
For many years, the only textbook on international taxation in Canada was the well-known primer by Brian Arnold and Michael McIntyre. Readers requiring a fuller treatment can now turn to this book. It is not a casebook, which relies heavily on long quotations from cases; rather, the approach it takes is generally to describe the law without the use of examples or problems. There are no footnotes but references are given at the end of each chapter. The material is presented in five parts: “Fundamentals of International Taxation in Canada” (60 pages), “Inbound Taxation” (70 pages), “Outbound Taxation” (110 pages), “Tax Avoidance and Administration” (90 pages), and “Other Issues” (40 pages). The Canada-US treaty is included as an appendix.

Alan M.


One method of illegal income splitting among the self-employed is paying a salary to one’s spouse even though no work is done. This article develops a way of estimating the prevalence of this practice and the consequent loss of tax revenue. In particular, the employment rate is significantly higher for wives whose husbands are self-employed than for those whose husbands are employed: 79.6 percent versus 72.9 percent. However, non-tax reasons could explain this difference. For example, a wife may be

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more likely to work when her husband is self-employed in order to gain access to health and dental benefits.

A way to separate the tax and non-tax factors for the difference in employment rates is to compare Canadian and US data. In the United States, there is no tax incentive to pay a spouse for non-existent work because couples file joint tax returns. Therefore, if the difference in employment rates in Canada is partially tax-driven, the difference in employment rates in the United States should be smaller. This is the case: while the employment rate of wives with self-employed husbands is again higher than the rate for those whose husbands are employed (74.2 percent versus 72.6 percent), the difference between the two rates is much smaller than the Canadian difference—1.6 percent versus 6.7 percent.

After using regression equations to control for the possibility that the two categories of wives differ on other dimensions, the author calculates that 1 in 18 self-employed husbands in Canada engaged in this form of illegal income splitting in 1998. This represents an annual revenue loss of $500 million. The good news, if there is any, is that the prevalence of income splitting seems to have declined from a rate of 1 in 10 in the late 1980s and early 1990s.

Alan M.


The inspiration for Diane Ring’s article is her observation that the “tax” aspect of international tax scholarship has generally displaced the “international” aspect. Because international tax rules are ultimately shaped by the dynamics of multijurisdictional relations, Ring seeks to provide a richer understanding of international taxation by drawing on international relations theory.

The first part of the article discusses various international relations theories, their implications for the formation and stability of international “regimes,” and their potential application to international tax. The second part considers the relevance of international relations theory to the development of an established international regime for the prevention of juridical double taxation through bilateral tax treaties. The final part of the article proposes an international relations tax research agenda aimed at assessing the likelihood of regime formation in other areas of international taxation such as transfer pricing, documentation standards, withholding, and international tax arbitrage.

Drawing on literature from other fields, such as international trade and international human rights law, Steven Dean’s article complements Diane Ring’s by suggesting a richer way of comprehending international tax relations. The “philosopher kings” to whom Dean refers in his title are neither tax academics nor tax practitioners, but imaginary state actors who, according to him, are generally assumed in international
tax scholarship to act in each country’s national interest in a consistent and economically rational way. Although this conception of a rational and benevolent state is rejected in much domestic tax policy scholarship (inspired, for example, by public choice theories of state behaviour), Dean argues that this assumption wrongly informs much thinking about international tax policy. Moreover, he emphasizes, this theoretical mistake is not without real-world consequences, as exemplified by the failure of attempts to discourage harmful tax competition initiated by the Organisation for Economic Co-operation and Development (OECD).

The first part of the article explains the so-called philosopher king model of international tax relations, which generally presume that states engage with each other as unitary participants in an international bargaining game. As an alternative to this state-centred conception of international relations, Dean proposes a more pluralistic view according to which domestic actors can also play a role on the international stage.

The second part of the article discusses the phenomenon of “tax flight” to tax haven jurisdictions and the apparent failure of “cooperation commitments” with these countries to prevent international tax evasion. Suggesting (curiously, to this reader) that these cooperation commitments could produce gross domestic product (GDP) gains for tax havens as well as tax flight jurisdictions, Dean concludes that the failure of this initiative suggests that state interaction does not follow the philosopher king model. In contrast, he argues in the third part of the article, the proliferation of bilateral tax treaties reflects pressure by non-state actors such as domestic investors seeking greater security against juridical double taxation than that provided by domestic foreign tax credits.

The final part of the article builds upon the earlier analysis by suggesting a different response to the tax flight phenomenon from the cooperation commitments proposed by the OECD’s initiative on harmful tax competition. Instead, Dean suggests, tax flight jurisdictions should offer to negotiate “tax flight treaties” with tax haven jurisdictions, pursuant to which the tax haven would commit to developing the information infrastructure that would enable it to exchange information with tax flight jurisdictions, while tax flight jurisdictions would agree to help finance the development of this information infrastructure and to share a portion of the additional revenues generated by the tax haven’s cooperation.

While this solution seems pretty reasonable, it isn’t obvious why it calls into question the philosopher king model that Dean is so keen to criticize. For him, however, the key point is that these tax flight treaties could end up reducing the GDP of the tax flight jurisdiction when one takes into account both the costs to secure cooperation by the tax haven jurisdiction and the lost income otherwise obtained by “tax cheats.”

Although one might question aspects of Dean’s argument, his article rightly suggests that international tax relations should be understood not merely as bargaining games between unitary state actors but as more complex phenomena involving multiple non-state actors.

D.D.

This article is a comprehensive examination from a US perspective of the implications of EU law for the national income tax systems of the member states. The analysis is situated in a wide-ranging context that includes comparisons with international tax concepts and norms and with US constitutional law governing state taxation powers. The authors begin by providing a historical and institutional introduction to the European Union and the role of the Court of Justice of the European Community (ECJ) in advancing the process of European integration. There follows an overview of the various components of the international tax system, the role of bilateral tax treaties in reducing double taxation, the credit and exemption methods, their relationship to the simultaneously unachievable goals of capital export and capital import neutrality, and tax discrimination.

The authors then review the ECJ’s corporate tax jurisprudence on tax discrimination and restrictions on fundamental freedoms in the EC treaty, as well as its rulings on the legality of various tax subsidies and incentives (or “state aid”) granted by the member states. The approach used in this article is interesting in that, unlike most analyses, it does not categorize the cases according to the fundamental freedom (free movement of labour, enterprise, services, or capital) that is alleged to be infringed by a national tax law of a member state. Instead, the authors present the case law in terms of (trade) discrimination against foreign products, foreign producers (incoming investment), or foreign production (outgoing investment), without distinguishing this from mere restriction on free movement or the separate EC treaty prohibition on state aid. This prepares the ground for the later comparison with US jurisprudence on interstate commerce and state tax incentives, as well as leading into the discussion of the demise, at the hands of the ECJ, of the various corporate tax imputation systems applied by member states in taxing dividends.

The example of the elimination of national imputation systems is seen as presaging similar judicial prohibition of member state tax incentives and foreign tax credits. The latter mechanism is, the authors suggest, incompatible with the fundamental freedoms because it prevents companies resident in high-tax member states from benefiting from lower tax rates in other member states by locating their branches and subsidiaries in such low-tax jurisdictions. It also prevents companies resident in low-tax jurisdictions that do business in higher-tax member states from benefiting from the low tax in their state of residence. The authors conclude that the ECJ’s “robust” approach to tax discrimination, which prohibits inequality of treatment of both incoming and outgoing investment, leads to an incoherent result (“the impossibility result”), in that equal treatment of foreign and domestic income simultaneously in two different countries is not possible as long as member states’ tax rates and bases are not harmonized. The strains put on the member states’ tax systems by the ECJ’s jurisprudence will, the authors assert, lead to either greater income tax harmonization within the European Union (which is not seen as likely in the foreseeable
future) or a return to greater fiscal autonomy of the member states. The article suggests that some “pullback” from the current rigidity of the ECJ’s position may occur, and in fact, this prediction has to some extent come true since early 2006, when the article was written. The authors note the recent appearance in opinions of the advocates general of the ECJ of a position that would distinguish between truly discriminatory provisions and restrictions on free movement, and “quasi-restrictions” that arise solely from the interaction of two divergent member state tax systems. The ECJ jurisprudence has not clearly reached the point of requiring equal tax burdens on companies that have sources of income in only one member state and those that have income sourced in another member state as well as in the residence state, so that quasi-restrictions may in fact be compatible with EU law. The authors’ insistence that without rate (as well as base) harmonization, the discrimination jurisprudence will continue to make inroads on the tax sovereignty of member states may thus be questionable.

The next section of the article describes the similarities and differences between the US Supreme Court’s constitutional jurisprudence on the taxing powers of the states and the ECJ approach. The very different political and constitutional contexts of Europe and the United States and the lack of coherence in the jurisprudence in both jurisdictions lead the authors to conclude that neither should look to the other for a solution to the problem of how to apply the principle of non-discrimination in tax matters.

The article then reviews the potential impact of the ECJ jurisprudence on US domestic and international tax policy. As already indicated, the authors consider that reference to ECJ jurisprudence by the US Supreme Court in constitutional decisions on state tax jurisdiction cases would be an unwise (though possible) development. The interpretation of US tax treaty provisions will not likely be affected by the ECJ’s interpretation of tax discrimination. The authors suggest that EU jurisprudence could, over time, affect the OECD’s interpretation of its model treaties, particularly its non-discrimination clause, and that this could lead toward a more comprehensive interpretation of non-discrimination articles in treaties based on the OECD model. In contrast, the World Trade Organization’s interpretation of discrimination will not expand in response to ECJ case law without an explicit authorization in a new WTO agreement, a development that is extremely unlikely in the authors’ view.

The potential application of the ECJ’s “open skies” case law to limitation-of-benefits provisions in the bilateral tax treaties between the United States and EU

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member states is then canvassed. Since the possibility exists that EU member states will not be able to conclude tax treaties with the United States that do not extend benefits to residents of all other EU countries, the authors recommend that the United States contemplate the long-term prospect of concluding a multilateral tax treaty with all EU countries. Finally, if the impact of the ECJ’s corporate tax decisions is to make the European Union a place where it is difficult for member states to impose or collect corporate tax, the United States will have to consider how to respond to the obvious competitive disadvantage it will face in persuading corporations to maintain investment in the United States.

Martha O’Brien

Deborah A. Geier, “Murphy and the Evolution of ‘Basis’”
(2006) vol. 113, no. 6 Tax Notes 576-82

Is compensation for emotional distress properly taxable as income? In a recent US decision, the DC Circuit Court of Appeals concluded that these amounts are non-taxable under the US constitution on the basis that damages for emotional distress are not received in lieu of income and that the framers of the sixteenth amendment would not have understood such compensation to be income. In this short article, Geier criticizes the decision on the grounds that it wrongly relies on an earlier case distinguishing between taxable income and the tax-free return of basis, and that the taxpayer at issue had no tax basis in her emotional well-being in respect of which the compensation could represent a tax-free return. While the argument makes sense to the extent that the court’s decision depends on the basis concept, it is not obvious that the court’s “in lieu of” approach actually depends on the notion that compensation represents a return of capital.

D.D.

New York University Law Review (forthcoming)

Among developed countries, the United States stands alone in taxing individuals on their worldwide income on the basis of US citizenship rather than residence. Notwithstanding this approach, the Internal Revenue Code has, since 1926, excluded some or all of the earned income of US citizens living and working abroad. Although this exclusion is currently capped at US$82,400, competitiveness concerns are often said to justify eliminating this limit.


3 Murphy v. IRS, docket no. 05-5139 (DC Cir. August 22, 2006).
In this article, Kirsch defends worldwide income taxation on the basis of citizenship on the grounds that citizenship-based taxation reflects traditional equity considerations related to benefits received and ability to pay, and neutrality considerations related to decisions about residence and citizenship status.

The first part of the article provides an interesting history of citizenship-based taxation in the United States, which originates in Civil War tax legislation motivated by the desire to compel non-resident citizens to help pay for the costs of the war. Although the modern US income tax adopted the same approach in 1913, concerns about international competitiveness of US investment after the First World War led to the introduction in 1926 of an exclusion for foreign-source earned income. Since 1962, however, this exclusion has generally been capped at a fixed dollar amount.

The second part of the article briefly discusses the economic and political changes over the last half-century that have motivated proposals to eliminate the cap on the exclusion of foreign-source earned income or (more broadly) to abandon citizenship-based taxation altogether. While globalization may increase competitiveness concerns, Kirsch argues that increased mobility and international communication actually strengthen the case for taxing US citizens living abroad.

The third part of the article makes the case for citizenship-based taxation, based on traditional tax policy principles of equity (benefits and ability-to-pay theories), neutrality, and compliance and enforcement, as well as the “expressive effect” of citizenship-based taxation on social norms. According to Kirsch, since citizens living in the United States generally view citizens living abroad as members of a common society, the exclusion of non-resident citizens from worldwide income might cause resident citizens to “conclude that citizens abroad are ‘getting away with something,’ thereby undermining the confidence in the tax system and the social norm of tax compliance in the United States.”

The fourth part of the article criticizes arguments for a foreign-source earned income exclusion. The fifth part advances legislative proposals to eliminate the exclusion while possibly introducing “narrowly targeted” measures designed to provide equity-based relief to non-resident citizens.

D.D.

Organisation for Economic Co-operation and Development,
The Political Economy of Environmentally Related Taxes
(Paris: OECD, 2006), 199 pages

With concern about the environment and global warming high on the political agenda, it is perhaps time to pay attention to some of the OECD’s work on environmental fiscal reform (EFR) and environmentally related taxes. This report provides an excellent introduction to the subject. It explains the concept of environmentally related taxes; surveys the current use of these taxes among developing countries; and reviews evidence on their environmental effectiveness, their effect on sectoral competitiveness, impacts on income distribution, administrative costs, and the use of these taxes in conjunction with other policy instruments such as tradable permits and
subsidies. A separate chapter—the most important perhaps—considers experience with measures designed to enhance public acceptance of environmentally related taxes.

D.D.


In the debate over cutting taxes versus leaving them constant or raising them, international comparisons are frequently made. For example, if country X has lower tax rates than Canada and it has also achieved certain desirable social or economic outcomes, perhaps Canada should match its tax rates with those of country X in order to achieve the same outcomes. This is usually the argument made by those who would like Canadian tax rates to be lowered to the level in, say, the United States or Ireland. However, an argument can also be made for raising Canada’s tax rates in order to achieve the desirable social and economic outcomes achieved by certain high-tax countries. While Brooks and Hwong do not go quite that far, they do compare a wide variety of social and economic outcomes (lower murder rates, low infant mortality, high educational levels, high GDP per hour worked, etc.) in six Anglo-American countries and four high-tax Nordic countries to support the argument that high taxes are at least not inconsistent with such desirable outcomes. Of course, simple international comparisons do not tell us directly whether higher taxes raise or lower societal well-being, since many other factors may be relevant in explaining differences among countries.

Alan M.


Warsame’s main hypothesis is that undergraduate tax courses in Canadian business schools cater to the accounting profession. To support this hypothesis, Warsame shows that the number of undergraduate tax courses offered by universities in different provinces is strongly related to the number of exemptions for tax courses given to incoming students in provincial chartered accountant training programs (zero in the Atlantic provinces, one in the western provinces, and two in Ontario and Quebec). Warsame argues that the content of undergraduate tax courses is also strongly influenced by the accounting profession. The courses generally focus on the “ex-post calculation of taxpayers’ tax liabilities and compliance in general”4 favoured

4 At 66.
by the accounting profession, rather than the Scholes-Wolfson decision-making issues that Warsame believes are more relevant for business students. Warsame’s view is that the ideal two-course sequence would be a first course of Scholes-Wolfson material followed by a second course of compliance material.

Alan M.

New Zealand, Department of Finance and Department of Inland Revenue, *Tax Incentives for Giving to Charities and Other Non-Profit Organisations* (Wellington, NZ: Inland Revenue Department, Policy Advice Division, October 2006), 31 pages

This discussion document issued by the ministers of finance and revenue of the New Zealand government makes some suggestions for increasing charitable giving that could be relevant to Canada. One suggestion, which has also been made by Canada’s minister of finance, is to provide a tax credit for volunteers’ time. A number of interesting questions are raised in the document:

- What should be the nominal hourly rate for calculating the credit, and how should it be set?
- Should there be a limit on the number of volunteer hours creditable in a year?
- Should the credit be limited to charities, or should it be extended to athletic and non-profit organizations?
- Should the credit be limited to certain types of activities?

The document also raises a concern that it would be necessary to rely on charities to validate the time given by individual volunteers, and they might not have the time and resources to do that accurately. Also, perhaps a tax credit is inconsistent with the idea of volunteering, which is to contribute not for pecuniary gain but for the common good.

A second suggestion, following the United Kingdom example, is to introduce a payroll giving scheme whereby charitable contributions are withheld from employees’ wage and salary payments at source. This could benefit the employee by making the tax saving immediate, rather than postponing it until the individual files an annual tax return. The potential benefit for charities, according to the document, is that the “regularity and certainty” of donations could be increased. While this kind of arrangement is allowed in Canada, it appears to be rare. The key to the United Kingdom’s success appears to be the establishment of approved payroll giving agencies that forward the money to the chosen charity.

Alan M.

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5 At 23.
A common view among economists of the debate on “fiscal imbalance” is that provincial governments want to have money to spend without going through the pain of raising it by levying higher taxes. Thus, a frequently proposed remedy is to transfer tax room from the federal government to the provinces, increasing their share of tax revenues. In this context, the federal government’s recent program of staged cuts to the goods and services tax (GST) suggests the possibility of ceding the GST to the provinces. These two papers discuss alternative ways in which this could be done.

Smart and Bird suggest moving all provincial consumption taxes into a value-added tax format, which they call a provincial value-added tax (PVAT), with a common tax rate across provinces but rates that vary by province. This involves major changes: the provinces that have implemented a harmonized sales tax (HST) would move to province-specific HST rates, which would increase as the province occupied the tax room vacated by the GST; Quebec would increase the Quebec sales tax rate similarly and harmonize in some way to the tax base of the other provinces; and the five other provinces that currently levy their own retail sales taxes would abolish these taxes to adopt the PVAT.

Smart and Bird analyze the political accountability and economic benefits from a PVAT. Their regressions show that following the introduction of the HST in Newfoundland, New Brunswick, and Nova Scotia, total private investment per capita increased, even after controlling for other determinants of investment. The authors then present a rough calculation of the required PVAT rate in Ontario (excluding the occupancy of vacated GST room), estimating it to be 8 percent—the same as the present retail sales tax.

The paper by Clemens et al. begins by analyzing revenue and expenditure patterns over time and producing three key conclusions. First, federal and provincial own-source revenues were approximately equal in 1990-91. Second, since that time federal expenditures have remained constant in real (inflation-adjusted) terms while provincial expenditures have grown 33 percent in real terms. Third, the federal government has increased its real spending in areas of provincial constitutional responsibility while decreasing its real spending in at least some areas of federal responsibility. These results lead Clemens et al. to the same point of view as Smart and Bird: the solution to the present fiscal problems, which some call fiscal imbalance, is to disentangle federal and provincial finances.

The specific form of disentanglement that Clemens et al. examine is for the federal government to couple abolition of the GST with termination of two key transfer
programs, the Canada health transfer and the Canada social transfer. This would apparently leave the federal government in approximately the same revenue position, though the authors do not study this point. They calculate the revenue position of each province as the provincial GST rate required to make up for the revenue lost from the ending of these transfer programs. The rate would vary from a high of 7.1 percent in Newfoundland and Labrador to a low of 4.2 percent in Alberta. (The Alberta figure is positive because even that province suffers from the loss of the transfers.) These rates would be in addition to present provincial sales tax rates. It appears that HST rates would fall as a result, but Clemens et al. do not discuss this point.

Alan M.


This is a very unusual Finance publication. Although it is described as a report by an arm’s-length panel, the panel acknowledges the assistance of eight employees of the department’s Tax Policy Branch, and the level of detail provided in the report, such as consideration of revenue costs and anti-avoidance rules, is what one would expect from such staff involvement. A 33-page section entitled “Plan Definitions and Details” is particularly noteworthy; it presents not only the design choices made, but also the alternatives and the associated advantages and disadvantages. Thus, the report seems to be an official Department of Finance product in all but name. Rarely has the thinking of the department in developing a policy proposal been laid bare in this way.

The report is also noteworthy for some peripheral comments on fundamental tax concepts. Two comments, in particular, seem not to be directly related to the purpose of the report, and perhaps reflect a change of perspective under the present minister:

- “Few would quarrel with the broad approach of horizontal equity, though many would quarrel with how it should be achieved. Vertical equity is a more problematic concept.”6
- “The term ‘tax expenditures’ is a euphemism, often used in a pejorative sense, to describe virtually any amount that is charged against a base revenue model. In essence the idea of a ‘tax expenditure’ is based upon an assumption that tax rates should be applied to a very broad definition of income so as to maximize tax revenue at any given tax rate.”7

Alan M.

6 At 11.
7 At 13, note 14.

Although this comprehensive book was produced in Australia for the Australian government, it will be useful to readers in other countries who seek information on comparative taxation. Most of the data compare the 30 OECD countries; however, for more certain and more complex design features, the data focus on a narrower group of countries—Australia and nine others considered to be similar: Canada, Ireland, Japan, the Netherlands, New Zealand, Spain, Switzerland, the United Kingdom, and the United States. Many of the comparisons are drawn from various economic studies that have appeared elsewhere, and appropriate references are given. The emphasis is on quantitative measures that can be summarized in graphs and tables.

Alan M.