its excellent staff.
143. See Ch. 2, above, pp. 81-83.
144. D.Y. Timbrel and H. Anson-Cartwright, The Taxation of the Mining Industry in Canada, Royal Commission on Taxation, Study No. 9, Ottawa: Queen's Printer, 1967.
145. Brown appeared before the Committee May 28 on behalf of McIntyre Porcupine Mines, and June 1st on behalf of the Canadian Institute of Chartered Accountants. Timbrell represented Rio Tinto Zinc before the Committee on June 15th.
146. Report of the Twenty-second Tax Conference, (Toronto: Canadian Tax Foundation, 1971), and Standing Committee of the House of Commons on Finance, Trade and Economic Affairs, Minutes of Proceedings and Evidence, Mar. 4, 1970, p. 25:4.
147. Robertson and Huggett interviews.
148. Huggett interview.
149. Standing Committee of the House of Commons on Finance, Trade and Economic Affairs, Minutes of Proceedings and Evidence, Jan. 20, 1970.
150. Standing Committee of the House of Commons on Finance, Trade and Economic Affairs, Minutes of Proceedings and Evidence, Reports 13, 16, 18, 25, 91 and 92; (April 7, 9, 14, 16, 1970).
151. Standing Committee of the House of Commons on Finance, Trade and Economic Affairs, Minutes of Proceedings and Evidence, Jan. 20, 1970, p. 13:9.
152. Bryce interview.
153. Ibid.
154. Standing Committee of the House of Commons on Finance, Trade and Economic Affairs, Minutes of Proceedings and Evidence, June 1, 1970, p. 49:4.
155. Goldenberg, p. 152.
156. Ibid., p. 135.
157. Meyer W. Bucovetsky and Richard M. Bird, "Tax Reform in Canada: A Progress Report", National Tax Journal, Vol. XXV, No. 1, (March, 1972), p. 21.

158. C.E.S. Franks, "The Dilemma of the Standing Committees in the Canadian House of Commons", Canadian Journal of Political Science Vol. 4, No. 4 (Nov.-Dec., 1971) pp. 461-476, esp. p. 476; John G. Head, "Canadian Tax Reform and Participatory Democracy", Finanzarchiv Vol. 31, No. 1 (1972) pp. 67-68; Goldenberg, p. 68; Gardner, pp. 811, 836; Doerr, "The role of white papers", p. 197; M.W. Bucovetskey, p. 98.
159. This point was also made by Gardner, p. 811.
160. See Eighteenth Report of the Standing Committee on Finance, Trade and Economic Affairs Respecting the White Paper on Tax Reform, Standing Committee of the House of Commons on Finance, Trade and Economic Affairs, (Ottawa; Queen's Printer, 1970). Figures are compiled from the published index of witnesses and briefs received, Appendices "A" and "B", Minutes of Procedings and Evidence, Standing Committee of the House of Commons on Finance, Trade and Economic Affiars, pp. 93:192-93:218.
161. These figures include primary metal producers with significant mining interests.
162. Bucovetsky (p. 98) judged 43 witness groups or 20 per cent of the total, "to have been primarily interested in overturning the mineral tax proposals".
163. Interviews with D.G. Hartle, D.R. Huggett, J.H. Perry, Ronald Robertson, and others. See also Gardner, p. 811.
164. This active subset of tax professionals does not include a number of the "big names" in taxation: some of whom were advising one of the parliamentary committees, governments or business clients and therefore did not appear before the Committee.
165. Professional qualifications were obtained from the lists cited above, and from the Canada Law Directory for 1970, published by the Canadian Bar Association, the 1969 Directory of Chartered Accountants, published by the Canadian Institute of Chartered Accountants, and the 1970 Financial Post Director of Directors.
166. While it is true that DOFASCO and Alcan were primarily engaged in basic metal production, as vertically integrated companies, they had significant interests in the extractive industries.
167. See above, Ch. 6, pp. 411-412, 443-444.
168. Wearing, pp. 62-63.
169. Goldenberg, pp. 68, 135.
170. A residual category of unclassified groups accounts for two additional cases. Some groups were classified under two categories, resulting in a total greater than 211.
171. Bucovetsky and Bird, "Tax Reform in Canada: a Progress Report", National Tax Journal Vol. 25 (Mar., 1972), p. 23.
172. Goldenberg, p. 88.
173. Goldenberg, p. 87; Gardner, pp. 775-785.
174. Gardner, p. 784.
175. Some more blatant examples from the Globe and Mail are: "Proposed reforms termed modified Carter report -- Brinco head assails white paper as not promoting growth", (a report of a speech by Alfred Powis, President of Noranda Mines), (Nov. 11, 1969), p. B3; "[Carter] Plan held deterrent to mines", (Jan. 30, 1970), p. B1.; "Tax incentives termed vital to mine growth",

(Feb. 13, 1970), p. B3; "President of drilling association blames tight money, tax worries for slowdown", (Feb. 21, 1970), p. B5; "Hudson Bay capital may go if tax passed", (May 1, 1970), p. B12; "White paper threat to Syncrude stressed by Imperial Oil head", (April 4, 1970), p. B1; "Mines brief states tax would kill incentive", (April 16, 1970), p. B3; and "White paper may cut Shell's explorations", (April 23, 1970), p. B5.

176. Goldenberg, pp. 88-89; Gardner, pp. 801-803.

177. The Committee did not publish any material received from Newfoundland, Nova Scotia and Manitoba, and did not receive submissions from British Columbia and Prince Edward Island. Goldenberg, p. 91.

178. "MacNaughton hopes talks with Ottawa will make provincial income tax system unnecessary", The Globe and Mail (Toronto), Nov. 11, 1969, p. B9.

179. Ibid.

180. Ibid.

181. "Premier is willing to drop death duty for gains tax", The Globe and Mail (Toronto), Dec. 8, 1969, p. 9.

182. Ibid.

183. "Tax proposals again assailed by Lawrence, (Jan. 29, 1970), p. B6.

184. "White Paper called damaging -- Economy could be retarded by tax plan, Robarts claims", The Globe and Mail (Toronto), Feb. 11, 1970.

185. Ibid.

186. Ibid.

187. Ibid.

188. Ibid.

189. "Builders told economic growth would be victim of white paper", The Globe and Mail (Toronto), Feb. 12, 1970.

190. Frances Russell, "Attack on tax reform reveals an old stand", The Globe and Mail (Toronto), Feb. 14, 1970.

191. "Benson strikes back, calls for defeat of Robarts Cabinet", (Feb. 21, 1970), p. 4.

192. Ibid.

193. "Ontario wants Canada to follow U.S. trends in taxation reform", The Globe and Mail (Toronto), May 5, 1970, p. B2; Standing Committee of the House of Commons on Finance, Trade and Economic Affairs, Minutes of Proceedings and Evidence, June 23, 1970, pp. 70:7-70:106 and 70:131-70:184.

194. "Proposed tax exemptions please Beaulieu", (Nov. 12, 1969), p. B5.

195. Ibid.

196. See Standing Committee of the House of Commons on Finance, Trade and Economic Affairs, Minutes of Proceedings and Evidence, Aug. 4, 1970, pp. 90:126-149.

197. "Thatcher against tax plan: pledges to lead western opposition", (Nov. 15, 1969), p. B1.

198. Ibid.; "Would Weigh Liberalism over tax plan: Thatcher", (Feb. 18, 1970), p. 4.

199. "Ontario supports tax reform but suggests other alternatives", The Globe and Mail (Toronto), Dec. 13, 1969.

200. Ibid.
201. "N.S. asserts white paper plans would sharply reduce tax base", The Globe and Mail (Toronto), Feb. 4, 1970, p. B2.
202. Ibid.
203. Standing Committee of the House of Commons on Finance, Trade and Economic Affairs, Minutes of Proceedings and Evidence, Aug. 6, 1970, pp. 92:39-92:131.
204. Standing Committee of the House of Commons on Finance, Trade and Economic Affairs, Minutes of Proceedings and Evidence, July 22, 1970, pp. 76:7-76:23 and 76:152-76:160.
205. Standing Committee of the House of Commons on Finance, Trade and Economic Affairs, Minutes of Proceedings and Evidence, July 20, 1970, pp. 74:161-74:175.
206. Eighteenth Report of the Standing Committee of the House of Commons on Finance, Trade and Economic Affairs, p.93:184.
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211. "Tax on unrealized gains most vexing proposal for Benson", The Globe and Mail (Toronto), Nov. 28, 1969, p. B2; see for example, the remarks of Benjamin Swirsky, Tax Manager for the Toronto office of Peat, Marwick, Mitchell & Co, "Competitive position of industry could be limited by tax changes", The Globe and Mail (Toronto), Nov. 28, 1969, p. 5.
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215. "Small business groups organize to fight white paper proposals", The Globe and Mail (Toronto), Dec. 19, 1969, p. B2.
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294. Goldenberg, p. 143.
295. "Angry Albertans tell Benson tax will destroy incentives", The Globe and Mail (Toronto), November 15, 1969, p. B1.
296. See Ch. 6, above, pp. 483-484.
297. Lewis, Louder Voices, p. 101.
298. White Paper, Tables 4-6, pp. 27-29.
299. Doerr, "The Role of White Papers", p. 194. Doerr refers to a January 1970 poll by the Canadian Institute of Public Opinion.
300. Ibid. The poll was also conducted by the Canadian Institute of Public Opinion.
301. Ibid.
302. Goldenberg, pp. 138-145; A. Doerr, "The Role of White Papers", in G. Bruce Doern and Peter Aucoin eds., The Structures of Policy-Making in Canada, (Toronto: Macmillan, 1971) pp. 179-203, esp. p. 196; C.E.S. Franks, "The Dilemma of the Standing Committees in the Canadian House of Commons" Canadian Journal of Political Science, Vol. IV, No. 4 (Dec., 1971.), p. 461-476.
303. Kierans, Huggett interviews.

304. Clermont, Gillespie, Danson, Mahoney and Roberts.
305. Gardner, p. 882-3. Gardner's source for their role in drafting the Report was The Globe and Mail (Toronto), Oct. 6, 1970.
306. Benson interview.
307. Gordon himself cautioned Benson to take a more cautious, incremental approach to tax reform, "...as this would tend to provoke too many people on too many issues." Correspondance with the author, Sept. 16, 1982. Eric Kierans (who, as President of the Montreal Stock Exchange, had helped to defeat Gordon's budget) attributes to this memory the anxiety of Finance to avoid getting into a similar predicament. Kierans interview. See Ch. 3, above, pp. 224.
308. Mr. Benson maintains, however, that he was very reluctant to take the white paper route and that moving directly to one or more pieces of legislation would have been faster and no less effective. Benson interview.
309. Benson, Bryce interviews.
310. These points are raised by Goldenberg, p. 89; 130-138.
311. The latter are described above, in Ch. 2.
312. See above, Ch. 2, pp. 117-118, and Ch. 6, esp. pp. 489-490.
313. "Benson counters business criticism of tax reforms", The Globe and Mail (Toronto), Dec. 18, 1969.

Chapter VIII: 1971 Tax Reform Legislation (Bill C-259)

Introduction:

The drafting of the tax reform legislation concluded the white paper process and signalled a return to the customary announcement of tax changes in the budget speech of the Minister of Finance, later presented in detail as proposed amendments to the taxation statutes.[1] However, these changes to the Income Tax Act went well beyond the normal number and range of annual budgetary amendments. This budgetary phase was distinguished from the white paper process in that the government appeared to be firmly committed to a specific policy which was spelled out in legislation. Although interested groups and individuals were expected to, and did make their views known, this "public participation" was far less overt than in the earlier phase.

The views of "the public" on tax reform had been heard and it was now time for the government to conclude the process by concrete legislation. Opportunities for further amendments, subject to the customary limits of parliamentary procedure, were still available, and concessions were made in response to further pressure applied through the Department of Finance, the Liberal Caucus, opposition parties, business and professional associations, and the mass media. As in the earlier stages of the reform process, the tax professionals, acting on

behalf of their professional associations, and as advisors to corporations and business groups, constituted the dominant source of non-governmental influence on the decision-making process.

Bill C-259 marked a further retreat from the tax reform agenda sketched out by the Carter Commission. The comprehensive income concept was demoted to an ideal shared by academic tax specialists, and comprehensive tax reform was replaced by what most tax professionals regarded as a modification of the existing system in the direction of the American system of taxation of capital gains at a preferential rate. The changes to Bill C-259 during its passage through Parliament, while ostensibly directed toward the solution of reputedly technical problems in the legislation, involved further concessions to domestic and foreign investors as well as undisguised concessions to the co-operative movement. Despite these additional compromises closure had to be invoked to secure the bill's final passage through the House of Commons. The Senate's reluctant approval was secured only with the promise of future adjustments in favour of investors.

Main Features of Bill C-259

Drafting of the tax reform legislation began in the fall of 1970. Charged with this task were J.R. Brown, F.R. Irwin, John Thompson, Douglas Andison (a tax lawyer with the Tax Policy Division), R.F. Lindsay (on loan from the Department of Justice), M.A. Cohen, and Dave

Pook, Director General for Tax Policy at the Department of National Revenue. This committee reported through the Deputy Minister, Simon Riesman, to the Special Cabinet Committee on Taxation.

The main features of the reformed system were announced in the House of Commons by Mr. Benson in his "tax reform budget" of June 18, 1971, and tabled in the customary form of a Notice of Ways and Means Motion. On June 30th, following a six-day budget debate, Bill C-259 was given first reading. The House then adjourned for the summer recess and did not reconvene until September 7, 1971.

The bill proposed to include half of realized capital gains in taxable personal income, with half of capital losses being deductible within specified constraints.[2] The tax would cover all financial assets, all real property except owner-occupied principle residences, and non-depreciable personal property in excess of $1,000 per item.[3] Gains would normally be taxed only on realization, except that there would be deemed realization on gifts and bequests.

Citing the recommendations of the Commons Finance Committee to reduce the weight of the Estate Tax in recognition of the "substantial tax impact arising on the death of a taxpayer",[4] the government decided to follow the advice of the Senate Banking Committee that the federal government vacate the estate tax field entirely in favour of the provinces. The government's rationale for this was that the tax netted the federal government only negligible revenue. Moreover, since 75 per cent of the approximately $200 million collected annually

was turned over to the provinces (two of which already refunded the tax to the estates), it was no longer possible for the federal government to ensure horizontal equity in the taxation of bequests. Bequests or transfers between spouses would not be subject to deemed realization, but on disposing of the assets, the surviving spouse would be subject to capital gains tax based on the original cost value to the deceased spouse.[5]

With regard to corporate income, the White Paper's integration proposal was scrapped and replaced by a dividend tax credit increased from 20 per cent to 33 1/3 per cent, and the amount included in income before the calculation of tax payable in order to give it some measure of progressivity.[6] The new bill ignored the criticism of the existing dividend tax credit in the Carter Report and the White Paper that the credit had been available to all "taxable Canadian corporations" regardless of whether or not any tax had actually been paid.[7] This meant that the shareholders of "foreign business corporations", such as Brascan, and mining and petroleum companies which reduced or eliminated their tax payable through depletion allowances, would continue to be eligible for the dividend tax credit to offset a non-existent corporate tax burden.

The rate of tax on corporate income was set at 50 per cent, to be reduced by one percentage point a year to 46 per cent in 1976.[8] The bill incorporated an incentive for new small businesses, featuring a special low rate of 25 per cent on the first $50,000 of taxable corporate income of Canadian-controlled private corporations. To

prevent some of the tax avoidance schemes which had taken advantage of the old dual corporate rate, the new incentive would not be applicable to investment income, nor to public or foreign-controlled corporations; it also had a built-in self-destruct feature in that it expired after the corporation had earned a total of $400,000 of taxable income.[9]

Concessions to mining interests previously announced by Mr. Benson were justified on the grounds of the need for:

> substantial tax incentives... to recognize the risks involved in exploration and development, the international competition for capital and the levels of incentives available in other countries.[10]

Among the more notable provisions affecting business income, was the full deduction allowed to corporations for interest paid on loans used to buy other corporations, effectively committing the government to paying about half the interest charges for all future corporate mergers. This stimulus to further concentration of Canadian corporate capital was justified by the government in terms of promoting greater Canadian ownership of the economy:

> This deduction for interest provides a substantial incentive for Canadian corporations to invest in other corporations and permits them to compete on an even footing with foreign corporations. Assuming a tax rate of 50 per cent, the cost of borrowing money for share purchases will be cut in half.[11]

Other business income provisions included the continued deductibility of convention expenses within specified limits, treatment of business expenditures called "nothings" (not previously deductible) in a manner similar to but separate from capital

expenditures, and tighter rules governing the depreciation of real property.[12] Mutual funds and trusts would generally be treated as conduits for transferring income to either their shareholders or beneficiaries.

As with corporate income, the differential tax on capital gains required some complicated rules to keep ordinary income and capital gains distinct for tax purposes. Transfers involving trusts would generally result in deemed realization for capital gains purposes, except for trusts where the spouse was a beneficiary. To prevent long-term tax avoidance, the assets in a trust would be subject to deemed realization every 21 years.[13]

The provisions regulating the taxation of international income generally followed those set out in the White Paper and endorsed by the Commons Committee. The old exemption for dividends received from foreign affiliates of Canadian corporations was extended to 1975. The Commons Committe recommendation that dividends arising from projects undertaken by 1975 and benefiting from tax incentives of developing countries not be taxed, was incorporated in the bill. Pending the negotiation of tax treaties with other countries which would permit exemption of dividends, those which did not otherwise qualify as tax exempt would be treated as a return of capital, and would therefore not be taxable.[14] The tax exempt status of foreign business corporations[15] would be phased out over five years, although dividends would be eligible for the new dividend tax credit.[16] The standard rate of withholding tax on payments to

non-residents in non-treaty countries would not be raised in 1974, as proposed in the White Paper, but be deferred to 1976.[17]

The personal rate structure generally reflected the recommendations of the Commons Committee. It was significantly more generous toward middle-income earners than the White Paper, which would have increased the tax burden on employment incomes for many taxpayers in the $5,000 to $40,000 range of taxable income.[18] The top personal marginal rate was to be reduced to a maximum of 61.1 per cent (including provincial tax at 30 per cent), cutting in at the $60,000 level of taxable income.[19] The rate schedule reduced the tax payable for all employees without dependents with taxable incomes below $8,000, and for those with dependents, the reductions extended right up the income scale.[20] This was made possible because of anticipated revenues resulting from the toughening of the dual corporate rate provisions, the (partial) taxation of capital gains and changes in the taxation of investment income of corporations.[21]

In addition to the stepped reductions in the corporate rate, the government committed itself to future incremental reductions in the rates of personal tax at the lower end of the taxable income scale.[22] Overall revenues were expected to be less than those projected by the White Paper, reflecting Mr. Benson's commitment to reduce rates in response to the controversy over the revenue projections in the White Paper.[23] The federal government expected to absorb $315 million of the expected total revenue loss of $338 million in the first year, with the provinces being compensated for

the remainder through a federal guarantee of provincial revenues and through an adjustment in equalization payments.[24]

Two provisions were included for averaging income to soften the impact of the progressive rates on "lumpy" receipts: a five-year "general averaging" system more generous than that proposed in the White Paper for all personal taxpayers, and an additional offset to recipients of capital gains income and certain specified lump-sum payments, a system of "forward averaging", available through purchase of "income-averaging annuities" which would spread the income over the taxpayer's remaining life, or for a fixed duration of up to fifteen years.[25]

The structure of personal exemptions and deductions outlined in the White Paper was preserved with minor changes, with the addition of a $650 deduction for taxpayers aged 65 and over.[26] This new deduction, available to the elderly poor and elderly rich alike, was clearly more valuable in dollar terms to the latter: a good example of what Eisenstein had mockingly referred to as "flexibility" in application of "ability-to-pay". A second change welcome to the middle and upper classes but offensive to the principle of vertical equity were the increased allowances for registered pension plan and registered retirement savings plans.

The inclusion in personal taxable income of medicare premiums and income maintenance plan payments made by the employer, unemployment insurance payments, and net scholarships and bursaries in excess of

$500, constituted an ironic nod to the comprehensive income concept of the Carter Report.

Assessment of Bill C-259

With the exception of the rate reductions on employment income at the low end and mid-ranges of the scale, practically all changes from the positions set out in the White Paper were in favour of business and investment income. The concessions to the mining and petroleum lobbies were largely a codification of Mr. Benson's announcement of the previous August.[27] The other major changes affected integration, the taxation of capital gains, and the taxation of gifts and bequests.

Integration:

The significance of the retreat on integration of personal and corporate taxes remains open to question. In the context of the comprehensive tax base, the Carter Commission's integration proposal satisfied the ability-to-pay principle more consistently than any subsequent governmental proposal. The White Paper's partial integration was at least an approximation to that proposed in the Carter Report, and an acknowledgement of the principle that any compensation for the so-called "double taxation" of corporate income should work in such a way as to distribute the benefits consistent

with ability to pay. Bill C-259, however, was closer to the Senate's recommendation to modify the existing dividend tax credit. The government had, in an ironic application of the proverb that he who wears the shoe knows best where it pinches, listened more attentively to those speaking on behalf of the recipients of the greatest part of the dividends.

A number of prominent tax professionals had dissented from the views or instincts of the majority of business spokesmen, pointing out that most shareholders would gain from integration. Mr. Benson, too, had demonstrated to a number of accountants on paper how they would benefit but always failed to convince them.[28] Lancelot J. Smith, though critical of some of the core elements of the White Paper, had also argued that:

> Regardless of whether or not integration is justified ...any businessmen who rejects the opportunity of getting a greater degree of integration is a fool....[29]

As Smith's candid remark suggests, the integration scheme was a money-loser for the government. The Royal Commission had acknowledged from the beginning that the scheme could only be tolerated on revenue grounds by widening the tax base, and on equity grounds by the full inclusion of capital gains in taxable income. This logical connection was again pointed out by R.D. Brown (one of the "tax advocates") and other tax professionals who told the business community that the abandonment of integration would make it easier to dismantle other tax reform proposals.[30] Whether or not businessmen understood the finer

points of integration, they knew how they felt about the steps proposed in the White Paper toward the broadening of the tax base. The fact that the full integration scheme was closely linked in the Carter Report to the taxation of capital gains at full rates, and that the full and partial integration proposals in the White Paper were similarly linked to the taxation of capital gains, best explains the apparently unreasoning opposition to the elimination of "double taxation" of which business had complained for so long.

In addition, the integration proposals, including the dual version offered in the White Paper, would provide progressively less relief the higher the income of the taxpayer. While one might argue that the increased incentive to low and middle income earners to purchase corporate shares would benefit current shareholders, it is equally plausible that wealthy shareholders withheld support for integration in hopes of extracting a relatively more favourable overall treatment for investment income in the hands of high-income earners.

Tax practitioners and many businessmen understood that integration would have been greatly complicated by the continuance of the dual corporate rate, and that this technical factor had been one of the reasons for the desire of Finance officials to introduce both integration and the flat-rate of corporate tax. The widespread tax avoidance practices which took advantage of the dual rate help explain the government's reluctance to concede on this issue, a reluctance which was appreciated and accepted by many tax practitioners.[31] Both the Carter Report and the White Paper had pointed out that the

dual rate subsidized all corporations, big and small; and all incorporated businessmen, rich and not-so-rich. By setting up a collection of apparently independent corporations (with the assistance of professional advice if required) it was possible for someone receiving much more than $35,000 per year to pay taxes at the same rate as an employee earning only about $8,000. Those opposed to the removal of the dual rate therefore were also inclined to oppose integration.

From the outset the mining corporations had opposed integration as recommended by the Carter Commission.[32] The advantage of the existing dividend tax credit from their point of view was that it was given to their shareholders regardless of the taxes actually paid by the corporation, so long as it was not listed as "tax exempt". To the extent that the extractive industries hoped to continue to benefit from tax incentives, their shareholders would not benefit from integration.

Capital Gains:

The bill's most significant departure from the comprehensive tax base advocated in the Carter Report was the inclusion of only half of realized capital gains in taxable income. Taking the Commission's rough estimate that about half of the income accruing from the increased values of corporate shares were the result of "goodwill gains" rather than retained earnings, this exemption would keep about

a quarter of the income of the corporate rich out of the tax base. This marked a retreat from the White Paper proposals which would have taxed all capital gains at full personal rates with the exception of gains on widely-held shares.[33] Even the Commons Committee had not gone so far in ceding to the demands of capital. On this point the government seems to have been guided more by the Senate Committee which opted for a system closer to the American distinction between short-term gains (to be treated as regular income) and long-term gains (which would be taxed at half the personal rate or a maximum of 25 per cent).

The government's concessions on capital gains were not out of line with the advice of a number of tax professionals, among them, W.A. Macdonald, senior partner with McMillan, Binch (and one of the "tax advocates"), who suggested inclusion of half of all realized gains, no five-year revaluation but with deemed realization at death and with a 25 per cent dividend tax credit. The result would be a maximum tax of 25 per cent on capital gains.[34]

Gifts and Bequests:

The decision of the federal government to leave the gift and estate tax field entirely to the provinces was defended by Mr. Benson both on grounds of revenue and of equity. The federal government's revenue from the Estate Tax was only about $55 million, with three times that amount being turned over to the provinces, two of which

refunded the amount to the estates which had paid the tax.[35] The Commons Committee had also recommended a reduction in the rate of tax on estates, which would cut the federal government's modest share even further.

On grounds of horizontal equity, to continue the Estate Tax would have been unfair to estates and beneficiaries in those provinces not refunding the tax. More significant for the government was the argument that the imposition of deemed realization of accrued capital gains at death, combined with the Estate Tax, "could in some instances result in substantial tax impact arising on the death of a taxpayer."[36] The government accepted the argument of business and professional critics of the Carter Report that there should not be any "double taxation" of inter-generational transfers of wealth.[37] The White Paper proposals combined with the amended Estate Tax were more generous to such transfers than the Carter Report, since gifts and bequests were to be treated more leniently than ordinary income. The government's subsequent abandonment of the five-year revaluation of widely-held corporate shares implied a return to the alternate principle of deemed realization at death.

This shift by the government revived the arguments against deemed realization at death when combined with the taxation of gifts and bequests. Tax professionals and journalists of the financial press had anticipated this during the debate over the White Paper when it appeared that their criticisms of the five-year revaluation proposal were being taken seriously by the government.[38] I.H. Asper noted in

his newspaper column that the idea of abolishing the Estate Tax appeared to be a favoured alternative, judging from "corridor comment from tax practitioners" at the March 1970 Tax Conference.[39] This pressure for removal or reduction of inheritance taxes rested on the principle that the taxation of accrued capital gains at death coinciding with estate and gift taxes constituted "double taxation". This ignored the perspective of the Carter Report, which had justified the taxation of capital gains at death as simply a matter of the tax collector finally catching up to the deceased for many years of unrealized and untaxed capital gains. The fact that the occasion of taxation coincided with the taxation of the bequest (either in the form of income tax or of estate and succession duties) was not an injustice toward the beneficiaries but an indication of the income which had escaped tax during the lifetime of the deceased.[40]

The social purpose of taxing transfers at death to mitigate what might otherwise become an undesireable concentration of wealth had been discussed by public finance specialists and appeared to have been accepted by Department of Finance officials.[41] Mr. Benson also appeared to have accepted the social and equity arguments for estate taxes when he was defending his amendments to the Estate Tax in 1969.[42] The decision of the federal government to abandon the estate tax field to the provinces was expected to put pressure on those provinces which were not already refunding the tax to abolish their own taxes on gifts and bequests. The result would be the tax-free transfers of large accumulations from one generation to the next, increasing the concentration of wealth. According to the

Minister's own figures, only five per cent of Canadians ever paid estate tax.[43] The government's decision can therefore be understood as the potential concession of $50 million annually (the federal share) and possibly as much as $200 million (the approximate total Estate Tax revenue in 1969) to the top five per cent of Canadian society.[44] Mr. Benson had revealed, during the course of the same speech, an additional measure of the distributive impact of his concession to wealthy Canadian families:

> We estimate that to raise about this amount from roughly the same group of persons who pay the bulk of estate taxes, that is, those with incomes over $10,000, would require a 15 per cent income surtax. If, instead, we raised this amount in income taxes from those whose estates are over $500,000, we would have to double their present income tax.[45]

As governments, commissions and tax theorists often say to supplicants for tax concessions, favours to one group have to be paid for by higher taxes on all the others. In the case of the Estate Tax, Mr. Benson told the House of Commons that, should that tax be abolished, the revenue loss could be made up by a one per cent increase in the social development tax.[46] In the context of Bill C-259, therefore, we can view the cost of the elimination of the estate tax as being in the order of one percentage point on the personal rate schedule.

The decision to abolish the Estate Tax was Mr. Benson's, taken without, and at least implicitly, against the advice of his Department.[47] The reasons appear to have been those given publicly by Mr. Benson, with the additional consideration that, as the federal

government received only a quarter of the revenue from death duties, the opposition and pressure resulting from having to enforce it was not worth the political cost. From the point of view of federal revenues, never far from the mind of a Minister of Finance, it was more advantageous to collect 50 to 70 per cent of the revenue from the taxation of capital gains than to collect only 25 per cent of the revenue from death duties. It seemed therefore like a suitable concession to make in return for the tax on capital gains with deemed realization at death.[48]

The Modification of Bill C-259

Although Bill C-259 was firm government policy, backed by the parliamentary conventions of governmental confidence and party discipline, it was treated by the opposition parties and organized interests as yet another "first offer" in the negotiation of a new tax system. However, the erosion of the bill was of a smaller order compared to that of the White Paper, and with the exception of the demands of the co-operatives (the only vocal, organized interest not yet invited to feast off the carcass of the comprehensive tax base) the language of debate was more technical than polemical. This was appropriate since the major questions of principle had already been won and lost. Technical discussions of the modalities of implementation and administration were the safest way to quibble for maximum advantage over significant details without arousing widespread opposition against the implantation of a new system of tax privilege

to replace the old.

Most business spokesmen welcomed Mr. Benson's June 1971 budget which, in an attempt to stimulate the economy out of recession, reduced the income and corporation tax rates to accompany changes in the tax structure. The banks[49], the Toronto Stock Exchange,[50] the Canadian Chamber of Commerce[51], and the governments of Ontario and Quebec[52] were among the major players in the tax reform stakes expressing satisfaction or relief at the government's tax reform legislation. Most chartered accountants whose views were reported by The Globe and Mail also viewed the tax structure changes in a favourable light.[53]

Consultations with Tax Professionals:

During the summer of 1971 the Department of Finance published a series of draft regulations to govern the application of Bill C-259, "to permit taxpayers to plan their affairs during the period until the reform legislation is passed and the regulations subsequently prescribed."[54] At the same time, Finance officials were meeting with representatives of the Canadian Bar Association and the Canadian Institute of Chartered Accountants "in order to learn [their] views ...regarding any technical problems that exist[ed] in the legislation."[55]

Finance officials also met with "other professional and trade

groups", and "a number of individuals and associations" met with Mr. Benson concerning the provisions of the bill and of its regulations.[56] While much of the discussion may indeed have focussed on technical matters, the only detailed study available of one particular group's interaction with the Department, that of the Co-Operative Union of Canada, indicates that its objective was the substantial modification of the provisions affecting co-operatives and credit unions.[57]

The bill was given second reading in the House on October 12th, then referred to the Committee of the Whole. The following day, Mr. Benson tabled a list of 95 amendments, the Department of Finance's response to the submissions received and to the discussions with various groups during the summer and fall. In introducing the amendments, Mr. Benson paid tribute to the organizations of tax professionals which had helped shape the legislation:

> The Canadian Institute of Chartered Accountants, the Canadian Bar Association, the Canadian Tax Foundation, as well as many other organizations and individuals, have spent a great deal of time and effort in reviewing the bill. I have been particularly impressed with the fact that most of the submissions have not merely focussed attention on potential hardship cases but have also indicated instances where amendments are necessary to prevent tax avoidance schemes. The submissions of these organizations and individuals have been valuable. In the main, the amendments are in response to these submissions.[58]

While conferring with the Department on technical aspects of the bill, the Canadian Institute of Chartered Accountants was busily instructing its members on the intricacies of the legislation so that

the accountants could do likewise for their clients. An editorial in the November issue of the Institute's periodical, The Canadian Chartered Accountant entitled, "On the Brink of Financial Disaster", admitted that even professional accountants attending its special course on Bill C-259 had difficulty coping with the complexity of the bill:

> ...the meanders of the legislation make one get vertigo.... Even if it has often been said, it should be recalled that first impressions of relative simplicity have been replaced by incredulity as experts dig more deeply into the legislation. Moreover, complexity is not so much in connection with large corporations or international matters, aspects the public traditionally links with complexity. For instance the provisions of the bill relating to small businesses are strewn with snairs. Chartered accountants who serve small businessmen, like those who serve the more important ones, must absorb in record time a mass of information, at least if present plans are to become effective on the scheduled date.[59]

As a result, the editorial suggested that proclamation of the Act, scheduled for January 1st, 1972, be deferred "until people have had time to grasp the meaning of it and to act accordingly"[60], a position supported in the House by the Conservative Party and by Créditiste members.

Positions of the Opposition Parties:

Bill C-259 was a three-inch, 735-page document, intimidating by its sheer bulk those members of Parliament who were relatively untutored in the analysis of tax legislation. Parliamentary decorum

required that Opposition members say something about the bill which might give constituents the impression that their MP's had devoted some critical thought to the document, and that they had some idea of its implications. Some of the members' speeches suggest that they may have been bluffing, like school boys trying to hide the fact that they had not understood their lesson. The adjective used most often in the opposition discourse was "complex". Mr. Stanfield used it several times during a twenty-minute speech on second reading.[61]

The complexity of the bill, charged Mr. Stanfield, would force small businessmen and farmers to rely more than ever on tax advisors. Worse still, the bill had been overtaken by events: President Nixon's economic policies aimed at improving the United States' balance of payments situation would require from the Canadian government different tax policies than those set out in Bill C-259. Although he did not specify how the bill ought to be changed, he implied that additional tax incentives might be needed to off-set the increased barriers facing exports to the U.S. In any case, the Conservatives wanted the bill split up, and the portion of it dealing with the structure of the tax system re-thought and re-drafted.[62]

Gordon Ritchie, a Conservative MP and member of the Commons Finance Committee which had studied the White Paper, charged that the bill would hurt small, unincorporated businessmen, including farmers. It would also reduce economic development and employment opportunities in rural areas by depriving mining companies of the incentive to explore for new mineral deposits. He quoted from a Globe and Mail

report of a statement by McIntyre Porcupine Mines Treasurer, A.G. Goodeve (one of the "tax advocates") as his authority:

> The tax reform package will make the development of new mines less attractive by lowering the return on mining investment. Certain marginal mines, which could be economic under present conditions, will no longer be viable under the new regime.... The most basic uncertainty regarding the new provisions relates to exploration yet its impact will be more immediate because the investment decisions which must be made now are concerned not with the short-term but with the eventual rates of return from discoveries not yet made, which must compare favourably with investment opportunities elsewhere.[63]

Eldon Woolliams, corporate lawyer and another Conservative member of the Commons Finance Committee, also attacked the bill for failing to provide adequate incentives to the resouce industries.[64] He was also critical of the Liberal's management of the process of tax reform, and scathing in his denunciation of the passivity and ignorance of Liberal back-benchers on the Finance Committee in 1970, and in the Commons Committee of the Whole during the discussion of the bill. In a witty reference to the government's elimination of the "basic herd" concept which had allowed farmers to treat a portion of their livestock as capital rather than inventory for tax purposes, he said the "basic herd" of Liberal back-benchers had been trotted in by the Liberal whip to vote for Bill C-259.[65]

New Democratic Party Leader, David Lewis, agreed with Stanfield regarding the complexity of what he called "...this complicated and unreadable bill...", defying anyone to say what it meant.[66] Like the Conservatives, Lewis thought that the bill had become obsolete as

a result of "Nixonomics", and wanted it withdrawn and changed in the light of the government's "re-appraisal" of its economic relations with the United States. However, Mr. Lewis wanted fewer concessions to multi-national corporations, especially those in the resource extraction industries. He charged that the bill gave

> ...important tax concessions to the large foreign-controlled corporations that yank Canada's wealth out of the ground and ship it elsewhere.... It is obvious that when one gives corporations that have their headquarters in the United States continuing tax concessions, one invites them to continue controlling our economy and indeed to increase that control.[67]

Stanley Knowles described the bill as "...not a piece of major tax reform but simply a number of changes in the present tax law"[68] and listed what the New Democrats found wrong with the legislation:

- -- personal exemptions should be higher, corresponding to a minimum subsitence level below which no-one should pay tax;
- -- the recognition for employment expenses should be higher and in the form of a tax credit to make its effect more progressive;
- -- the increase in the deduction for elderly taxpayers and its extension to taxpayers between 65 and 70 years of age should be made retroactive to 1971;
- -- the federal Estate Tax should be retained;
- -- the full amount of capital gains should be included in income;
- -- co-operatives and credit unions should be given a "decent break".[69]

With the exception of the old age exemption and the party's

generosity to co-operatives and credit unions, the New Democrat's position was similar to that taken by the Carter Report. Of course, the Commission had recommended the abolition of estate taxes and succession duties, but only as part of an integrated system where all gifts and bequests were included in income and all realized gains taxed at normal personal rates with deemed realization at death. The nearest approach to that position in the circumstances would have been the retention of the Estate Tax.

Speaking on December 10th during debate on third reading, John Burton added that the NDP objected to the bill's concessions to the resource industries on the grounds that those provisions violated the concept of "neutrality" put forward by the Carter Commission. His party also wanted to see limits placed on the deductions of advertising expenses from business income. Like the Conservatives, they thought that the "basic herd" concept should be retained for farmers, and that bona fide farmers should be able to sell their farms to other farmers without deemed realization provided the property continued to be used for farming.[70]

The Senate's Treatment of Bill C-259:

Tax bills in the House of Commons could not be referred to a standing committee but had to be discussed in Committee of the Whole. The Senate not being so constrained, its Standing Committee on Banking, Trade and Commerce studied the bill and heard witnesses from

approximately the same "public" which had offered its advice on the White Paper.

As a preliminary to its public hearings, the Banking Committee was briefed by Stephen Smith and Arthur A.R. Scace, two tax lawyers from the Toronto firm of McCarthy and McCarthy, the same firm as the Committee's Chairman, Salter Hayden. Smith and Scace had jointly prepared a special course on Bill C-259 for the Law Society of Upper Canada and used the same material to instruct the Senate Committee on the legislation. Scace was among the "tax advocates" discussed in the previous chapter, having appeared before the Commons Committee on behalf of the Canadian Institute of Public Real Estate Companies. Asked by Senator Lazarus Philips, Vice-Chairman and Chief Counsel for the Committee to give a general appraisal of the bill, Scace offered the following comment:

> I think you will all be aware that this is probably the most difficult piece of legislation that has ever been placed before Parliament.... You have probably heard a lot of criticism in the press and from various associations about its complexity, with people saying they cannot understand it. It is difficult, but I believe a lot of practitioners have now come to the conclusion that it may not be complex enough; that there are gaps, that there are things that should be in there and that are not. I believe it will get worse before it gets better.[71]

Of 25 witness groups heard before the Committee issued its "Preliminary Report on the Summary of the 1971 Tax Reform Legislation" on November 4th, only four were not either corporations, business groups or associations of tax professionals. Two of these represented the co-operatives and credit unions. Only four of the witness groups

had not appeared before the Commons Committee examining the White Paper. As was the case during the White Paper debate, the major corporations were the hegemonic spokesmen of business: of the eight individual corporations appearing before the Banking Committee before November 4th, only one, the Sears-controlled Allstate Insurance Company, was not included in Clement's list of "dominant" and "mid-range" corporations.

The Senate's report on the bill was critical of several features, and proposed a number of "technical" amendments, as well as others which amounted to a further softening of the bill's impact on certain forms of investment income and remuneration normally received by corporate executives. One study of the behaviour of the Senate Banking Committee summarized these more substantive amendments which would have:

> (1) allowed for greater discretion in donors' valuation of gifts; (2) provided that capital-gains taxes not be levied on beneficiaries of profit-sharing plans until the holdings are disposed of; (3) curtailed for at least another two years the foreign-accrual property income tax; (4) exempted from the law certain classes of non-resident investors; (5) permitted the payment of capital-gains taxes in installments for up to six years; and (6) dispensed from the Act's departure tax rules those who had been resident in Canada for less than thirty-six months.[72]

The Senate Committee's package of proposed amendments raised the prospect that it might refer the bill back to the House of Commons. While unable to block the passage of a tax bill indefinitely, the prospect of a further delay was not welcomed by the government. At least partly in order to encourage the Senate to pass the bill with

only the government-sponsored amendments already tabled in the lower chamber, Mr. Benson announced in the House on December 10th his intention to introduce further amendments to the Act in 1972 which would be retroactive to the beginning of the year.[73] These amendments would affect deemed realization on gifts to charities, deferred profit-sharing plans, rules affecting deemed realization of property and income averaging for taxpayers leaving Canada, so-called "passive" income from foreign sources, and rollovers arising from corporate reorganizations.[74]

The amendments promised by Mr. Benson were ultimately introduced into the House as Bill C-222 by his successor as Minister of Finance, the Hon. John N. Turner. Mr. Turner's Assistant Deputy Minister for Tax Policy, Marshall Cohen, while speaking to the 1972 Tax Conference, had this to say regarding the amendments and the role of the Senate Banking Committee:

> ...if you examine the report of [the Senate] committee which resulted from its deliberations on Bill C-259 and then look at the provisions of Bill C-222 and some of the more recent government pronouncements about proposed tax changes of a technical nature, you will see a good picture of the importance of the deliberations of this Senate Committee.[75]

The Government's Position:

Mr. Benson's response to the opposition criticism of the complexity of the bill was that this should not be a problem for the majority of Canadian taxpayers -- those earning wages and salaries,

and whose taxes were deducted at source by the employer. The really complicated parts of the bill -- those affecting business income and corporations -- were the result of the government attempting to be fair and to design a tax system appropriate for a complex commercial world:

> The more complex provisions of the bill, those involving the corporate tax regime and the provisions dealing with capital gains transactions, are of principle concern to the business community. A complex tax system is nothing more than a reflection of a complex commercial world.[76]

Mr. Benson explained that many of the complexities in the bill arose from a number of what he called "relieving features", especially those bringing only half of capital gains into income, exempting certain kinds of income from tax (such as capital gains on owner-occupied homes), deferred application or phasing-in of a number of features (such as those affecting the resource industries and international income), and the dividend tax credit which had to cope with the favoured treatment of capital gains.[77] Implied, but left unsaid, was the thought that, had the government hardened its heart against the business lobbyists and applied the Carter Commission's "a buck is a buck" philosophy, the bill would have been a good deal shorter and simpler.

But that was not to be. The concessions were made because the government felt it had little choice in the circumstances and was then determined to make the best of it and sign the bill into law by the beginning of 1972.

Liberal back-benchers generally defended the bill, though some agreed with opposition members that it should be amended to include concessions to co-operatives and credit unions. Several admitted that the legislation was not as good as it might have been but that it was a significant improvement over the existing Act: at least capital gains would be subject to tax, personal exemptions would be raised to assist low-income people, and the resource incentives would be better designed to achieve their purpose. Ross Whicher responded to John Burton's criticism of the mining and petroleum incentives in the bill by pointing to the employment created by, and the economic "spin-offs" associated with resource industries:

> Even if a mine employs only a few people, it is better for the economy of Canada if that mine is open rather than closed. I suggest that many mines, oil wells and gas wells are operating in Canada as a result of sensible concessions given to them which enable them to employ Canadian labour. Their workers eat Canadian wheat, pay Canadian taxes and enjoy the Canadian way of life.[78]

Two Liberal members, however, were less confident that the bill was an adequate response to what they understood as the need for tax reform. John Roberts was reported by the Globe and Mail to have told a Committee for an Independent Canada meeting in Thunder Bay that the legislation did "not represent real tax reform at all", that the government had no concept of what it wished the economy and industrial structure to look like in ten years, and without which, reform of the taxation system, or any rational policy on competition or foreign ownership, was not possible.[79] Roberts did not criticize the bill in the House, however, said that the Globe and Mail report was

inaccurate, and voted with the government on third reading.[80]

The other Liberal dissident was Eric Kierans, who had resigned from the Cabinet and was speaking simply as the Member for Duvernay. Kierans' opposition was reasoned and detailed, capturing the silent attention and admiration of the opposition members and perhaps of some government members as well. When his allotted time had expired, the House gave its unanimous consent for him to go on. Kierans' central objection to the bill was similar to that of the New Democrats: that it was defended by the government as a major tax reform, yet it had abandoned the equity goal of the Carter Commission:

> Fairness in taxation, as it was conceived by the Carter Commission, demands that persons with equal amounts of income pay equivalent amounts of tax and that persons with larger or smaller incomes pay proportionately different rates of tax. This principle was enunciated clearly in their report, but this principle no longer obtains. Income is still divided into two classes, income from labour and from enterprise and from effort, and income from rolling over wealth, that is, capital gains. And whatever the rate that applies to workers on wages and salaries, the gains on wealth are going to be taxed at exactly half that rate. Persons in similar circumstances are not treated in the same manner.[81]

Kierans took issue with the reason always trotted out by those defending concessions to investment capital, that they were necessary to ensure an adequate rate of investment and of economic growth. There was no reason, Kierans argued, to accept the threat that people would not invest if capital gains were taxed like other income because if they did not invest their money they would have to slowly consume it.[82]

Linked to what he charged was a completely unjust and unnecessary concession to capital, was the bill's proposed subsidization of corporate concentration. The provision to allow Canadian corporations to deduct the interest charges on money borrowed to buy other corporations meant that the government, and through it, other taxpayers, would be paying half the interest on money used to finance corporate takeovers. Tax policy would thus lead to greater concentration in the economic structure, reduced competition, and greater concentration of wealth and power:

> The primary effect of this clause will be to create conglomerates, firms whose only objectives are growth, growth of assets, growth of revenues, and growth of net income. But growth and accumulation are wealth, and wealth is that part of annual income which is not taxed, which is not distributed. To favour wealth and accumulation is to favour size and the concentration of power, and this is neither fairness nor justice. This is the opposite of the main objective of the Carter Commission, to make corporations more responsible to people, to shareholders and consumers alike.[83]

Since even foreign-controlled corporations could take advantage of the provision, Kierans pointed out that Imperial Oil could buy out several of the largest Canadian-controlled companies, but that the reverse would not be true since Imperial was owned and controlled from New York. Thus the tax system would work in the opposite direction to the government's policy on foreign ownership.[84]

As a result of the concessions to resource industries, Kierans said that a similar contradiction existed between tax policy and industrial and economic policies. The concessions in the bill would

continue the trend to increasing dependence on the export of natural resources, particularly non-renewable natural resources with a relatively low labour-to-capital content ratio. Since the countries to which Canada sold these raw materials themselves exported manufactured goods, Canada, in subsidizing the cost of their raw materials, was making these manufactured exports more competitive against any that Canadians might produce. It was also contibuting to future pressure to accept increasing volumes of manufactured goods to balance the trade accounts with Canada's industrialized trading partners. In Canada, the tendency would be toward a modern, competitive sector exporting raw materials and employing few people, co-existing with a weak domestic sector paying low wages, with high unemployment, and an expanding and inefficient state sector to manage the economic and social misery. Meanwhile, in using tax policy to depress the price of raw materials, Canada would be assisting the industrialized countries in suppressing the economic development of third world countries which exported similar raw materials.[85]

The Co-operatives:

The Co-operatives, through their lobby organization, the Co-Operative Union of Canada, (or CUC) had been working since the appointment of the Carter Commission to preserve the features in the existing Income Tax Act which had allowed deduction of patronage dividends from taxable income and which had allowed a three year tax exemption for new co-operatives.[86] In spite of sustained efforts,

the co-operatives had failed to convince the Royal Commission, the Department of Finance in its White Paper, or the Senate or Commons Standing Committees studying the White Paper.

The CUC intensified its efforts at the final legislative stage, with its solicitor, J.J. Dierker (one of the "tax advocates") meeting with cabinet ministers, officials in the Department of Finance, and members of Parliament.[87] The co-operatives were also mobilizing their members to write letters to their members of Parliament and the increased interest of MP's in the issue rewarded the CUC with greater access: CUC delegations attended caucus meetings of the Conservatives, New Democrats, and the Economic and Consumer Affairs and Agricultural Committees of the Liberal Caucus.[88] The CUC also had the support of Eugene Whelan, who appears to have been instrumental in getting the co-operative spokesmen access to the Liberal caucus[89] and was pressing Mr. Benson for concessions.[90] All parties had members favouring better tax treatment for co-operatives, credit unions and caisses populaires, including all the House leaders except the Conservative's Gerald Baldwin.[91]

Mr. Benson's first set of amendments to the bill softened its impact on the cooperatives, but not to the satisfaction of the CUC, which argued in a submission to the Senate Banking Committee for the removal of the "capital employed" concept in the bill which put a lower limit on the taxable income of co-operatives. Benson introduced a second package of amendments at the end of October which included further concessions to co-operatives and credit unions, but still not

to the CUC's satisfaction.[92] In November, following two days of House debate on co-operative taxation, the Cabinet asked Allan MacEachen, the Liberal House Leader, to negotiate with the CUC.[93] Working through Gordon Blair, a Liberal MP and a former solicitor for the Co-Operative Union of Canada, the government and the CUC were able to reach an agreement.[94]

While lacking the financial resources of the major business interests, the co-operatives and credit unions had achieved their objectives through effective mobilization of their members, tireless and skillful lobbying by their representatives in Ottawa, and the strategic (though perhaps somewhat fortuitous) placement of some co-op supporters as MP's. Even so, their efforts might have come to nothing had it not been for the government's impatience to get the bill enacted before the end of the year so that it could be applied in 1972.[95] The NDP was pressing for amendments similar to those asked for by the CUC, while the Conservatives and several Liberals agreed. For the government, concessions to the co-operatives were an acceptable price to pay in order to get the bill through quickly without raising a great deal of media attention through the use of closure.

In the end, the co-operatives got even more than they asked for, since the government, in introducing its own amendment, felt that it had to be different from that proposed by the NDP. MacEachen therefore went a step further in generosity to the co-ops, proposing the removal of the "capital employed" concept and substituting a 15

per cent withholding tax on patronage dividends over $100, to be creditable against the individual member's personal income tax. Provisions for credit unions and caisses populaires were similarly satisfactory.[96] Thus the success of the co-operative's lobbying efforts were due, as much as to anything else, to good luck.

The Conclusion of the Tax Reform Process:

In spite of the government's concessions to the co-operative movement and its supporters in the House, consideration of the bill in Committee of the Whole continued on into December with little prospect that it would receive third reading before the Christmas recess. On December 2nd Mr. MacEachen introduced a motion under Standing Order C-54 to limit debate in Committee to an additional four days.[97] The motion was carried, with two New Democrats, Andrew Brewin and Max Saltsman voting with the government.[98] On December 14th, MacEachen introduced a second motion to allow only four more days of House debate, with the vote on third reading to take place no later than 3:45 in the afternoon of December 17th.[99]

Prime Minister Trudeau, one of the final government speakers on the bill, read from a prepared text praising the bill as the crowning achievement of a decade of tax reform, during which, "For the first time in Canada a government has invited the population as a whole to participate with it in the formulation of a major policy."[100]

Opposition members, their opportunity to discuss the bill any further foreclosed, heckled the Prime Minister at every opportunity. However, a sense of the occasion had taken hold in the House following Mr. Trudeau's observation that the process had begun only a few months short of a full decade earlier with the appointment of the Royal Commission on Taxation. Then Eric Kierans calmly condemned the bill by setting it against what the Royal Commission had recommended.

The New Democratic Party's Finance critic, Max Saltsman, repeated the reasons for his party's opposition to the bill, and like Kierans, compared it unfavourably to the equity principles and recommendations of the Carter Report:

> ...we think a comprehensive income concept has to be adopted, with all forms of economic gain subjected to a graduated scale of income based on ability to pay.... We accept the Carter Commission proposal that all income be taxed on the same basis.[101]

Saltsman also made some attempt to come to terms with the role of the Minister of Finance in the failure of the tax reform process to attain the goals set out in the Commission's Report. He did not regard Mr. Benson as the villain of the piece, in spite of the fact that Benson was "...the one who did away with tax reform."[102] Benson, Saltsman observed, started out with the intention of reforming the tax system along progressive lines but was thwarted by his own party:

> ...I think in the early days there was a real wish on the part of this man to bring in genuine tax reform, but there was no rapport between him and his party and

> pressures were continually being brought on him within his own party. His own backbenchers were going across the country saying how terrible this tax bill was, how they were going to do something about it, assuring their business supporters "do not worry, we will get to Benson and we will make him back off." They did get to the Minister of Finance and he has backed off.[103]

With debate ended on the afternoon of December 17th, the bill was passed on third reading, with all opposition parties, and the Member for Duvernay, voting against.

The Results of Tax Reform

The decade of tax reform ended with the self-congratulations of federal government spokesmen regarding the unparalleled level of public participation encouraged by the government and the unprecedented extent to which it had "listened" to the criticisms of its White Paper proposals for reform. Typical of such apologetics were the remarks of Patrick Mahoney, Parliamentary Secretary to Finance Minister Benson:

> This may not be reform by the standards of the socialists who feel not only that a buck is a buck, but that it is the government's buck. It is not revolution. It is reform by any rational standards of definition. It is reform supported by unparalleled research, expert comment and input. It is a reform founded on an unprecedented process of public participation -- a process of good democracy, good politics, good government. It is responsible reform.[104]

Despite this self-congratulation, we must draw the balance on the gains and losses and identify the winners and losers. The moral is

clearly that suggested by government spokesmen at the conclusion of the process: participation in policy formation is indeed beneficial, at least to those who get involved. The 1972 Act represented a compromise on tax reform which did not please everyone but was well within the spectrum of opinion of the tax professionals who dominated the debate. Practically none of them wanted accrued capital gains to be taxed, and it was not in the legislation. Most were prepared to accept taxation of realized capital gains at a reduced rate. Acknowledging that this implied deemed realization at death, most called for the reduction or elimination of estate taxes, and the government did not disappoint them. Tax professionals were divided on the question of integration and those in favour were unable to persuade most of their business clients and colleagues. The new Act included a modified dividend tax credit, allowing a form of integration only as an option for private companies. Most tax professionals were prepared to admit that the dual corporate rate, at least in its existing form, ought to go, provided it were replaced with a more efficient incentive to new small businesses. This was reflected in the new Act. The tax professionals had long been in agreement that the marginal rates were too high at the upper-income end, and the new personal rate schedule satisfied this demand to the extent that the revenue constraints imposed by other concessions permitted.

Writing in a publication of the Canadian Institute of Chartered Accountants printed specially for the occasion, Donald Huggett, a former member of the Tax Analysis Unit and one of the "tax advocates",

told his professional colleagues that the government had given them what they had been asking for, and in a more ironic sense, what they deserved:

> That they [the government] really did listen is obvious from the legislation which no matter what one might think of it, must certainly come as close to reflecting a consensus as is realistically possible.... Despite all recriminations, the Minister of Finance had demonstrated, to his great credit, that he did take into account the views of all Canadians, all levels of government and, in particular, the views of both the Senate and Commons Committees. In the process, our fundamental tax problems remain unsolved, but the Minister must have delighted in proving that participatory democracy can be made to work.[105]

Huggett pointed out that the new Act did not represent reform, simply a "renovation", but retaining all the problems that a decade earlier had prompted the appointment of the Carter Commission:

> Double taxation of corporate income continues to be a feature of our new system, the corporate surplus problem and the provisions to prevent dividend stripping are as bad as they were and are made worse by the retention of the ministerial discretion contained in old Section 138A.... The associated company problem is still with us, only the stakes are greater and, to cap it all off, we must continue to try to differentiate between capital gains and income! Insofar as distribution of the tax burden is concerned, a new hand has been dealt, but preferences still remain, some of them, such as gifts and bequests, to a greater extent than before.[106]

If solutions to the structural problems had been sacrificed in favour of some greater good it is not apparent what that more pressing objective might have been. It does not appear to have been that of economic growth, at least to the extent that growth could be influenced by the tax structure. The government claimed to have found a balance between what it claimed to see as the opposed goals of

equity and economic growth, yet if any balance had been achieved it was in the equal failure to achieve either. In an economic analysis of the effects of the tax reform legislation, John Bossons (one of the original architects of the Carter comprehensive income concept) concluded that the goals of both equity and economic growth had been sacrificed in favour of what he called a "pessimal political compromise -- a compromise which, in its attempt to avoid hurting anybody too much, hurts everybody more than it would do if it were not so over-compromised."[107]

Bossons was especially critical of the abolition of the federal estate and gift taxes, supposedly as compensation for the inclusion of half of realized capital gains in income with deemed realization at death. The capital gains tax, even at half rates, when combined with the failure to implement integration, would present a substantial disincentive to investment. The elimination of the taxation of bequests, that is the removal of a distant and uncertain disincentive unconnected with investment behaviour, could not begin to offset the disincentive presented by the capital gains tax.[108]

Bossons could not conceive of a more costly and ineffecient investment "incentive" than the removal of the estate and gift taxes. Their abolition constituted, according to Bossons' calculations, a windfall to upper-income Canadians of about $12.5 billion in taxes that would not have to be paid. Assuming a discount rate of 8 per cent, this constituted a Christmas bonus of at least $4.5 billion to wealthy families, with the gift being increasingly generous the

wealthier the family. Bossons weighed the opportunity costs in terms of other possible tax changes with equal revenue costs: a 10 per cent reduction in personal tax rates for all incomes over $15,000; or a reduction in the top personal marginal rate from 61 per cent to 40 per cent.[109] Mr. Benson, when he was still defending the Estate Tax in February 1969, had argued in roughly similar terms.[110]

Economic growth questions aside, Bossons concluded that the combination of the capital gains tax and the elimination of the Estate Tax worked to the relative advantage of existing concentrations of wealth and against potential new accumulations of wealth, that is, towards increasing concentration of wealth and reduced social mobility.[111] There could be no social or economic defence of the government's decision, which was grossly inefficient in promoting all its declared tax reform objectives:

> Were the government serious in a desire to increase growth, Bill C-259 should be accompanied by some efficient investment incentives that would be focused on making risk-taking investments more attractive. Were the government serious in achieving the purported redistributive and reform objectives of Bill C-259, it would not have thrown out the federal estate tax. The redistributive, economic growth, and equity objectives could all be attained to a greater extent than is achieved by the new Income Tax Act. As a result, Bill C-259 provides a good example of policy inefficiency.[112]

In redistributive terms, the lower income earners (who, nevertheless earned enough to pay income tax) benefited from the rate reductions and increased exemptions, while the wealthiest, especially those making over $250,000 a year, benefited from the reduced marginal rates and the elimination of gift and estate taxes, which would, on

[illegible]. "Revisions to estate tax likely in place of capital gains plan", The Globe and Mail (Toronto), Mar. [illegible], 1971, p. B1; and Ronald Anderson, "Capital gains tax war is over: fight shifts to death duties", The Globe and Mail, Mar. 4, 1971, p. B2.

[illegible]. "Reduction in estate tax rates probably most sensible policy", The Globe and Mail (Toronto), April 7, 1971, p. B4. Not all practitioners were prepared to go this far, however: R.D. Brown argued for the continuation of the Estate Tax with a combination of increased exemptions and reduced rates. See R.D. Brown, "The Taxation of Capital Gains", Report of the Twenty-second Tax Conference, pp. [illegible]; and Ronald Anderson, "reduction in estate tax rates probably most sensible policy", The Globe and Mail (Toronto), April 7, 1971, p. B4.

[illegible]. See Ch. 5, pp. 732-741; 748-754.

[illegible]. When the federal government was considering estate and succession duties during the Second World War, Bryce had favoured taxing bequests according to the income of the recipient, rather than according to the size of the estate, as favoured by Kenneth Eaton. Bryce interview.

[illegible]. See Ch. 7, above, p. 511.

43. "Text of a speech by the Honourable E.J. Benson ...February 5, 1969; House of Commons Debates, Feb. 5, 1969, p. 5179.

44. We cannot state that precisely the top five per cent of income-earners would receive the benefit, though one would expect it to remain very largely within the families which had, through their ample and only partially taxed incomes, accumulated estates large enough to exceed the exemptions provided under the Estate Tax Act.

45. Ibid.

46. Ibid.

47. Bryce interview. This was confirmed in an interview with another Department of Finance official.

48. Benson interview. An analysis of projected revenues from the estate tax and from deemed realizations at death by John Bossons, ("An Economic Overview of the Tax Reform Legislation", pp. 56-57) provides independent confirmation of the fiscal wisdom of the federal government's decision. It does not explain why the provinces were prepared to accept this, however.

49. "Bankers express relief over tax changes", The Globe and Mail (Toronto), June 19, 1971, p. B3.

50. "Tax changes appear bullish to TSE", The Globe and Mail (Toronto), June 19, 1971, p. B5.

51. "Chamber praises cut, letting Canadian firms be more competitive", The Globe and Mail (Toronto), June 19, 1971, p. B5.

52. The Globe and Mail (Toronto), June 22, 1971, p. B2.

53. "Accountants like cuts, reforms", The Globe and Mail (Toronto), June 19, 1971, p. B7; and "Accountant calls 'rose-coloured' budget outwardly simple but in fact complex", The Globe and Mail, June 21, 1970, p. 1.

54. Department of Finance, News Releases 71-6 (June 30, 1971), 71-80 (July 6), 71-94 (Aug. 4), 71-115 (Sept. 22).

55. E.J. Benson, "Address ...to the Law Society of Upper Canada ...August 26, 1971", Department of Finance, News Release 71-100,

Table 8-1
Changes in Corporation Income Tax Revenues
Resulting From Provisions of Bill C-259
(1972 revenues, $ million)

Changes from existing tax system	Impact in 1972	Post-transition impact
Reductions in corporation tax rate.....	---	-242
Additions to the tax base:		
- Realized net capital gains.....	10	46
- Elimination of exemption for income from new mines, less adjustment for additional acceleration of capital cost allowances...	---	11
- Revision of depletion allowances.....	---	57
- Elimination of deductibility of provincial mining taxes.....	---	34
- Miscellaneous changes.....	---	[illegible]
Other changes:		
- Additional abatement of taxes to provinces on mining income.....	---	-128
- Increase of the amount of income subject to a lower rate of tax, less the effect of restricting applicability of the low rate..	85	[illegible]
- Part IV tax on dividends received by private companies that are not currently paid out to shareholders.....	30	28
Total Changes	130	-14

Source: J. Bossons, "Economic Overview of the Tax Reform Legislation", in Report of the Twenty-third Tax Conference (Toronto: Canadian Tax Foundation, 1972), p. 49.

The only short-term change of any significance therefore was the tightening up of the dual rate of corporate tax, a reform whose time had come, in the view of most tax professionals if not of most businessmen. The largest longer term change was the government's commitment to gradually reduce the corporate tax rate to 46 per cent, an annual concession at maturity of about $242 million to the corporations. This more than offset the base-broadening changes which would have included half of realized capital gains, and the revision of the mining and petroleum provisions, to result in a modest net gain for the corporate sector.

There was also a redistribution of tax burden within the corporate sector, chiefly a transfer from mining and oil companies to other corporations. The change in the small business incentive would also have resulted in a redistribution of tax burden among corporations but a determination of the precise pattern would require a penetration of the links between a host of nominally separate corporations subject to common ownership or control.

As part of its overall project of a neutral tax system, the Carter Commission had recommended the removal of special tax privileges for particular industries and their replacement where clearly warranted by expenditure subsidies or by more efficient tax incentives. This was an integral part of the comprehensive income principle, that all additions to economic power should bear the same tax regardless of the source or form of the transaction. Measured against this standard, Bossons compiled the following list of industrial sectors and types of income, showing the relative percentage of reduction in tax subsidies from the pre-1969 system:

TABLE 8-2
RELATIVE IMPACT OF TAX REFORM
BY INDUSTRIAL SECTOR

Type of income	Extent of reduction of subsidies
mining industry	30%
petroleum industry	60%
life insurance	90%
other financial institutions	95%
capital gains	50%
employee benefits	95%

Source: J. Bossons, "The Analysis of Tax Reform", in L.H. Officer and L.B. Smith, eds. Issues in Canadian Economics (Toronto: McGraw-Hill, 1974), p. 307.

The relative success of the mining industry in Table 8-2 is over-stated, as it reflects the fifteen percentage point abatement of corporate mining taxes to the provinces, a gap which the latter could, and did move to fill. The relative relief, in terms of the reduced corporate rate and the failure to tax capital gains in full was shared by all corporations. Not shown in Bossons' figures are features not amenable to calculations based on anticipations of business behaviour. The deductibility of interest charges on inter-corporate buy-outs would probably be one of the major factors here, and would depend on the extent to which corporate boards took advantage of this provision. This suggests the utility of a separate study to determine to what extent the appointment of the Royal Commission on Corporate Concentration (the Bryce Commission) constituted a symbolic response to problems left unsolved or exacerbated by the government's earlier response to the Report of the Carter Commission.

The significance for the distribution of income of the relative success of the corporations to preserve their tax advantages in comparison to the poor and the wage- and salary-earners depends on the assumptions one makes in relating corporate income to individuals.[117] The Carter Commission had decided to conceive of corporations as simply conduits of income as far as resident individuals were concerned, consistent with its definition of income as being additions to the power of individuals over goods and services for end uses. It did not overlook the problem of corporate executives deriving personal benefit from the exercise of their corporate responsibilities (hence its recommendations to tax finge benefits) but

widespread agreement that the tax system was badly in need of reform, and both the Liberal and New Democratic Parties quarrelled, not with the need for the Royal Commission, but with the failure of the government to take more immediate action in the interim. As political events, these affected the extent to which the Conservative government could capitalize on its decision to appoint the Commission. The impetus for the decision itself came almost entirely from businessmen and tax professionals.

According to our decision-making framework, the definition of the problem and its insertion onto the political agenda was the joint project of the tax professionals and business community. The primary fora were the organizations of the tax professionals -- the Canadian Tax Foundation, the Canadian Institute of Chartered Accountants and the Canadian Bar Association, as well as other business and professional associations and meetings. The problem was defined in terms of the need of business executives and entrepreneurs to work in a favourable tax climate in order to promote economic growth. The concept of tax equity was heard only rarely in these fora, and even then, it was only horizontal equity -- equality of tax treatment so that all could compete on equal terms. Discussion of the need for greater vertical equity did not take place, and only occasionally did the tax professionals discuss the idea of extending the definition of taxable income to include capital gains, and then in the context of horizontal equity.

The business community and the tax professionals therefore had the

Notes to Chapter VIII

1. The preparation of the tax budget is described by Douglas G. Hartle, The Revenue Budget Process of the Government of Canada: Description, Appraisal, and Proposals (Toronto: Canadian Tax Foundation, Tax Paper No. 67, 1982), and by David A. Good, The Politics of Anticipation: Making Canadian Federal Tax Policy (Ottawa: Carleton University School of Public Administration, 1980).
2. "Summary of 1971 Tax Reform Legislation", pp. 29, 72.
3. Ibid., p. 32.
4. Ibid., p. 33.
5. Ibid., pp. 33-34.
6. Ibid., pp. 35, 36, 76.
7. Ibid., p. 36.
8. Ibid., pp. 37-39, 76
9. Ibid., p. 37.
10. Ibid., p. 45.
11. Ibid., p. 50.
12. Ibid., pp. 51-51.
13. Ibid., pp. 52-54, 86-88.
14. Ibid., pp. 55-57, 90.
15. This referred to corporations which did practically all their business in a foreign country. See the White Paper, p. 76.
16. Ibid., p. 57, 90.
17. Ibid., p. 58.
18. White Paper, Tables 4-9, pp. 27-32; see above, Ch. 7, p. 557.
19. Ibid., pp. 11, 17, 70.
20. Ibid., Tables
21. Ibid., p. 11. Most of the reduction is accounted for by the removal of the 3 per cent income surtax which was expected to have yielded $305 million in 1972.
22. Ibid., pp. 61.
23. See above, Ch. 7, pp. 582.
24. Ibid., p. 61.
25. Ibid., pp. 12-13, 70.
26. Ibid., pp. 8, 66.
27. See Ch. 7, pp. 583-584.
28. Benson interview.
29. "The tax integration arguments differ in detail, not principle", The Globe and Mail (Toronto), Mar. 3, 1970, p. B2.
30. See above, Ch. 7, p. 578-579.
31. See above, Ch. 7, pp. 571-572.
32. See above, Ch. 6, pp. 467-468.
33. See above, Ch. 7, p. 523.
34. Ronald Anderson, "Alternative to extreme action.-- Revised tax reform in 3 stages urged to terminate furor", The Globe and Mail (Toronto), Feb 26, 1970, p. B3; and "The tax integration arguments differ in detail, not principle", The Globe and Mail, Mar. 3 1970, p. B2.
35. "Summary of 1971 Tax Reform Legislation", p. 33.
36. Ibid., p. 33.
37. See above, Ch. 6, esp. pp. 456-458.

78. "Revisions to estate tax likely in place of capital gains plan", The Globe and Mail (Toronto), Mar. 11, 1971, p. B1; and Ronald Anderson, "Capital gains tax war is over; fight shifts to death duties", The Globe and Mail, Mar. 24, 1970, p. B2.
79. "Reduction in estate tax rates probably most sensible policy", The Globe and Mail (Toronto), April 3, 1971, p. B9. Not all practitioners were prepared to go this far, however: R.D. Brown argued for the continuation of the Estate Tax with a combination of increased exemptions and reduced rates. See R.D. Brown, "The Taxation of Capital Gains", Report of the Twenty-second Tax Conference, pp. 63-65; and Ronald Anderson, "reduction in estate tax rates probably most sensible policy", The Globe and Mail (Toronto), April 3, 1970, p. B2.
80. See Ch. 5, pp. 339-342; 345-349.
81. When the federal government was considering estate and succession duties during the Second World War, Bryce had favoured taxing bequests according to the income of the recipient, rather than according to the size of the estate, as favoured by Kenneth Eaton. Bryce interview.
82. See Ch. 7, above, p. 511.
83. "Text of a speech by the Honourable E.J. Benson ...February 5, 1969; House of Commons Debates, Feb. 5, 1969, p. 5179.
84. We cannot state that precisely the top five per cent of income-earners would receive the benefit, though one would expect it to remain very largely within the families which had, through their ample and only partially taxed incomes, accumulated estates large enough to exceed the exemptions provided under the Estate Tax Act.
85. Ibid.
86. Ibid.
87. Bryce interview. This was confirmed in an interview with another Department of Finance official.
88. Benson interview. An analysis of projected revenues from the estate tax and from deemed realizations at death by John Bossons, ("An Economic Overview of the Tax Reform Legislation", pp. 56-57) provides independent confirmation of the fiscal wisdom of the federal government's decision. It does not explain why the provinces were prepared to accept this, however.
89. "Bankers express relief over tax changes", The Globe and Mail (Toronto), June 19, 1971, p. B3.
90. "Tax changes appear bullish to TSE", The Globe and Mail (Toronto), June 19, 1971, p. B5.
91. "Chamber praises cut, letting Canadian firms be more competitive", The Globe and Mail (Toronto), June 19, 1971, p. B5.
92. The Globe and Mail (Toronto), June 22, 1971, p. B2.
93. "Accountants like cuts, reforms", The Globe and Mail (Toronto), June 19, 1971, p. B7; and "Accountant calls 'rose-coloured' budget outwardly simple but in fact complex", The Globe and Mail, June 21, 1970, p. 1.
94. Department of Finance, News Releases 71-6 (June 30, 1971), 71-80 (July 6), 71-94 (Aug. 4), 71-115 (Sept. 22).
95. E.J. Benson, "Address ...to the Law Society of Upper Canada ...August 26, 1971", Department of Finance, News Release 71-100,

Aug. 2[illegible], 19[illegible].

56. E.J. Benson, "Address ... to the Law Society of Upper Canada"

57. Margaret Anne Kipp, The Co-Operative Union of Canada Carleton University, Ottawa, unpublished M.A. dissertation, 19[illegible].

58. House of Commons Debates, Oct. 1[illegible], 1971, p. 8640.

59. Quoted by Gilbert Rondeau, Member of Parliament for Sheffield, Ibid., Dec. 2, 1971, p. 10372.

60. Ibid.

61. Ibid., Oct. 12, 1971, pp. 85[illegible]-86[illegible].

62. Ibid.

63. Ibid., Oct. 12, p. 8611.

64. Ibid., Oct. 2[illegible], pp. 886[illegible]-886[illegible].

65. Ibid., Dec. 14, 1971, p. 1044[illegible].

66. Ibid., Oct. 12, 1971, p. 86[illegible].

67. Ibid., Oct. 12, 1971, p. 8604.

68. Ibid., Oct. 12, 1971, p. 8618.

69. Ibid., Oct. 12, 1971, pp. 8618-8621.

70. Ibid., Dec. 10, 1971, pp. 10367-10370.

71. Standing Senate Committee on Banking Minutes of Proceedings and Evidence, Sept. 29, 1971, p. 35:5.

72. Campbell, pp. 16-17.

73. House of Commons Debates, Dec. 10, 1971, p. 359.

74. Ibid.

75. Report of the Twenty-fourth Tax Conference, Toronto: Canadian Tax Foundation, 1973), p. 12.

76. House of Commons Debates, Oct. 13, 1971, p. 8641.

77. Ibid.

78. Ibid., Dec. 10, 1971, p. 10374.

79. The Globe and Mail (Toronto), Dec. 13, 1971, p. 11.

80. House of Commons Debates, Dec. 17, 1971, p. 10531.

81. Ibid., Dec. 16, 1971, p. 10553.

82. Ibid.

83. Ibid., p. 10553.

84. Ibid.

85. Ibid.

86. This account of the lobbying efforts of the co-operatives is taken from Margaret Kipp, The Co-operative Union of Canada. Kipp (p. 24) attributes to the Royal Commission "a prime motivating factor in the CUC's second reorganization ... [which turned it] into an organization of large, financially strong co-operatives."

87. Ibid., p. 153, 160.

88. Ibid., pp. 157-159.

89. Ibid., p. 159

90. Benson interview.

91. Kipp, The Co-operative Union of Canada, pp. 159-160.

92. Ibid., p. 157.

93. Ibid., p. 161.

94. Ibid.

95. Ibid.

96. Ibid., pp. 162-163.

97. House of Commons Debates, Dec. 2, 1971, pp. 10076-10077.

98. Ibid., Dec. 2, p. 10092.

99. Ibid., Dec. 14, 1971, p. 10435.

100. Ibid., Dec. 16, 1971, p. 10534.
101. Ibid., Dec. 17, p. 10583.
102. Ibid.
103. Ibid.
104. "Notes for an address by the Honourable P.M. Mahoney, Minister of State to a joint meeting of Estate Planning Professions, Skyline Hotel, Ottawa, Ontario, Thursday, February, 24, 1972" (Ottawa: Department of Finance, News Release No. 72-19).
105. "Nine years for naught, but democracy", in Spotlight on Tax Reform (Toronto: Canadian Institute of Chartered Accountants, 1972), p. 2.
106. Ibid.
107. John Bossons, "Economic Overview of the Tax Reform Legislation", Proceedings of the Twenty-third Tax Conference, (Toronto: Canadian Tax Foundation, 1972), p. 60.
108. Ibid., pp. 55-59.
109. Ibid., pp. 54-55.
110. House of Commons Debates, Feb. 5, 1969, p. 5179; see above, Ch. 7, pp. 511.
111. Bossons, "Economic overview...", p. 55.
112. Ibid., p. 60.
113. Ibid..
114. Ibid., pp. 57, 60.
115. The Redistribution of Income in Canada (Toronto: McClelland and Stewart, Carleton Library, No. 124, 1980), pp. 165-167.
116. Ibid.
117. W.I. Gillespie's conclusion that the 1971 tax reform and other federal tax policies during the early 1970's failed to redistribute income in a progressive direction was consistent with a range of assumptions allocating corporate and other income to individuals. See: The Redistribution of Income in Canada, pp. 170-172.

Chapter IX: Tax Reform and the Democratic Process

The Odyssey of the Comprehensive Income Concept

This study has presented both a case-study of the tax reform process and the odyssey of an idea. The principle that all additions to individual economic power constituted income and that all income ought to be treated the same way for tax purposes was an idea widely accepted among academic economists and public finance specialists in most Western countries, and especially in the United States. While it had found support in the minority report of the 1954 United Kingdom Royal Commission on the Taxation of Profits and Income, and in principle, from economic advisors to the new Kennedy Administration in the United States, its life in Canada was confined to the American public finance texts used in the universities.

The frustrations of businessmen and tax professionals with the Canadian income tax system changed all that. The economy was in the doldrums at the beginning of the 1960's and business spokesmen were increasingly blaming Canada's sluggish economic growth on the tax system. They said that the rates on personal income were too high for the talented, the energetic and those willing to risk their savings to invest in productive ventures. There should be tax incentives to encourage investment and innovation. The tax system was too complicated and its rules too unpredictable, making business planning slow, risky and expensive. Too often disputes arising from the seemingly arbitrary assessments of taxation officials were settled years later in the courts and even then, in an unpredictable fashion.

No-one knew for certain where the boundary was between income (taxable at rates as high as 81 per cent) and tax-free capital gains. Many were resorting to subtle methods to escape the high tax liabilities, causing taxation officials to add further complications to the system in order to protect the state revenues, while successive governments oscillated between closing loopholes and acceding to business pressure to alleviate the tax burden on certain transactions and types of income. The revenue loss resulting from tax avoidance and special tax concessions, combined with growing government expenditures, prevented any general lowering of tax rates such as had taken place during the 1920's and in the years immediately following the Second World War. Combined with the revenue needs was the requirement perceived by government politicians and senior officials to maintain the appearance of a progressive tax system by retaining the nominally high marginal rates on large incomes. Behind this perception was the fear was that widespread knowledge of the real distribution of the tax burden would fuel political radicalism, and threaten the balance between private enterprise and state intervention achieved during the post-War period.[1]

As the Carter Commission pointed out later, broadening the tax base to include capital gains, and eliminating other tax preferences would have permitted a substantial lowering of the rates for all taxpayers, but that was a speculative and somewhat subversive notion before the Commission submitted its Report. It had occasionally been raised by the odd maverick tax professional, only to be firmly put down by his more responsible colleagues.

With the recession of 1960-61, the professional and business dissatisfaction coalesced into a demand for a thorough reform of the tax system to encourage economic growth. The reform agenda was that put forth by business spokesmen and tax professionals at the Canadian Tax Foundation conferences, annual corporate meetings and other business and professional meetings. The message was carried to the public and to politicians through media reporting of their utterances. The Toronto Globe and Mail was especially keen on the reform project, with its editor, Oakley Dalgleish, not only championing the cause on the editorial page and reporting the gospel of its advocates in the news pages, but also personally persuading Ontario's Premier Leslie Frost and Prime Minister John Diefenbaker of the need to appoint a Royal Commission to study the tax system and recommend reforms. Business, in the person of Wallace McCutcheon, a member of the Argus group, controlling the largest corporate empire in Canada, applied pressure more directly on Mr. Diefenbaker to appoint a Royal Commission. With the Conservatives' popularity waning, its economic policies in apparent disarray, an election in the offing, Mr. Diefenbaker felt he needed the support of business and the Globe and Mail. The price, the appointment of McCutcheon to the Senate and the Cabinet as Minister of Trade and Commerce, and the promise of a Royal Commission on taxation if re-elected, did not seem unreasonably high.

There is no evidence of any widespread tax revolt among the poor, the working class, or the salaried middle class. Editorial opinion following the appointment of the Commission suggests that there was

widespread agreement that the tax system was badly in need of reform, and both the Liberal and New Democratic Parties quarrelled, not with the need for the Royal Commission, but with the failure of the government to take more immediate action in the interim. As political events, these affected the extent to which the Conservative government could capitalize on its decision to appoint the Commission. The impetus for the decision itself came almost entirely from businessmen and tax professionals.

According to our decision-making framework, the definition of the problem and its insertion onto the political agenda was the joint project of the tax professionals and business community. The primary fora were the organizations of the tax professionals -- the Canadian Tax Foundation, the Canadian Institute of Chartered Accountants and the Canadian Bar Association, as well as other business and professional associations and meetings. The problem was defined in terms of the need of business executives and entrepreneurs to work in a favourable tax climate in order to promote economic growth. The concept of tax equity was heard only rarely in these fora, and even then, it was only horizontal equity -- equality of tax treatment so that all could compete on equal terms. Discussion of the need for greater vertical equity did not take place, and only occasionally did the tax professionals discuss the idea of extending the definition of taxable income to include capital gains, and then in the context of horizontal equity.

The business community and the tax professionals therefore had the

decisive influence in determining both the initial definition of the problem and of the institutional form that the problem-solving activities would assume. At least three of the seven members of the Royal Commission were chosen from among the tax professionals, with a fourth (Grant) being a lawyer and executive of a trust company. The Commission's Counsel, John Stewart, the most influential senior staff member of the Commission aside from Hartle, was a successful tax lawyer and professional colleague of Carter's. Most of the research staff on the tax structure side were tax professionals, as were many of the specialists who performed contract research for the Commission and reviewed many of the staff studies. Since the analysis of the Commission's records and interviews with key Commission members and staff indicated that the content of the briefs and hearings played little part in determining the Commission's recommendations favouring the comprehensive income concept, this study has not examined the balance of representation of interests whose views were placed before the Commission. However, the list of witnesses and of the authors of briefs published with the Commission's Report supports the conclusion that, as was the case for the later stages of tax reform, business interests and tax professionals dominated the "public participation" in much the same way as during the White Paper debate.[2] An analysis of the briefs by Gardner led him to the same conclusion.[3]

Although providing raw material and hypotheses for the Commission's research staff to test, the briefs and hearings did not constrain its efforts to search for and evaluate alternative solutions, and in the process, to re-define the problem. Nor did the

all-encompassing terms of reference for the Commission inhibit it from considering the whole question in depth, allowing it to critically re-examine some of the basic assumptions about taxation widely propagated by the business community and tax practitioners.

The effective constraints on the Commission's decision-making processes were more related to political and practical contingencies: the internal power struggle within the Commission's senior staff regarding the Commission's organization and the basic research strategy, the frustrations of assembling and organizing a competent research staff when levels of remuneration and authority to pay rested with Treasury Board, the efforts required to come to terms with a skeptical and occasionally hostile government bureaucracy, and the impatience of Walter Gordon and the new Liberal government to incorporate tax reforms in up-coming budgets. In some cases, the resolution of these tensions was of considerable import for the content of the Commission's Report, notably Hartle's acquisition of full control over the Commission's research effort, and the Commission's ability to repeatedly postpone its reporting date. Had these events worked themselves out in a different fashion it is very likely that the Report would have been a more short-term, practical document, more expedient, and less concerned with optimum solutions to fundamental problems of the tax system. Other problems facing the Commission, such as those of assembling the research staff, organizing the research effort and meshing it with the deliberations of the Commission, were all time-consuming and exhausting, indicative of a highly inefficient way to produce a document defending the

comprehensive tax base. In retrospect, the Commission should have been able to do the necessary research and produce its Report with a fraction of the time and resources. However, this ignores the learning effect which two full years of concentrated collective effort had on the key members of the Commission and their staff. It was only after laboriously sifting through mountains of straw that the Commission's decision-makers could see and appreciate the jewel that remained.

Aside from the sheer comprehensiveness, coherence and tight logic of the Commission's argument for the comprehensive tax base, what impresses one most is the number of contingencies in the process required to give the Report its remarkable qualities. The backgrounds of the Commissioners suggest that the Diefenbaker government had appointed a competent but "safe" commission. No-one expected anything radical to come out of it. It was dominated by tax professionals and businessmen, and without any representation from organized labour. Carter was known to be generally conservative in his views, and his firm had helped to drill the many loopholes in the existing tax system. Perry was one of Canada's foremost tax specialists, one of the few who was not either a lawyer or chartered accountant, but a former taxation official in the Department of Finance, and the former Executive Director of the main organization of the tax professionals, the Canadian Tax Foundation. Probably no-one else in the country knew the existing system more extensively, or how it got there. Implicated in the development of the existing system, a loyal civil servant, long-time friend and associate of the tax professionals, trusted by

the bankers as Executive Director of the Canadian Bankers' Association, he was expected to deliver to the Commission knowledge, competence, and experience, not a dangerous imagination. Nor would anything radical have been expected from the other commissioners.

It took a long series of happenings to convert a majority of the commissioners to the comprehensive tax base. The acquisition by the Commission of the services of Douglas Hartle and Geoffrey Conway turned out to be key events. Conway was a qualified economist and chartered accountant and had been doing graduate work at Harvard on capital gains taxation. His study for the Commission advocating the taxation of capital gains, and the companion study of capital gains jurisprudence done with John G. Smith, were crucial in winning John Stewart and the majority of commissioners over to the inclusion of capital gains in income. Carter would likely not have been persuaded had it not been for his respect for the sober judgement of Stewart, and for the two-year learning process into which Carter had thrown himself. His interviews with tax specialists and administrators in the United States and Europe had made him skeptical of the utility of tax incentives and opened his mind to a wide range of alternative modes of taxation, one of them being the inclusion of capital gains in income. Eisenstein's book, The Ideologies of Taxation, had alerted him to the self-serving nature and lack of logical consistency of most utterances on taxation, especialy those of his colleagues in the law and accounting professions.

Although the commissioners and their staffs continued to be

exposed to news reports and other contemporary stimuli, their work, protected by the tight secrecy of the Commission, was relatively insulated from the pressures and influences of the business community and tax professionals. They continued to listen to different points of view, some of which were repeatedly argued in brief after brief, but they kept counsel. Royal Commissions have an aura of authority, prestige and objectivity, encouraging its members and their staff to stand above the object of the enquiry and to present a judgement which, in standing the test of time, will reflect credit on those associated with it long after the government which had appointed it has been forgotten. It was this desire to do something worthwhile, which would have a lasting beneficial effect, which motivated Hartle to plead with Carter to postpone the reporting date, Harvey Brazer to appeal to Carter in very similar terms, and Carter to accept the challenging standard for the Report for which Hartle had argued.

Factors specific to decision-making through royal commissions: the insulation of privacy, the concentration and duration of responsibility and effort, and the atmosphere of occasion -- that a few individuals had the rare opportunity to make an historic contribution -- all played a part in overcoming the normally decisive influence exerted by the business community and tax professionals in tax policy matters. When the commission stage of the process was concluded the effects of business and tax professional dominance again began to take effect. Two of the Commissioners, Beauvais and Grant, never did accept the comprehensive tax base in the rigour defended in the majority Report, and their minority reports represented the

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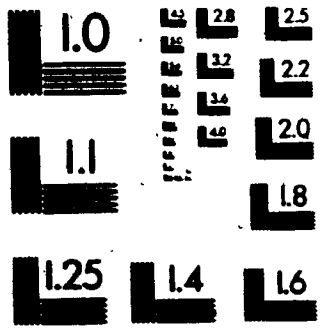

beginning of a movement within the business community and among tax professionals to discredit the majority Report.

However, public debate could not return to the same level as before the Commission's appointment, as its Report had permanently changed the definition of the problem, or at least provided a powerful alternative definition. Discussions of capital gains were no longer characterized by conjecture over the advantages or disadvantages of extending the tax base. The Commission had drawn up a blue-print for a complete taxation system including capital gains as an integral and necessary part of income. The Commission had also taken up the challenge of business to design a tax system which encouraged investment and economic growth, pointing out that the existing system was so inefficient and inequitable that it was possible to have a tax system that substantially improved both equity and contributed more to economic growth. A major part of the inefficiency in the existing system was the prevalence of loopholes through which wealthy taxpayers deprived the state of a substantial portion of its potential revenues, with the result that wage and salary-earners paid much more than their share. Hence the Commission further re-defined the problem by shattering the myth of the progressive tax system. Businessmen and tax professionals had complained that the system was too progressive. Some had been advocating a flat-rate tax, with a constant marginal rate applicable regardless of income level, while others were calling for reduced emphasis on direct taxes and more on indirect commodity taxes. The Carter Commission, in effect, accused the wealthy of not paying their share, and revealed the effect of the tax professionals

in abetting the avoidance activities of their wealthy clients. This demystification of the tax system explains much of the outrage of the businessmen and tax professionals which surprised the Commissioners and their staff.

With a competing definition of the problem and proposed solution in the public domain, many businessmen and tax professionals began to discover the merits of the existing system. Others looked to the American system with its preferred treatment for capital gains as a possible model. The press was flooded with professional and business denunciations of the Report, with meetings of the Tax Foundation, professional and business conferences and annual corporate meetings providing numerous occasions for making anti-Carter news. There were many arguments put forward in opposition to the Carter recommendations but the one common to almost all of them was that investors would not be prepared to risk their savings if they knew that half of the profits would be taxed away. A flight of capital out of the country was predicted, especially in the mining and petroleum industries, with a consequent loss of employment and collapse of the economies of regions dependent on resource development. Warnings of dire consequences such as these were repeated over and over by tax professionals and corporate executives, with many being in positions to influence the investment decisions of major corporations, thereby contributing to the very consequences they were predicting.

The last Pearson government had been the hapless recipient of the Commission's Report. Aware from the advance study of the Report

carried out by the Tax Analysis Unit that the Commission's recommendations could not be implemented without alienating the corporate support for the Liberal Party, the government rejected the hand dealt it by the Commission, and the then Minister of Finance, Mitchell Sharp asked his Department to re-shuffle the cards. In order to play for more time Sharp asked interested parties to add some new cards to the deck by sending in briefs commenting on the major recommendations. Over 900 briefs were received, nearly all of them the product of collaboration between businessmen and tax professionals, and in comparable proportion, against the recommendations respecting the comprehensive tax base. This creative delay, combined with the Liberals' prudent silence on the question of tax reform during the 1968 election, allowed Pierre Trudeau to ride an ideologically ill-defined coalition of business and reform-minded popular support to establish the first majority government since 1962.

Though some ministers in the first Trudeau government would have been happy to allow it to do so, tax reform could not wait forever. At least two ministers, Edgar Benson and Eric Kierans, were anxious to push ahead, but any formula based on the Carter recommendations would have divided the Cabinet and the Party. Mr. Benson's change of heart on a draft bill versus a white paper signaled the government's division and indecision. The white paper route ultimately won out because all the significant external pressures -- business, tax professionals, the provincial governments and the major opposition party -- were all demanding it, and it allowed the government to test the winds of "public" reaction before taking any responsibility for

reform legislation.

The formulation of the White Paper represented the second time during the tax reform decade that the decision-making process retreated into a closed forum. Though the shield of secrecy was as effective as it had been during the internal deliberations of the Carter Commission, the protection from exernal pressures was not nearly as effective. Consideration of alternatives had to take account of the political consequences for the government as well as of the desirable objectives listed by the Carter Commission, and which the government later professed to share. As the records of this process remain closed, we have been permitted only fragmentary glimpses of a process which began with a technical analysis of the Carter Report and the production of a range of alternative policy options within the Department of Finance and ended with Cabinet approval of the White Paper. As was the case during the Commission stage, the tax professionals played an important part in the process, both as career officers and as consultants brought in for limited periods. To some degree there appears to have been an analogous shift in perspective of the private practitioners once immersed in an environment where problems were approached from a more public-interest viewpoint than that to which they had been accustomed in the private sector.

However, the effect of this "contagion from the public sector" was greatly moderated by political constraints emanating from Cabinet through the Minister's office, and interpreted and anticipated at the

senior bureaucratic level. This process of "anticipation", the formulation of budgetary proposals with a form and content which "will wash" with the Minister, Cabinet and the relevant public has been described by David Good for the period following tax reform.[4] The changes under consideration during the tax reform period went beyond the range of incremental changes which generally emerge from such a process, and the White Paper deviated too far from the limits of acceptable tax policy set by known "attentive actors" for this model of decision-making to be applicable. However, the disjointed and very narrow range of options put before the Tax Reform Committee of Cabinet described by Eric Kierans support the view that significant policy options were screened out in the Department of Finance's Tax Review Committee and in the Minister's Office.[5] As Good points out, the anticipatory process, when it works smoothly, operates very subtly in the minds of the participants. Knowing the "starters" from the "non-starters" was an important part of the mental working tools of each official in the chain of tax policy formation.[6] The Carter Commission's formula for the comprehensive tax base, though admired in a technical sense by Finance officials, was understood to be a "non-starter".

Much as the comprehensive tax base was denounced by business interests and most tax practitioners, it had much to commend itself to government. Governments were perpetually seeking new sources of revenue as alternatives to raising the rates on existing taxes or cutting back popular expenditure programmes. Thanks to the Carter Report, broadening the tax base could be defended on grounds of

horizontal and vertical equity, and promoting economic growth, while at the same time adding new revenue sources. While it is true that the Carter Report, consistent with its terms of reference, recommended a system to raise as much but no more revenue than the existing system, it is clear that a more efficient tax system operating at lower marginal rates increased the potential revenues which might be extracted given the stimulus of a demand for greater expenditures. The rise of social expenditures at the end of the Second World War was made possible through the increased fiscal capacity occasioned by the strengthened system of wartime taxation.[7] The senior civil service of the 1960's were generally oriented toward a more interventionist state and the tax system recommended by the Carter report would help to provide the wherewithall. This was hinted in the Report itself, when, in abstaining from recommending a negative income tax, it advocated a general re-appraisal of income transfer programmes.

This fear of a strengthened public sector was the second major theme of the opposition to the Carter Report and the White Paper, both repeatedly denounced as "socialist", "communist" and "red". Often the charges were put more subtly, in terms of the Report or White Paper envisaging a different society from the one Canadians had grown up and prospered in. The red-baiting of the tax reform proposals and proponents was also linked to the frankly re-distributive aims of both the Commission's and the White Paper's recommendations. One thing about the political system which businessmen and tax professionals clearly understood or intuited was the historic sanctity of private property rights within the parliamentary system, and the links between

the protection of private property from taxation and the development of both parliamentary institutions and civil liberties. They tended to regard taxation as a form of theft or extortion imposed on them by governments beholden to the votes of the greedy masses, especially to the degree that government revenues went to fund social welfare programmes. This sentiment often found expression at the annual tax conferences during the 1960's.

The Commissioners, perhaps somewhat quixotically, had asked Canadians to hold their own private interests temporarily in suspense and allow themselves to be convinced that their proposed system would, as a package, work to the general good and before long, to everyone's material benefit. An important part of the propaganda effort directed by the business community and tax professionals against the Report was to undermine the credibility of this argument. Taxpayers were warned repeatedly that, regardless of the fate of integration, averaging, and other "money losers", the government would not be able to resist the temptation to adopt the more punitive measures such as the full taxation of capital gains, the elimination of the dual corporate rate, and the taxation of employee fringe benefits. To the extent that such fears were generated among small businessmen, middle-income shareholders, and amid the corporate sector outside those industries earmarked for removal of special privileges, the warnings had the effect of building a more solid front of opposition to the Report.

In spite of the nearly unanimous outrage of business and of the opposition of most tax professionals from the private sector, the

Report was supported by organised labour, the New Democratic Party, and most tax professionals based in universities. While representing only a small minority of articulate opinion, it was forceful enough to prevent the government from openly conceding to demands from business and the tax professionals to drop the Report and continue with the customary practice of incremental amendment of the existing tax system. This unequal polarization among relevant opinion-makers left the government between the two stools of its business and professional support on one hand and its hitherto successful strategy of progressive populism on the other. The intended role of the White Paper was to re-define the problem of tax reform a second time and build a moderate coalition of support around a compromise version of the comprehensive tax base.

The government was aware that the strategy was risky, since it could not be sure whether the supporters of the Carter Report and its more moderate critics could be united behind a new set of reform proposals, and if it were possible, where the optimum compromise was to be found. The white paper strategy allowed the government to hedge until it was clear what the business community would tolerate, and what the propaganda of business, the tax professionals, and all other actors could persuade the wider public to accept. What emerged as the White Paper represented a guess by Edgar Benson and senior Finance officials as to what the government could get away with as an initial position without undermining its credibility. Mr. Benson never expected that this position would survive the White Paper debate. Although the proposals represented a fairly coherent income tax

system, they lacked the logical consistency of the Carter Report. The major departure from the Carter formula -- notably the half taxation of capital gains on widely-held corporate shares combined with five-year deemed realization and half integration -- suggested a more flexible and eclectic approach. Its near-total rejection by the tax professionals, which surely must have been anticipated by Brown and his officials, supports the hypothesis that it was put forward by the government purely as a point of departure. Through the process of its rejection, however, it served to underscore the validity of the logic in the Carter recommendation for deemed realization of capital gains at death. While heaping ridicule on the closely-held versus widely-held distinction between corporations and the five-year deemed realization of accrued gains on widely-held shares, the tax professionals felt themselves being steered back toward the Carter formula of deemed realization at death.

Seen in this light, the 1968-69 reform to the Estate Tax represented the fortifying of a bargaining chip for the federal government, to be used in negotiations with business and with the provinces. This reform considerably increased the burden on transfers of wealth within the upper-class, while at the same time providing some assurance that the government was not wedded to the comprehensive tax base. In attacking the White Paper's five-year deemed realization of accrued capital gains on widely-held corporate shares, the tax professionals knew they had to suggest what would be acceptable in its place. Increasingly they came to favour deemed realization at death with a reduction in the weight of estate taxes. Business spokesmen

and several provincial governments also spoke in favour of this idea.

However, nothing in the Carter Report had implied that the taxation of gifts and bequests should be thought of as an alternative to the taxation of capital gains. Both were separate entities: increments in the value of assets were income to their owners, while gifts and bequests represented income to the recipients or beneficiaries. To the original owners of the property, the gifts or bequests represented simply a form of consumption, or realization. The temporal juxtaposition of the application of the two taxes on the death of the property-holder -- one on the estate of the deceased, and the other on the income to the beneficiary -- was a result of the life-long tax holiday enjoyed by the deceased on his unrealized capital gains. In the eyes of the wealthy and of their estate planners, however, this amounted to double taxation, even confiscation. The outrage which this proposal evoked represents, for those sharing the perspective of the Carter Report, a rough measure of the magnitude of income which had gone untaxed.

Having proposed the inclusion of gifts and bequests in income, the Carter Commission had logically recommended the abolition of all estate taxes and succession duties. The Commission was saying, in effect, that inclusion of gifts and bequests in taxable income constituted a more equitable alternative to separate gift and estate taxes. By reforming the Estate Tax before the publication of the White Paper, Mr. Benson encouraged participants to lose sight of the Carter Commission's perspective on wealth transfers and think of the

tax as potentially an alternative, not to the inclusion of gifts and bequests in taxable income, but to deemed realization of accrued capital gains at death.

The government's attempt to re-define the problem of tax reform in order to permit a compromise solution was a qualified success. The New Democratic Party had, after some hesitation, supported the White Paper, thereby adding to the document's reform credentials. Academic tax specialists generally remained more critical however, finding the White Paper to be a less successful attempt than the Carter Report to come to terms with both equity and growth objectives. However, the Carter definition of tax reform was no longer on the political agenda, depriving this criticism of much of its political effect. The government's "Summary of 1971 Tax Reform Legislation", while including a comparative listing of the features of the existing system, the White Paper, the two parliamentary committee reports, and Bill C-259, did not include the Carter recommendations.

As many tax professionals recognized, however, the compromise solution was flawed in that it did not solve the structural tax problems which set the whole tax reform process in motion more than a decade earlier. The problem of distinguishing capital gains from income, and the temptations for surplus stripping and other forms of tax avoidance, though partially mitigated, still remained. Having re-defined the problem to permit a politically acceptable "solution", the government failed to solve the substantive problems which gave rise to the controversy.

Nearly everyone had some cause to be unhappy with the results of tax reform. The disruption of routine, the intrusion of non-government people into the policy-formulation machinery, and the change-over to a new system was upsetting and exhausting to government officials. Tax professionals participating at the centre of the reform process in Ottawa found personal and business relationships strained by their implication in the reform project. All tax practitioners suffered the instantaneous obsolescence of their inventories of career-long accumulations of tax wisdom. The maintenance of professional competence would henceforth require a greater effort to master the unfamiliar complexities of the new system. Liberal politicians never succeeded in healing the rift between themselves and the business community which developed over Walter Gordon's first budget and widened over tax reform.[8] The Tories watched their Liberal opponents wiggle one more time out of an apparently hopeless dilemma, while the New Democrats watched what had promised to be an ideal political issue slip from their grasp. Business, large and small, lost some of their tax loopholes, at least until their tax advisors had had time to thoroughly case the new system. For all its frustrations, the old system had provided enterprising businessmen with a low average tax burden while preserving the outward impression that they were over-taxed. The future looked more threatening and uncertain: how long would the growing revenue needs of government allow it to tax only half of capital gains? Wage and salary earners, to the extent that they were not oblivious to the process, suffered through being shown the

promised land in the Carter Report then having it quietly snatched away from them. The poor, passive victims of the failure to materially re-distribute the tax burden, continued to bear a relatively heavy burden from indirect taxes. To the extent that the failure to implement the Carter recommendations compromised the pursuit of the collective values espoused by the Commission -- fairness, more goods and services, full employment without inflation, a free society, and a strong, independent federation -- all Canadians had lost something of value.

However, tax reform had also been a vehicle for the upward mobility for youthful ambition. Presumably talent would find its way to the top regardless of the need to reform the tax system, though one is struck by the list of the later prominent professionals, public servants and politicians who were connected with the Carter Commission. Nearly every major law and accounting firm and most university economics departments and law schools had one or more "graduates" of the Royal Commission. Others went to responsible positions in the Department of Finance and in Treasury Board. Michael Pitfield, having "lost" the struggle for control over the Commission's organization, became Clerk of the Privy Council, serving Pierre Trudeau, whose services he had once retained on behalf of the Commission. Marc Lalonde, once a special advisor to Carter, became Principal Secretary in the Prime Minister's Office and later one of the most powerful cabinet ministers. Having so many "old friends" in positions of power did not help in getting the Commission's recommendations accepted, however.

The maze of careers which criss-crossed in and out of the story of tax reform provide some indication of the small size of the relevant public for discussions of tax policy. A combination of factors -- the inherent complexity of the tax system, the controls on entry to the tax professions, the very high marginal productivity of most tax professionals (an hour's time of a good tax lawyer could save a corporate taxpayer many thousands of dollars), and the organization of business interests into associations -- all encouraged the formation of a relatively small number of technically very competent, highly paid tax specialists. Given the pattern of their working relationships, the fact that most significant matters affecting tax policy and administration centre on two federal departments in Ottawa, and the interaction encouraged through professional associations and the logic of their work situation (the value of a tax advisor to his client depends on, among other things, the usefulness of his "contacts"), most members of the tax professions knew, or knew of the others. The tax professional working in the Department of Finance or National Revenue at one time was likely to have once worked as a tax practitioner in the private sector, or likely would do so at some time in the future.

The closeness of the community of tax professionals encouraged the transmission of common assumptions and opinions about taxation. It is noteworthy that the tax professionals based in universities and generally following separate career patterns, tended to deviate more from the dominant norms of the private-sector professionals. This

phenomenon of the inter-penetration of corporate and bureaucratic worlds had been observed by John Porter at the senior bureaucratic level, prompting his concern that the extensive inter-penetration of the business and corporate elites would strengthen the dominance of the latter and erode the delicate balance of independent, competing elites which preserved a measure of democratic pluralism for the society as a whole.[9] Porter had nevertheless concluded that the incidence of career linkages between the bureaucratic and corporate elites had not reached the point of threatening the relative autonomy of the bureaucratic elite.[10] He said this was the case particularly with the Departments of Finance and External Affairs, a position not supported by this study for the tax reform period, as far as careers related to tax policy are concerned. In the case of that portion of the federal bureaucracy concerned with tax policy and administration, this inter-penetration has been very extensive down to the working officer level. While the notion of competing elites may have had some validity during the post-War period covered by Porter, the present study has found the bureaucratic, political and corporate centres of power to be linked by the tax professionals -- an identifiable social category of individuals with common professional backgrounds, playing common social and economic roles, and with a tendency to share common assumptions about the economic organization of Canadian society. The public sector institutions discussed in the preceeding chapters, both political and bureaucratic, although formally exercising regulating functions on tax-related activities in the private sector, resemble more the frontier outposts of corporate power than independent, competing centres of power. The image of frontier outposts is used

because, although the agents of corporate power dominate all other social categories in the public sector institutions, their dominance is never more than contingent, limited by universal suffrage and the pandering to the expensive wants of the masses which it engenders.

One effect of tax reform may well have been to enlarge the community of tax professionals. When Douglas Hartle was trying to recruit economists to his research staff, he had difficulty finding Canadians qualified in public finance. The course of tax reform has ensured that there is now a more adequate supply. Coopers, Lybrand and Co. (formerly McDonald, Currie and Co.) acquired its first chartered accountant who specialized entirely in taxation only in 1954. By 1983 the firm had over 200 across the country, each specializing in some aspect of taxation.[11] A senior partner in the late John Stewart's law firm, Fraser Beatty, agrees that the new tax system has forced lawyers to specialize more than ever before.[12]

The initiation of federal income tax in 1917 also spawned the tax avoidance industry. It grew and prospered as tax rates climbed and the system became more intricate. In the post-war years the influence of the tax professionals was sufficient for them to become the chief spokesmen for business in tax policy matters, articulating its interests and assumptions and inserting them into the policy process.

The Carter Report questioned some of the assumptions of business which the tax professionals had adopted as their own, such as the idea that the tax system should take less from the economically

successful. The Report also seemed to imply that the activities of the tax professionals -- to the extent that they concentrated on the avoidance of tax liability -- were not socially productive. We are deprived of the opportunity to know how the Carter system might have affected the vitality of the tax avoidance industry, though it is clear that one aim of the recommendations was to construct a "leak-proof" system. The growth in the numbers of tax professionals since 1972 suggests that the reforms actually enacted have not done the industry any harm.

Tax Reform and the Participatory Democracy

This study has confirmed the charges of some of the participants and observers of the tax reform process, that the "participatory democracy" was bogus. The scope of genuine participation (beyond the filling in of coupons or responding to poll questionnaires) was confined to a very small proportion of the population. The effective "public" active during the tax reform debate consisted almost exclusively of two categories of individuals: those we have called the "tax professionals" (primarily lawyers, accountants and economists who devoted their careers to taxation matters); and "businessmen", a complex category including the proprietors of small and medium business establishments, and senior executives, officers and directors of large corporations. All shared a strong pecuniary interest in understanding and manipulating the relationship between business and other financial transactions, and the tax rules in order to minimize

the revenue they had to turn over to governments. We have noted several features of the pre-reform tax structure -- the very progressive personal rate structure culminating in conspicuously high marginal rates at the upper income end; the absence of any tax on a poorly-defined category of receipts known as "capital gains"; a number of what economists call "non-neutralities" in the tax system, some derived from the two structural factors already noted, and others from tax preferences given to certain other forms of income, all of which caused the form and process of a transaction to be highly significant in terms of future tax liability; the very complicated system of statutory provisions, regulations, administrative practices and legal precedent consequent upon this tax structure and the cat-and-mouse game of tax avoidance and loop-hole plugging played by tax practitioners and the government. These factors combined to produce a small group of highly tax-conscious high-income individuals, driven on one hand to find increasingly ingenious ways to minimize their taxes, and on the other to engage in lobbying and other political activities in order to change the tax rules in their favour.

The categories of businessmen and tax professionals overlap considerably, indicative of the significance of the fields of law and accounting for recruitment to the executive levels of business organizations. The heightened significance of the non-neutral tax system for business decision-making put a premium on the skills of the lawyers and accountants specializing in taxation. The analysis of a sub-set of the tax professionals which we labeled the "tax advocates" in Chapter 7 illustrates the close ties between the tax

professionals and the major corporations and affords a glimpse of the many links between the interests of different sectors of corporate capital.

In addition to being a part of the business community, the tax professionals were also the primary opinion-makers for business on matters of tax policy. What they had to say at the Tax Foundation conferences and on the business conference circuit was listened to attentively by corporate executives and entrepreneurs. The financial press featured detailed reports of the proceedings of the major tax conferences and of many of the sectoral and corporate meetings. On behalf of their law and accounting firms, the tax professionals also interpreted tax policy proposals and changes to their business clients, in the process indicating problem areas for future tax planning and for possible discussions with government officials and politicians.

The majority of taxpayers were wage- and salary-earners whose income taxes were deducted at source at marginal rates well under 50 per cent. For most, income tax was an annual bother, not worth the sustained effort required to explore, especially when most avenues for tax avoidance were available only to recipients of investment and business income. For them, the tax professionals were the shamans in tax policy matters: the uninstructed laymen had no personal experience or knowledge against which to test one professional opinion against another. If a tax expert knew the system well enough to earn a reputation, advise corporations, and perhaps get rich himself, then

it would be reasonable to treat his opinions on tax policy with some authority. When, as was often the case during the decade of tax reform, the experts did not all agree, the layman would be swayed by sheer numbers of expert opinions, finding most reasonable the view repeated most often.

To the extent that most politicians were also laymen in tax policy matters, they, too, were dependent on the tax professionals to tell them what needed changing in the tax system, what particular changes would likely accomplish the general social or economic objectives they sought, how the legislation and regulations should be drafted, and how the system should be administered. Even the taxation officials serving the government in the departments of Finance and National Revenue were recruited from the private sector professional firms, many of them returning to successful careers as tax advisors after they had gained the "insider's" knowledge and experience. One frustrated Deputy Minister of National Revenue once complained that his Department was becoming a post-graduate school for tax accountants. Politicians also relied on the tax professionals to a considerable extent to tell them what "the public" thought of tax proposals, this while the experts were, through the media, virtually telling the public what to think. Most of Mr. Benson's encounters with "the public" while defending his White Paper were in meetings sponsored by tax professionals, or at gatherings where he shared the platform with tax professionals. This must have seemed perfectly natural to Mr. Benson, himself a tax professional. Yet, while he continued to protest that the "silent majority" of taxpayers who would

benefit from his reform proposals were at least passively in favour, he did little to mobilize that constituency. Bill C-259, and the amended Income Tax Act of 1972 were then defended by government spokesmen as the product of participatory democracy, proof that the government had listened to the "public" and modified its policy accordingly. The language used by the government to help legitimize its concessions to business was borrowed from the propaganda put forth by business and the tax professionals.

The Tax Professionals and the Structure of Power

The community of tax professionals is somewhat like the modern physicist's model of the atom: there are lots of parts moving around inside of it, and there is a definite core, but the boundary of the outer shell is defined only in terms of probabilities. We have conceptually defined the tax professionals as those who earn their living by studying and interacting with the tax system. In practical terms, it can be described as the people who regularly attend the conferences of the Canadian Tax Foundation, though this would exclude many tax professionals outside the major cities of Central Canada, and include many people who spend most of their time in other than tax-related matters. Nearly all tax professionals outside the universities and public-sector institutions are lawyers or accountants working in private firms as "tax practitioners", or employed by businesses.

With the exception of university-based professionals and those who remain and expect to remain in the public sector throughout their working lives, there is a strong tendency to feel a community of interest with their natural clients, taxpayers seeking to minimize their tax burdens. The structure of the tax system, the high social concentration of wealth and income, and the concentration of control of the major business organizations within the hands of the same wealthy individuals, all contribute to providing a small, powerful and socially homogenous clientele for the tax professionals. The nature of the skills of the tax professionals and their relative scarcity opened up the higher circles of business and society to them. And as members of the corporate elite became increasingly concerned with growing government expenditures and higher taxes, the corporate elite merged with the upper ranks of the tax professionals. Our analysis of the "tax advocates", an active subset of the tax professionals, indicated that 18 (or 11 per cent) were members of Wallace Clement's corporate elite, that is, they were on the boards of one or more of 113 dominant Canadian corporations. As the corporate elite included only 946 Canadian residents, about two per cent of their number were, themselves, among the "tax advocates". The corporations controlled by this elite were represented by about 55 per cent of the "tax advocates".[13]

The relationship between the corporate elite (the board members of the dominant corporations) and the families and individuals who own controlling interests in the dominant corporations -- the "big bourgeoisie" in the sense used by Clement and other neo-marxists such

as Jorge Niosi[14] -- is complicated by the different roles of the career business managers, normally internal directors, the legal and technical specialists who appear to sit on the boards primarily as advisors, and those who own blocks of shares large enough (those having "controlling interest") to determine the behaviour of the corporations. In some cases, members of the first two categories would also be members of the latter group, that is, they would also be members of the big bourgeoisie.

Niosi's critique of Clement's inclusion of all the board members of the dominant corporations within the big bourgeoisie is persuasive, however. The evidence in the public domain indicates that most of the legal and technical advisors do not have large stock holdings in the dominant corporations on whose boards they sit, and that their role on the boards is merely an advisory one.[15] A portion of the "tax advocates" were career managers rather than professional chartered accountants or lawyers, and some of these also belonged to the economic elite defined by Clement. Niosi's analysis indicates that even these highly paid executives, who also benefit from generous stock options and consequently from capital gains and dividend payments, do not usually own sufficient blocks of shares to exercise control over the corporations they manage.[16] Nevertheless, they do receive handsome compensation, much of it derived out of corporate profits, and exercise the executive function of the big borgeoisie in economic matters. Hence, we accept Niosi's conclusion that they should be considered at least subordinate members of the big bourgeoisie.

The primary social function of the group at the centre of our study, the tax professionals, is that of the technical advisors to the bourgeoisie on taxation matters.[17] They are part of a more encompassing category of lawyers and accountants supporting the wider area corporate activity. Law and accounting are both vital fields to the bourgeoisie: their economic power, based on the legal institution of private property is exercised through and protected by a system of legal relationships; their economic power is maintained and reproduced, and their levels of consumption supported by corporate profits which are measured and audited by the accounting profession. Corporate lawyers and chartered accountants are therefore twin watchdogs of bourgeois private power. Gramsci's terminology of "organic intellectuals" is entirely appropriate for both professional groups:

> Every social group, coming into existence on the original terrain of an essential function in the world of economic production, creates together with itself, organically, one or more strata of intellectuals which give it homogeneity and an awareness of its own function not only in the economic but also in the social and political fields. The capitalist entrepreneur creates alongside himself the industrial technician, the specialist in political economy, the organisers of a new culture, of a new legal system, etc....
>
> If not all entrepreneurs, at least an élite amongst them must have the capacity to be an organizer of society in general, including all its complex organism of services, right up to the state organism, because of the need to create the conditions most favourable to the expansion of their own class, or at least they must posess the capacity to choose the deputies (specialized employees) to whom to entrust this activity of organising the general system of relationships external to the business itself. It can be observed that the "organic" intellectuals which every new class creates alongside itself and elaborates in the course of its development,

> are for the most part "specializations" of partial aspects of the primitive activity of the new social type which the new class has brought into prominence.[18]

Modern conditions of corporate organization (such as the use of joint stock corporations and holding companies) and the veil of secrecy which cloaks the relationship between corporations and their owners, makes tracing the membership of the big bourgeoisie difficult. We do not know, for example, who controls the Canadian banks, widely acknowledged to be the most powerful economic institutions in the country. Studies of economic and social power, like those of Porter and Clement, have therefore treated the members of the boards of the largest corporations as a sort of proxy group for the "upper class" or "bourgeoisie". In addition to the methodological difficulties of penetrating beyond the boards, there is the jusitification that it is through heirarchical organizations like corporate bureaucracies that power in contemporary society is exercized, and that the boards operate on a collegial principle whereby responsibility for decisions is shared.[19]

Niosi on the other hand, argues that, in focusing on the boards of directors, we are studying the agents of power, not the power itself, which rests with those individuals, groups and families owning controlling interest in the dominant corporations. Niosi names several groups and families, and the total, given that there are fewer than 150 dominant corporations, should logically be no larger than this.[20]

The maintenence and reproduction of the economic power of the big bourgeoisie rests with its ability to retain control over the major corporations, often through pyramids of holding companies and corporate subsidiaries.[21] Creative use of the corporate device, the absence of any tax on capital gains, and decades of enterprising tax avoidance had contributed toward the preservation and growth of the assets under their control. Implementation of the Carter Report, with full taxation of capital gains (the source of about half of the big bourgeoisie's income), with deemed realization on death, and the inclusion of gifts and bequests in taxable income, would have struck at the pillars of bourgeois power.[22]

The authors of the Report and its defenders argued that its recommendations would enhance rather than hinder Canada's economic growth while preserving the capitalist form of economic organization. The model of capitalism they had in mind, however, was an abstract, classless form of market capitalism. Savings from all levels of society were channeled through a variety of institutions in accordance with market signals and invested in productive enterprises. Investors, it was acknowledged, had to be given sufficient incentive in the form of after-tax profit, and the Commission estimated that they would tolerate a marginal tax rate of about 50 per cent. Reduction of tax subsidies for some hitherto privileged economic sectors would more than be compensated for by increased investment in others, supplemented by overall increased economic growth as a result of a more neutral, efficient tax system. This model abstracted from the high concentration of wealth and of control over corporations.

The economists on the Commission's research staff had paid little attention to these issues, except to consider wealth as a source of income in the form of capital gains and as a source of investment capital. Corporations, they viewed simply as conduits for income to the shareholders. The idea of the exercise of power (either by a class, an elite or whatever) through the vehicle of corporations, while not actually denied, was not seen to be relevant to the problem.

The Commissioners were aware of the arguments being made at the time about entrepreneurial families losing control of businesses by having to liquify their assets in order to pay estate taxes and succession duties. The Commission enquired into this but was not able to find any authentic case of this happening. Even if this were to be one of the consequences of their recommendations, the Commissioners were not overly concerned: there was no evidence, they said in their Report, that family-controlled businesses were more productive than other businesses.[23]

The spell cast by the logical and technical prowess of the Report was sufficient to elicit a substantial proportion of the tax professionals to applaud it for at least a couple of weeks following publication. It really did offer solutions to the very problems they had complained about and lived with for years. During this "honeymoon" period the Report enjoyed a considerable amount of favourable publicity, as reporters, editors and commentators obligingly followed the paths set out by the Commission and judged the Report on its own terms. While one may be tempted to explain the

decisive shift toward a more negative stance by the tax professionals by the time of the April 1967 Tax Conference as simply the result of having read the six-volume Report, their criticisms focussed on major recommendations easily gleaned from a cursory reading of even the first volume. Any competent tax specialist would have known most of what he needed to know after spending the first week-end closeted with the Report. This was sufficient for the reporters of the financial press to deliver surprisingly detailed and accurate accounts. A more convincing explanation for the opposition of the private-sector tax professonals is their gradual understanding of the threat posed by the Carter recommendations, not for the classless capitalism of the Carter Report but for the real, class-dominated capitalism which they knew and served. Such an understanding required more than an attentive reading of the Report, if that at all, but rather an appreciation of the significance of a small number of wealthy people in the structure of power.

The private-sector tax professionals, whom, as we have seen, opposed the Carter and White Paper proposals to widen the tax base and increase the tax burden on the wealthy, were much more closely-linked to the big bourgeoisie (and also the wider circles of progressively smaller capital below it) than the university-based professionals. They helped design the corporate chains through which wealth was controlled and profits were channeled. As their personal and confidential advisers they assisted with estate planning to ensure that family fortunes would remain intact for the next generation. As the officers, directors and advisors to the corporations, they worked

to reduce to a minimum the fraction of profits handed over to the state. When that fraction seemed too high, they were the ambassadors of private capital to the government officials charged with formulating and enforcing the tax rules. When the whole set of rules of the tax game were being re-negotiated during tax reform, they were the active propagandists of private capital, working to inculcate in the politicians and the entire population an understanding of the problem consistent with the needs of large capital. They were, indeed, capital's organic intellectals.

The role of the university and public-sector tax professionals is more problematic. The comprehensive income concept was a contribution to the public policy agenda from the university-based tax professionals.[24] While the university-based economists were included in Gramsci's concept of the organic intellectuals, their relationship to private capital is a more distant one than that of the lawyers and accountants in the private sector, being mediated by state funding of universities and of research, and by substantial professional collegial control over the recruitment and promotional structures. A related factor is the more diversified clientele for the services of economists.

The tax professionals working within the Departments of Finance and of National Revenue were in a roughly intermediate position. Their career histories or aspirations were frequently linked to the private sector and/or the universities. The economists' model of a classless, market capitalism generally held sway within the Department

of Finance, and the comprehensive tax base was both logically persuasive and attractive from a revenue standpoint. These considerations were partially offset by the vertical chain of ministerial accountability and authority, and by the frequent contact with private lobbyists. This left the public-sector professionals in an indeterminate position: the magnitude and direction of their influence would depend more on conjunctural factors than would be the case for either the private-sector or university professionals. For the officials in the Department of Finance during the White Paper period, the decisive factors were the orientation of, and the tactical political exigencies facing the Minister. For the staff of the Carter Commission, it was the relative insulation of the structure of the Royal Commission from external pressures, combined with an enhanced sense of occasion and opportunity for individuals to play historically significant roles.

The findings of this study are consistent with the hypothesis that the owners of large capital -- the big bourgeoisie -- do constitute a ruling class. The representatives of the largest corporations were able to prevent the state from taking decisions inimical to what they perceived to be their vital interests. It also suggests that this bourgeois control remains contingent: the bourgeoisie can never feel completely safe. There is always a possibility of the decision-making process going "off the rails" via rash electoral promises to the greedy multitude, or of Royal Commissions which get "out of control" as a result of some Commissioner's messianic sense of the public good. At such times, the power of capital has to be visibly mobilized

in order to be effective, but at the cost of displacing the veil that normally discretely covers the relationship between private capital and the state. The fact that the possibility of the state slipping out of bourgeois control exists, lends support to the hypothesis that, while the state in capitalist society must conform to the general imperatives of private capital accumulation, it has a "relative autonomy" from the more specific demands of capital. When the various sectors of capital become united on a specific issue of vital concern, however, the state will yield, regardless of the interests of subordinate classes.

We are led to the conclusion therefore that the complex decision-making process of tax reform, despite the facade of "participatory democracy", resembles more that of class rule than pluralist democracy. One must add the ironic observation that class rule was exercised through the same institutions which are widely believed to be the foundations of pluralism. Strangely enough, it was in the most insulated, secretive fora that the decision-making processes tended to favour the great majority of the population: the internal deliberations of the Royal Commission, and (to a lesser degree) the internal decision-making within the Tax Policy Division of the Department of Finance. The most "democratic" fora, those open to the public, were dominated by the spokesmen of large capital. The political structures of ministerial responsibility; the representation of interests before the Commission, the Minister of Finance and the parliamentary committees; the openness of members of Parliament to the views of constituents; and the dependence of the government and

political parties on the support (electoral and financial) of citizens; all tended to reinforce the power of capital. Dispersal of governmental power in Canada through federalism also worked almost systematically to the benefit of the owners of capital and against the majority of Canadians. The ideological hegemony of capital was reinforced by the tax professionals, their views being practically uncontested in the press, itself largely in the hands of the same people who controlled the other large corporations.[25] Tax professionals were quoted in Parliament as authorities, and concessions to capital were defended by government spokesmen using phrases borrowed from the practitioners.

Although our story ends with the enactment of the 1972 Income Tax Act, the attack on the progressive aspects of the new system continued under a new Minister of Finance, John Turner. In 1981, the Minister of Finance of the day, Allan MacEachen introduced a minor re-incarnation of the Carter Report in attempting to close loopholes opened since the 1972 tax reform, using the revenues thus gained to lower the top marginal rates. MacEachen, an actor in the earlier tax reform, was no more successful than Benson in increasing the tax burden on the owners of capital. The very need for such a reform, less than ten years after the first, and for which Mr. MacEachen made a persuasive argument, served to underline the failure of the earlier reform. While this is beyond the scope of the present study, it reinforces our conclusions and reminds those who won the earlier tax reform debate that nothing is permanent in the world of taxation.

Notes to Chapter IX

1. See, for example, Claude Isbister's remarks to the Carter Commission, above, Ch. 3, pp. 152-153.
2. Carter Report, Vol. I, pp. 121-130.
3. Gardner, The Politics of Reform, pp. 286-339. Gardner did not have access to the Carter Commission records and therefore was unable to assess the influence of the briefs and hearings on the Commissioners' decisions.
4. Good, The Politics of Anticipation: Making Federal Tax Policy, (Ottawa: Carleton University School of Public Administration, 1980.)
5. See above, Ch. 7, pp. 515-517.
6. Good, pp. 46, 51-60.
7. Bryce interview.
8. See Christina McCall Newman, Grits: An Intimate Portrait of the Liberal Party, (Toronto: Macmillan, 1982), pp. 267-269.
9. John Porter, The Vertical Mosaic, pp. 436-456, 528-532.
10. Ibid., p. 456.
11. Interview with D.R. Huggett.
12. Interview with S.E. Edwards.
13. This probably understates the degree of representation somewhat, since the economic elite control other companies besides those listed by Clement. In addition, tax professionals likely provided advice to the dominant corporations through a number of more discrete channels other than the highly visible one of appearing on their behalf before the Commons Committee.
14. See: The Economy of Canada: Who Controls It?, trans. Penelope Williams, (Montreal: Black Rose Books, 1978), Canadian Capitalism A Study of Power in the Canadian Business Establishment, trans. R. Chodos, (Toronto: James Lorimer & Co., 1981).
15. Niosi, The Economy of Canada, pp. 134-142.
16. Ibid., pp. 142-145.
17. We are considering the role of the tax professional as such. Of course, the specific individuals we have placed in this category will vary considerably in the extent to which they divide their efforts between this and other roles.
18. Antonio Gramsci, Selections from the Prison Notebooks, trans. Q. Hoare and G.N. Smith, (New York: International Publishers, 1971), pp. 11-12. We are in agreement with Niosi's like characterization of the more encompassing set of technical advisors on corporate boards. Niosi, pp. 126, 133-142.
19. Porter, pp. 220, 255.
20. Niosi lists 146 dominant corporations not subject to foreign control with assets in excess of $100 million as of 1975, of which data on share ownership existed for 136. He concluded that at least 68 per cent of these were controlled by small groups or families rather than the management of the firms. Clement listed 113 dominant corporations.
21. At this level of generality, virtually all students of corporate economic power, with the qualified exception of Porter, are agreed.

22. This differs from Gardner's assessment, (The Politics of Reform, p. 423.) that the Carter Report, while looking beyond the immediate concerns of individual capitalists, posed no threat to the capitalist system of power. While the authors of the Report did accept a reasonable return on capital as a fundamental constraint for their proposed system, they did not allow for the fact that control of investment capital was concentrated in a few hands.
23. Carter Report, Vol. 3, pp. 476-477.
24. While it is true that Geoffrey Conway had been employed by Clarkson, Gordon & Co., he was working on his dissertation at Harvard before joining the Commission. His interest in capital gains arose out of his graduate work.
25. Clement, The Corporate Elite, Ch. 7.

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Mr. Donald G. Grant. Halifax, N.S. Dec. 3, 1983.
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Mr. Donald R. Huggett, C.A. Montreal, May 3, 1983.
Dr. Claude M. Isbister. Toronto, July 17, 1982.
Mr. F.R. Irwin. Ottawa, April 5, 1983.
The Hon. Eric W. Kierans, P.C., By telephone, April 28, 1983; Halifax, Dec. 5, 1983.
Mr. Dennis Orchard, Ottawa, Nov. 14, 1975.
Mr. J. Harvey Perry. Toronto, Oct. 23, 1981.
Mr. Ronald Robertson, Q.C. Toronto, Nov. 22, 1982.
Mr. Ernest H. Smith. Ottawa, Nov. 14, 1975.
Mr. John G. Smith. Toronto, Nov. 22, 1982.
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APPENDIX "A"

The "Tax Advocates"

We have defined as the "tax advocates", the 162 individuals included in the following list who attended at least one of the two Canadian Tax Foundation Conferences of 1967 (abbreviated 4.67 CTF and 11.67 CTF), and also appeared before the House of Commons Standing Committee on Finance, Trade and Economic Affairs (FTEA, followed by the date and the corporation or association represented). The affiliation is indicated for each individual at the time of the respective activity, with " used to indicate the same affiliation as in the previous instance. The professional qualifications of each (in parentheses with the city of residence) have been checked with the Canada Law Directory and the Directory of the Canadian Institute of Chartered Accountants of 1970, and of later years in some cases. Law degrees are indicated by "LAW", CA degrees by "CA". Directorships of corporations have been taken from the 1970 Directory of Directors (70 DoD). Dominant corporations are abbreviated as (D), mid-range as (M). The number of additional directorships are given following a + sign. Directorships in oil and gas corporations are also indicated. For a discussion of the "tax advocates", see Chapter 7, pp. 552-558.

W.J. Adams; FTEA 18.6.70 Cdn Life Insurance Assoc; 4.67 CTF Can Life Assurance Co. (D); (Tor, Act)

J. Kenneth Allison; FTEA 9.6.70 Trust Cos Assoc of Can; 4.67 CTF Asst. Gen Mgr Mtl Trust (D); (Mtl, CA); 70 DoD 1D +2

A. Andras; FTEA 22.6.70 Cdn Welfare Council, 31.7.70 CLC

Charles Patrick Forsythe Baillie; FTEA 4.6.70 Cdn Council for Fair Taxation; 4.67 CTF Thorne, Gunn, Helliwell & Christenson (Tor, CA); 11.67 CTF Deloitte, Plendere, Haskins & Sells

K.F. Baldwin; FTEA 20.7.70 St. John BoT (Thorne, Gunn, Riddell & Co.); 4.67 CTF Hudson, McMackin & Co. (St. John, CA)

J.B. Barber; FTEA 7.5.70, V-P Fin Algoma Steel, 7.5.70 Steel Industry of Can; 4.67 CTF Algoma Steel (D); 70 DoD 2D: Cdn Steamship Lines (D) + 2

J. Flavelle Barrett; FTEA 4.6.70; 4.67 CTF Imperial Oil (D); (Tor)

Merrill Bélanger; FTEA 22.4.70 Nfld Inst of CA's, 22.7.70 Nfld & Lab CoC; 69CICA H.R. Doan & Co. (Corner Brook, CA)

Marcel Bélanger; 29.7.70 Bombardier (M); 4.67 CTF Belanger, Dallaire, Gagnon & Accoc (Que, CA)

K.P. Benson; FTEA 29.7.70 V-P Fin & Dir B.C. Forest Products (D); 11.67 CTF " 69CICA (Van, CA)

W.E. Bergen; FTEA 18.6.70 Co-operative Union of Can; 4.67 CTF Tres & CEO Fed Coops Ltd (Saskatoon); 70 DoD +3

E.J. Brown, Q.C.; FTEA 9.6.70 Trust Cos Assoc of Can; 4.67 CTF Eastern & Chartered Trust (Tor, law); 70 DoD sst V-P Can Perm Mort & of Can Perm Trust (D)

N.J. Brown; FTEA 7.5.70 V-P & Comptroller Stelco (D), 7.5.70 Steel Industry of Canada; 11.67 CTF Stelco (D); (Hamilton)

R.A. Brown Jr.; FTEA 2.6.70 Chm & Pres Cygnus Corp, 2.6.70 Chm & Pres Home Oil (D); 70 DoD 4D, 1M: incl Crown Trust, Trans Can Pipelines +2; 69CICA (Cal, CA)

Robert D. Brown; FTEA 1.6.70 CICA, 28.5.70 McIntyre Procupine Mines (M); 4.67 CTF Price Waterhouse (Tor, CA); 70 DoD Pres Corp Services, Pres 5 Mines & 4 Oil & gas, Dir 13 mines & oils +1

A. Gordon Burton; FTEA 25.6.70 Cdn Assoc of Oilwell Drilling Contractors; 4.67 CTF Peat, Marwick, Mitchell & Co.(Cal, CA)

George C. Campbell; FTEA 18.6.70 Cdn Life Insurance Assoc; 4.67 CTF Metropolitan Life (D); (New York)

H. Marcel Caron; FTEA 16.6.70 Que CoC; 4.67 CTF Clarkson, Gordon & Co. (Mtl, CA); 70 DoD Dir AECL; Woods, Gordon & Co

William M. Carlyle; FTEA 21.5.70 CBA; 11.67 CTF Ladner, Downs, Ladner & Co. (Van, law)

D.M. Clark; FTEA 21.5.70 CBA; 11.67 CTF Clark, Wilson & Co. (Van, law); 70 DoD Dir B of BC (M), +2 mines +2

P.T. Clark; FTEA 9.6.70 Tor BoT; 4.67 CTF Consultant (Tor); 70 DoD V-P Mkting G&B Automated Equip (Tor)

R.M. Clark; FTEA 29.7.70 UBC; 4.67 CTF " (Van, ECO)

Maurice G. Clennent; FTEA 18.6.70 Cdn Bankers' Assoc; 4.67 CTF Dep Gen Mrg Royal Bank (D)

John Coates; FTEA 28.7.70 Cdn Machine Builders' Assoc; 4.67 CTF Borden, Elliot, (Kelly & Palmer) (Tor, law); RCT

Robert William Cochrane, F.C.A.; FTEA 4.6.70 Treas & Dir Taxation Gulf Oil (D); 11.67 CTF BA Oil (Tor, CA)

Ronald B. Coleman; FTEA 2.6.70 Secy Cygnus Corp, 2.6.70 Secy & Gen Counsel Home Oil (D); 11.67 CTF " (Cal, CA); 70 DoD 2D +1

Laurence E. Coward; FTEA 5.5.70 Exec V-P & Dir Wm M. Mercer Ltd; 4.67 CTF " (Tor); 70 DoD 2

Dave B. Craig; FTEA 28.5.70 Mining Assoc of Can; 4.67 CTF Shell Can (D) (Tor)

H.J. Crofts; FTEA 9.6.70 Life Underwriters; Elder, Donaldson & Crofts (Tor)

Glen Edward Cronkwright; FTEA 30.4.70 Retail Council of Can; 4.67 CTF Clarkson & Gordon (Tor, CA)

R.J. Dart; FTEA 25.6.70 Cdn Assoc of Real Estate Bds, 31.7.70 Tor Real Estate Bd; 4.67 CTF Price, Waterhouse (Tor, CA)

J. Joe Dierker; FTEA 18.6.70 Co-operative Union of Canada, 18.6.70 Natl Assoc of Cdn Credit Unions (Francis, Gauley, Dierker & Co); 4.67 CTF Fed Co-ops Ltd (Saskatoon, law)

Russell G. Disney; FTEA 22.6.70 Cdn Conference of the Arts; 11.67 CTF Touche, Ross, Bailey & Smart (Tor, CA)

Stanley Ewart Edwards; FTEA Mbr Taxation Comm Met Tor BoT; 4.67 CTF Fraser, Beatty, Tucker & Co (Tor, law)

Charles Rainforth Elliott; FTEA 20.7.70 Conwest Explorations, 28.5.70 Mining Assoc of Can (Bownanville, CA); 70 DoD Pres 4 mines, Dir 6 mines +1

Jack T. Ellis; FTEA 20.7.70 James Richardson & Sons (D); 4.67 CTF " (Winn, CA)

Sydney Eric Ewens; FTEA 4.6.70 Imperial Oil (D); 4.67 CTF Imperial Oil (Tor)

Ronald J. Farano; FTEA 4.6.70 Cdn Council for Fair Taxation (Cocomile, Feldman & Farano); 4.67 CTF Davies, Ward & Beck (Tor, law)

Donald B. Fields; FTEA 29.7.70 UBC; 4.67 CTF " (Van, CA); RCT

Ian Forbes; FTEA 22.6.70 Chm Taxation Comm Regina CoC; 4.67 CTF Clarkson & Gordon (Regina, CA)

Donald Hugh Ford; FTEA 26.5.70 Noranda (D), 28.5.70 Mining Assoc of Can; 4.67 CTF Noranda (Tor, CA)

D.A. Foster; FTEA 26.5.70 Noranda (D); 4.67 CTF " (Tor)

Keith Otis Fowler; FTEA 19.5.70 CMA, 4.6.70 Texaco (D); 11.67 CTF Texaco (Mtl); 81CICA (Edm, CA) Alta Energy Co.
John M. Fuke; FTEA 21.5.70 CBA (Fraser, Beatty); 11.67 CTF Osler, Hoskin & Harcourt (Tor, law)

Graham C. Gibb; FTEA 19.5.70 Cdn Pulp & Paper Assoc; 4.67 CTF CIP (Mtl)

J. Kerr Gibson; FTEA 28.5.70 Mining Assoc of Can, 9.6.70 Met Tor BoT, 22.6.70 George Weston Ltd (D); 4.67 CTF Clarkson, Gordon & Co. (Tor, CA)

A.G. Goodeve; FTEA 28.5.70 McIntyre Porcupine Mines (M); 4.67 CTF Rio Algom (M) (Tor)

John Godfrey, Q.C.; FTEA 11.6.70 Cdn Mutual Funds Assoc (Campbell, Godfrey & Lewtas Co.); 4.67 CTF (Tor, law); 70 DoD Pres 4, Dir 2 mines + Mtl Trust (D), +13

W.E. Goodlet; FTEA 1.6.70 CICA, 21.7.70 Chimo Gold Mines, 21.7.70 Iron Bay Trust; 4.67 CTF Riddell, Stead, Graham & Hutchison (Tor, CA)

Wolfe D. Goodman; FTEA 25.6.70 Urban Dev Inst, 5.5.70 Community Funds & Councils of Can; 4.67 CTF Goodman & Carr (Tor, law)

William Alan Greenman; FTEA 4.6.70 Shell Can (D); 4.67 CTF Shell Can (Tor, CA); 11.67 CTF

Harold M. Griffith; FTEA 7.5.70 Pres & CEO Stelco (D), 7.5.70 Steel Industry of Canada; 70 DoD Dir CGE (D), TD Bank (D), +5

G.E. Hall; FTEA 30.4.70 Retail Council of Can; 4.67 CTF Tax Mgr. Robert Simpson Co. (D) (Tor)

E.C. Harris (Edwin); FTEA 23.7.70, NS Voluntary Econ Plan Bd; 4.67 CTF Dal (Hal, law)

Kenneth Harry; FTEA 8.6.70 Cdn Gas Assoc; 4.67 CTF Consumers' Gas (D) (Tor)

E.H. Heeney; FTEA 9.6.70 Pres Natl Trust (D); 4.67 CTF " (Tor); 70 DoD +2

L.F. Heyding, F.C.A.; FTEA 29.7.70 (for himself); 4.67 CTF Peat, Marwick, Mitchell (CA)

V.G. Hobbes; FTEA 9.6.70 Trust Cos Assoc of Can; 4.67 CTF Royal Trust (D) (Mtl)

David S. Holbrook; FTEA 7.5.70 Steel Industry of Can; Chm & Pres Algoma Steel (D); 70 DoD +Dir Can Steamship Lines (D), Royal Bank (D), Dupont (D), Dominion Bridge (D), +1 mine

W.C.C. Howland; FTEA 12.5.70 Treas Law Soc of UC; 70LAW McMillan, Binch (Tor, law); 70 DoD Chm or Pres 2, + Dir 17

Donald R. Huggett; FTEA 1.6.70 CICA, 28.7.70 Mtl BoT; 4.67 CTF McDonald, Currie & Co. (Mtl, CA)

Frederick Warren Hurst, F.C.A.; FTEA 28.4.70 Investor-Owned Gas and Electric Utility Cos, 28.4.70 & 8.6.70 V-P, Cdn Gas Assoc; 4.67 CTF V-P Fin & Asst Secy Consumers' Gas (D) (Tor, CA); 69CICA F.H. Deacon, Hodgson Inc.

Julien R. Hutchinson; FTEA 22.6.70 TSE; 4.67 CTF Wood, Gundy (Tor, CA); 70 DoD Dir 2

A.R. Ilersic; FTEA 9.6.70 Van BoT; 4.67 CTF U of London (UK, law)

Reginald L. Kayler; FTEA 9.6.70 Life Underwriters; 4.67 CTF " (Tor)

Richard J. Kelly; FTEA 28.7.70 Allied Boating Assoc; 4.67 CTF Chagnon, MacGillvray & Co.; (Hamilton, CA)

James Mitchell Patrick Kelly, Q.C.; FTEA 29.7.70 Dir Campeau Corp (D), 25.6.70 Cdn Inst of Public Real Estate Cos; 70 DoD Pres Cdn Inter-Urban Prop (D), +1, Counsel Seguin, Carbonneau, Goulet, Landriault & Patenaude (law)

Denham John Kelsey, CA; FTEA 30.7.70 (himself); 4.67 CTF Thorne, Gunn, Helliwell & Christenson (Van, CA)

Lionel P. Kent; FTEA 9.6.70 Cdn CoC; 11.67 CTF Riddell, Stead, Graham & Hutchison (Mtl, law)

John P. Kinghorn; FTEA 26.5.70 Hollinger Mines (D); 11.67 CTF Riddell, Stead, Graham & Hutchison (Mtl, CA)

Alan Douglass Laing; FTEA 7.5.70 DOFASCO (D), 19.5.70 CMA; 4.67 CTF DOFASCO (Hamilton, CA)

Cecil Lamont; FTEA 27.7.70 Equitable Income Tax Foundation; 4.67 CTF North-West Line Elevators Assoc. (Winn)

Donald J. Lawson, Q.C.; FTEA 12.5.70 Law Society of BC; 11.67 CTF Crease & Co. (Vic, law); 70 DoD Dir 1

Marc Leduc; FTEA 15.6.70 Cdn Export Assoc; 11.67 CTF Dept. of Justice; 70 CTF Alcan Finances (D) (Mtl, law)

John G. Lees; FTEA 19.5.70 CMA, 4.6.70 Alcan (D); 4.67 CTF Aluminum Securities (D)

William Robert Lord; FTEA 24.7.70 Loram Ltd; 4.67 CTF " (Cal, CA); 69CICA Touche, Ross (Edm)

D.S. Lyall; FTEA 4.6.70 V-P Fin Gulf Oil (D); 11.67 CTF BA Oil; 70 DoD Dir Superior Propane (M) +2

William Atwood Macdonald; FTEA 21.5.70 CBA, 22.6.70 Denison Mines (M), 27.7.70 Vanier Inst of the Family; 4.67 CTF McMillan, Binch & Co. (Berry, Dunn) (Tor, law); 70 DoD Dir Victoria & Grey Trust (D) + 4

Harry W. Macdonell, Q.C.; FTEA 15.6.70 Rio Tinto Zinc (M); 22.7.70 V-P & Gen Counsel Br Nfld Corp (D); 4.67 CTF Fasken, Calvin, MacKenzie & Co. (Mtl, law); 70 DoD +2 mines +2

Walter Chester MacDonell; FTEA 22.7.70 Cdn Coop Wheat Producers; 4.67 CTF Man Wheat Pool; 69CICA (Winn, CA) Man Pool Elevators

Lyman MacInnes; FTEA 28.7.70 NHL Players' Assoc; 11.67 CTF Trans Can Pipelines (D); 70 CTF McDonald, Currie & Co.(Tor, CA)

Donald Alexander Macintyre; FTEA 19.5.70 Chm Subcomm on Corps & their Shareholders, Taxation Comm CMA, 15.6.70 Cdn Chemical Producers' Assoc; 4.67 CTF Imperial Oil (D); 11.67 CTF "; 69CICA (Tor, CA)

D. Fraser Macorquodale; FTEA 5.5.70 Mbr Taxation Comm Cdn Pension Conf; 4.67 CTF Aluminum Fiduciaries (D) (Mtl)

Frank John Mair; FTEA 2.6.70 Mbr Taxation Comm CPA, 2.6.70 Hudson Bay Oil & Gas (D); 4.67 CTF HB Oil & Gas (Cal, CA)

M. Mair; FTEA 28.7.70 Cdn Machine Builders Assoc, 28.7.70 Inst of Assoc Executives

M.H. Maltby; FTEA 18.6.70 Cdn Bankers' Assoc; 4.67 CTF Bank of Commerce (D)

E.D. Marchant; FTEA 25.6.70 Chm Spec Comm on the govt proposals for tax reform Urban Development Inst; 4.67 CTF indep. (Port Credit, CA); 70 CTF Sr. V-P Fin Bramalea Consolidated Investments (D)

Edward Douglas Kirkpatrick Martin; FTEA 4.6.70 Asst Mgr Tax Dept Imperial Oil (D); 4.67 CTF Imperial Oil (Tor, CA)

John Maybin; FTEA 28.4.70 Cdn Gas Assoc, 28.4.70 Chm & Chief Cdn Utilities Ltd. (D) & assoc. cos, 28.4.70 Investor-Owned Electric and Gas Utility Cos; 70 DoD Chm & Pres Northwestern Utilities (D) +2

John D. McAlduff; FTEA 11.6.70 Chm Taxation Comm Cdn Mutual Funds Assoc, 20.7.70 Exec V-P Investors Group Trust Co; 4.67 CTF Investors Group (D); 11.67 CTF Investors' Group (Winn, CA)

Edward Bruce McConkey; FTEA 22.6.70 V-P Fin & Treas Denison Mines (M); 4.67 CTF " (Tor, CA); 70 DoD +1 mine +1 cement

A.B. McKie; FTEA 18.6.70 Cdn Bankers' Assoc; 4.67 CTF B of NS (D)

Charles McLaughlin; FTEA 1.6.70 Mbr Taxation Comm CICA; 4.67 CTF CIL (D) (Mtl, CA)

Walter V. McNally; FTEA 28.7.70 Mtl BoT, 30.7.70 Cdn Electircal Mfgrs' Assoc and Canada Wire and Cable; 4.67 CTF Mgr Income Taxes Northern Electric (D) (Mtl, CA)

Charles Burdon Mitchell; FTEA 2.6.70 Investment Dealers' Assoc; 4.67 CTF Thorne, Gunn & Co. (Helliwell & Christenson) (Tor)

A.M. Moore (Milton); FTEA 29.7.70 UBC

John S. Morris; FTEA 27.7.70 Chm Taxation Comm & Consultant to Cdn Fed of Insurance Agents; 11.67 CTF Clarkson & Gordon (London, CA)

A.C. Mosher; FTEA 21.7.70 Pres Chimo Gold Mines; 21.7.70 Pres Iron Bay Trust; 70 DoD Dir +3

John Murray Mulholland; FTEA 8.6.70 auditors of Natl Cancer Inst.; 4.67 CTF Thorne, Gunn, Helliwell & Christenson (Tor, CA)

Alan M. Murray; FTEA 30.7.70 V-P Fin Cominco (D); 4.67 CTF " (Mtl, CA); 70 DoD +Dir B of M (D), Pine Pt Mines (D) +4

Eric Newman; FTEA 12.5.70 CICA; 4.67 CTF Touche, Ross, Bailey & Smart (Mtl, CA)

Paul Hartley Palmer CTF 4.67 York Steel Const; FTEA 22.6.70 Asst. to V-P Fin Denison Mines (M); 11.67 CTF;

Derek H. Parkinson; FTEA 9.7.70 Van Bot, 29.7.70 Council of Forest Industries of BC, 11.6.70 MacMillan Bloedel (D); 4.67 CTF Price Waterhouse (Van, CA)

D.D. Peters; FTEA 18.6.70 Cdn Bankers' Assoc; 4.67 CTF TD Bank (D)

Bruce Blair Philip; FTEA 22.6.70 Cdn Welfare Council; 4.67 CTF Riddell, Stead, Graham & Hutchison (Ott, CA)

Neil F. Phillips, Q.C.; FTEA, 28.4.70 Investor-Owned Electric and Gas Utility Cos, 4.6.70 Dir & Counsel Aquitaine (M), 28.4.70 & 8.6.70 Counsel Cdn Gas Assoc, 4.6.70 Dir Internat. Utilities Corp; 70 CTF Phillips, Vineberg & Co. (Mtl, law); 70 DoD Dir +1 oil +2

R.H.D. Phillips; FTEA 22.7.70 Cdn Coop Wheat Producers; 4.67 CTF Sask Wheat Pool; 11.67 CTF "

Hans O. Pintea; FTEA 20.7.70 Winn CoC; 4.67 CTF Deloite, Plender, Haskins & Sells (Winn, CA)

Beryl Plumptre; FTEA 27.7.70 Pres. Vanier Inst of the Family; 4.67 CTF Consumers' Assoc of Can (Tor, ECO)

J.W. Popkin; FTEA 18.6.70 Cdn Life Insurance Assoc; 4.67 CTF Sr Econ Sun Life (D); (Mtl, ECO)

Zdenko Peter Pokrupa; FTEA 4.6.70 Shell Can (D); 4.67 CTF Shell (Tor, CA)

William Rogerson Purslow; FTEA 22.7.70 Cdn Coop Wheat Producers; 11.67 CTF Sask Wheat Pool; 69CICA (Regina, CA)

R.D. Radford; FTEA 18.6.70 Cdn Life Insurance Assoc; 4.67 CTF Assoc Tres Canada Life (D) (Tor)

Henry B. Rhude, Q.C.; FTEA 23.7.70 Solicitor Natl Sea Products; 4.67 CTF Stewart, MacKeen & Co. (Covert) (Hal, law); 70 DoD Pres 1, Dir NS Trust (M), +5

Gordon Wiliam Riehl; FTEA 9.6.70 Mbr Tax Reform Comm Cdn CoC; 11.67 CTF Deloite, Plender, Haskins & Sells (Oshawa, CA)

John F. Robinson; FTEA 29.7.70 Silverwood Dairies etc. (M); 4.67 CTF Clarkson, Gordon & Co. (London, CA)

Bartlett Bidwell Rombough (Bart); FTEA 2.6.70 Treas Cygnus Corp; 2.6.70 Treas & Dir Home Oil (D), 2.6.70 Independent Petroleum Assoc.; 11.67 CTF Home Oil (Cal, CA); 70 DoD Dir +2

Irving Lewis Rosen, F.C.A.; FTEA 4.6.70 Cdn Council for Fair Taxation; 4.67 CTF Rosen, Ezrin & Co. (Tor, CA)

Victor St. Onge; FTEA 16.6.70 Que CoC; 4.67 CTF Que Cartier Mining (Port Cartier)

Keith V. Sandford; FTEA 25.6.70 Cdn Construction Assoc; 4.67 CTF (Ott)

Arthur R.A. Scace; FTEA 25.6.70 Counsel Cdn Inst of Public Real Estate Cos; 11.67 CTF McCarthy & McCarthy (Tor, law)

Gordon R. Sharwood; FTEA 2.6.70 Cdn Growth Study Assoc; 4.67 CTF Bank of Commerce (D); 70 DoD Dir Guarantee Trust (D) +9

M.A. Shaw; FTEA 22.7.70 Mbr Saskatoon BoT; 4.67 CTF Touche, Ross, Bailey & Smart (Saskatoon, CA)

S.A. Shepherd; FTEA 18.6.70 Cdn Bankers' Assoc; 11.67 CTF V-P Pension Plans B of M (D)

Frank Howard Sherman; FTEA 7.5.70 Steel Industry of Can, 7.5.70 Pres & CEO Dofasco (D); 70 DoD Dir B of NS (D), Crown Life (D) +9

Sheldon Silver; FTEA 25.6.70 Cadillac Dev Corp (D); 4.67 CTF Goodman & Goodman (Tor, law)

V.G. Staff; FTEA 30.7.70 Mgr Gen Tax Accounting Cdn Electrical Mfgers' Assoc, and Canada Wire and Cable Co; 4.67 CTF Peat, Marwick, Mitchell & Co (Tor, CA)

Keith Elroy Steeves; FTEA 28.5.70 Mining Assoc of Can, 27.7.70 BC Mining Assoc; FTEA 27.7.70 V-P Fin & Tres Bethlehem Copper (M); 4.67

CTF "; 70 DoD Dir +1; 69CICA (Van, CA)

H. Heward Stikeman; FTEA 23.7.70 Prof Art Dealers' Assoc, 30.7.70 Bowaters, (M) 31.7.70 Tor Real Estate Bd; 4.67 CTF Stikeman, Elliott, Tamaki & Co. (Mtl, law); 70 DoD Dir Crown Trust (M) +3

T.R. Suttie; FTEA 18.6.70 Can Life Insurance Assoc; 4.67 CTF Exec V-P Equitable Life (M) (Waterloo, Act)

S. Thom (Stuart); FTEA 12.5.70 Law Soc of UC; 4.67 CTF Osler, Hoskin & Harcourt (Tor, law)

Robert Douglas Thomas; FTEA 12.5.70 Exec Dir CICA; 4.67 CTF CICA (Tor, CA)

Pat N. Thorsteinsson; FTEA 28.5.70 Tax Advisor Syncrude (D) (i.e. Imperial Oil, Gulf, Atlantic Richfield, Cities Service), 20.7.70 Inter-prov Steel & Pipe, 28.7.70 Western Interntl Hotels, 28.7.70 Woodward Cos; 4.67 CTF Thorsteinsson, Mitchell & Little (Van, law)

David Y. Timbrel; FTEA 15.6.70 Rio Tinto Zinc (M); 4.67 CTF McDonald, Currie & Co. (Tor, CA)

J. Ross Tolmie, Q.C.; FTEA 2.6.70 Home Oil (D) and Gen Counsel & Dir Cygnus Corp (its parent); 11.67 CTF Herridge, Tolmie, Gray, Coyne & Blair (Ott, law); 70 DoD Dir Trans Can Pipelines (D) +2

John A. Tuck; FTEA 18.6.70 Mging Dir Cdn Life Insurance Assoc; 4.67 CTF "

William Osborn Twaits; FTEA 4.6.70 Pres Imperial Oil (D); 4.67 CTF Imperial Oil (Tor); 70 DoD Royal Bank (D) +1 +VChm & Trustee Natl Ind Conf Bd, Gov U of T, Mbr Econ Council of Can, Internat Adv Council Stanford Research Inst, Adv Council to Minister of IT&C, Natl Adv Comm on Petroleum, Cdn-Amer Comm, Cdn Econ Policy Comm, Br North American Comm

Philip F. Vineberg, Q.C.; FTEA 25.6.70 Counsel & Chief Spokesman Cdn Assoc of Real Estate Bds; FTEA 30.7.70 Assoc of Cdn Distillers; 11.6.70 Assoc of Internat Business Corps (incl Massey Fergusson (D), Seagrams, Aquitaine (M), Rio Tinto (M) +4); 12.5.70 Bar of the Prov of Que; 4.67 CTF; 11.67 CTF, Phillips, Vineberg, Goodman & Co. (Mtl, law); 70 DoD Dir Seagrams (D), Edper Inv (M) +11

Robert H.E. Walker; FTEA 21.5.70 CBA; 11.67 CTF Martineau, Walker, Allison & Co. (Mtl, law); 70 DoD Gov CTF, Dir 1 gas +4

Wayne Stanbury Walker; FTEA 20.7.70 Investors' Group, Mgr Tax Services Investors Syndicate Ltd (D); 4.67 CTF Westmount Life Insurance Co.; 11.67 CTF Investors' Group (Winn, CA)

P. Walton; FTEA 29.7.70 Council of Forest Industries of BC, 9.6.70 Vice-Chm Taxation Comm Van BoT; 70 CTF Peat, Marwick & Mitchell (Van, CA)

V.C. Wansbrough; FTEA 26.5.70 Cdn Potash Producers' Assoc; 4.67 CTF Mining Assoc of Can (Tor)

D.A. Wilson (Alex); FTEA 19.5.70 Cdn Pulp & Paper Assoc; 4.67 CTF Mills, Spence & Co Ltd (Tor, CA); 69CICA Queen's School of Bus

J.C. Wilson; FTEA 15.[illegible].70 Rio Tinto Zinc (M) 22.7.70 Br Nfld Corp (D); 11.67 CTF Peat, Marwick, Mitchell & Co. (Mtl, CA)

Russell W. Wilson; FTEA 19.5.70; 4.67 CTF CIP (Mtl, CA)

Orville C. Winstrem; FTEA 4.6.70 Tax Administrator Texaco (D); 4.67 CTF " (Mtl)

J. Wleugel; FTEA 15.6.70 Treas Massey Ferguson (D); 4.67 CTF " (Tor)

Wolfgang Wolf; FTEA 22.7.70 Sask CoC; 11.67 CTF Deloitte, Plender, Haskins & Sells (Regina, CA)

Don S. Wood; FTEA 28.7.70 Inst of Assoc Executives; 4.67 CTF Don S. Wood Ltd. (Tor)

R.B. Wright; FTEA 11.6.70 Asst to Pres United Corps Ltd (M); 4.67 CTF "; 70 DoD Dir +2

Adam Hartley Zimmerman; FTEA 19.5.70 Mbr Exec Bd. Cdn Pulp & Paper Assoc, 26.5.70 Noranda (D), 26.5.70 Cdn Potash Producers' Assoc; 4.67 CTF Noranda (Tor).

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