Current Tax Reading

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Which taxpayers cheat on their taxes, or are non-compliant in other ways? In 2009, the Canada Revenue Agency (CRA) released, for the first time, detailed information on taxpayer compliance. The papers listed above report the findings of two recent CRA studies of compliance by individual taxpayers.

In the first paper, Boame, who is a CRA analyst, describes a study that analyzed confidential CRA data from the 1996-2002 taxation years for 18 million individual taxpayers. The study examined three types of tax compliance:

1. *filing compliance*: the percentage of taxpayers who were not subject to a late filing penalty;
2. *reporting compliance*: the percentage of taxpayers who reported accurately (that is, with a tax payable difference of $50 or less in either direction between the amount reported by the taxpayer and the amount assessed by the CRA); and
3. *payment compliance*: the percentage of taxpayers who were not charged arrears interest or instalment interest on deficient payments.

The data showed that for the years covered by the study, the rate of reporting compliance was the highest (95 percent), the rate of filing compliance was in the middle (93 percent), and the rate of payment compliance was the lowest (91 percent) in 2002.1 Overall, Boame notes, “Canadian taxpayers were slow to pay their taxes in...”

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1 IRS conference paper, at 10.
the study period.”

My impression is that there is also a problem with filing compliance. Since the majority of taxpayers have a refund and thus cannot be assessed a late filing penalty, a 7 percent overall rate of filing non-compliance implies that at least one out of seven taxpayers who owe money are filing late.

Boame uses a logit model to evaluate the determinants of each of the three forms of compliance. Focusing particularly on reporting compliance (understatement of tax liability), some of the more interesting results are as follows (where each comparison is based on holding all other factors equal): 3

- Males are more likely to underreport than females.
- Underreporting is highest among taxpayers aged 35 to 54, lowest among taxpayers under 35, and in the middle for taxpayers aged 55 and over.
- Underreporting is lowest for taxpayers who are married and highest for those who are separated; single taxpayers are in the middle.
- Underreporting is higher among taxpayers whose main source of income is capital gain/loss or self-employment income than taxpayers whose main source of income is wages.
- Taxpayers who use a tax preparer are less likely to underreport than those who prepare their own return.
- Taxpayers who netfile are less likely to underreport than those who file paper returns.
- Taxpayers in the lowest and highest federal tax brackets are less likely to underreport than taxpayers in the two middle tax brackets.

Of all of these results, the one that is most surprising is the high rate of underreporting among taxpayers who file paper returns compared with taxpayers who netfile. One would have thought that the absence of a requirement to file receipts might lead to lower compliance by netfilers.

Perhaps the finding only means that people who file paper returns are more likely to make simple arithmetic errors in reporting tax payable, since the netfiling system has built-in mechanisms to control for such errors. However, if that is the explanation, both overreporting errors and underreporting errors should be greater for paper filers than netfilers. Boame’s paper does not include any analysis that might be used to verify this theory.

The second paper by Boame presents a time-series analysis of Canadian reporting compliance and payment compliance (as defined in the IRS conference paper reviewed above). There is one data observation for each year from 1987 to 2003, for a total of 17 observations. Only four independent variables are used in the final estimating equations: the effective tax rate, which is defined as total tax paid divided by taxable income; the unemployment rate; the bankruptcy rate; and a dummy variable

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2 Ibid., at 11.
3 Ibid., at 34.
for the existence of the voluntary disclosure program from 1992 onward. The most interesting finding is that the existence of the voluntary disclosure program seems to have reduced reporting compliance. Boame offers the following explanation: “This might be due to the fact that taxpayers would intentionally underreport their income, knowing that they could avoid criminal prosecution by availing themselves of the voluntary disclosures program.”

A.M.

**Sage Research Corporation, Attitudes Towards Payment of Debt and Compliance**, prepared for the Canada Revenue Agency, report no. POR 022-09, December 2009, 85 pages


The Federal Accountability Act requires that public opinion research reports contracted by Government of Canada departments and agencies since August 1, 2006 be made public. Under this requirement, the CRA has released about half a dozen reports each year. However, no announcement of the release is made, and because the reports are not always made available on the CRA Web site, it is sometimes difficult to find a specific report even when the title is known. Nevertheless, one can always locate these reports by entering “Canada Revenue Agency” as the author in a Library and Archives Canada Web-based database devoted to public opinion research.

Sage Research (the author of the first report listed above) investigates public opinion on various topics relating to tax debt and tax payment methods, one of which is whether the CRA should allow taxpayers to pay their tax owing by credit card. One would think that the CRA would have a lot to gain by providing this payment option, since it would allow delinquent taxpayers to make instant payments over the telephone in response to a dunning call. Also, allowing credit card payment would not necessarily imply that the CRA would not be receiving 100 cents on the dollar for payments—the merchant discount could simply be added to the amount required for full payment, as is the practice of the US Internal Revenue Service (IRS).

Using focus groups, Sage Research found that public opinion is against allowing payments by credit card. The concern expressed is that credit card debt normally carries a higher interest rate than the CRA charges on unpaid tax, and it would be

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4 ICITA conference paper, at 14.
5 SC 2006, c. 9.
6 Library and Archives Canada, *Public Opinion Research Reports*, electronic database (http://www.porrrop.gc.ca/). Using a search engine such as Google to search for a report (for example, by its title) does not locate the document because all of the reports are in a database rather than on a Web page.
7 Sage Research, at 30-31.
inappropriate for the CRA to promote a payment option that would cause people to go deeper into debt than they would if they worked with the CRA on a payment plan. One may conclude that if the CRA should decide to allow this option, it would be prudent for it to emphasize that it was doing so in response to public demand, and not actively promoting the payment of tax debt by credit card.

In the second study listed above, Corporate Research Associates surveyed Canadians on their attitudes toward the sharing of tax information by the CRA with other government bodies. The most interesting finding is that 50 percent of Canadians think it is a good idea to share such information with other federal government departments and provincial governments while 40 percent think it is a bad idea.\(^8\) Thus, Canadians seem to be strongly split on the current practice, which is to share information in this way. On the other hand, support for this practice is up 13 percentage points from the last survey in 1999.\(^9\) Also, support rises to two-thirds at the end of the survey, after a variety of information-sharing scenarios has been presented.\(^10\) The scenario for which support is strongest is the sharing of information about serious criminal activity with the police (64 percent).\(^11\) Support is also strong for using tax information to more effectively collect debts on behalf of other federal government departments (67 percent).\(^12\) In addition, 73 percent of the survey respondents said that they trust the federal government’s privacy laws to guard against misuse of personal information.\(^13\) In general, support for information sharing is lower among Canadians who are older or less educated and those who live in the western provinces.\(^14\)

A.M.


This study is one of about a dozen internal audit reports that the CRA posts on its “corporate reports and information” Web site each year. It documents what appear to be serious problems in compliance with the goods and services tax/ harmonized sales tax (GST/HST), with a level of candour that one would expect in a report from the auditor general of Canada, not the CRA itself.

\(^8\) Corporate Research Associates, at 13.
\(^9\) Ibid.
\(^10\) Ibid., at 14.
\(^11\) Ibid., at 32.
\(^12\) Ibid., at 36.
\(^13\) Ibid., at 26.
\(^14\) Ibid., at 51-52.
The study reports that non-compliance problems are concentrated among new registrants—half fail to file or remit on time.\textsuperscript{15} CRA followup to correct these problems is difficult because the current business registration procedure is designed to maximize the number of voluntary registrations and minimize the burden on taxpayers who register voluntarily. The study reports that business numbers are routinely issued even for applications that omit key information needed in the auditing process; for example, 59 percent of registrant accounts do not contain estimated annual gross sales, and 20 percent do not include the industry type.\textsuperscript{16}

Non-compliant registrants do not respect the “trust fund” relationship. Instead of recognizing that GST/HST collections are government monies that they are holding in trust, many of these businesses regard the taxes they collect as a source of cash flow, perhaps to fund a struggling operation. In such situations, the preferred option is simply not to file a GST return. (The CRA’s survey of non-compliant taxpayers shows that cash flow problems are the most common reason for not filing.)\textsuperscript{17} CRA staff view current practices in dealing with these taxpayers as too lenient. Non-compliant registrants have a competitive advantage over compliant registrants, to the point where some registrants may feel that they have to be non-compliant just to compete. In particular, CRA staff believe that arrangements for delayed payment should be accepted only after assessing the ability of registrants to pay their debt. Also, CRA staff regard the level of prosecutions as too low: there are “hundreds of thousands of non-compliant filers at any one time, many having two or more overdue returns,” even though in 2006-7 there were only 22 prosecutions across the country for failure to file GST/HST returns.\textsuperscript{18}


Feminist and other critical tax scholars have, until recently, focused their attention primarily on tax theories and domestic tax issues. This article extends the feminist analysis to international taxation. Brooks states that her goal is to “engage feminists and progressive international tax scholars in a shared dialogue about the importance of protecting and enhancing the state’s revenue-raising and international revenue distribution roles.”\textsuperscript{19} This article marks a significant step toward the achievement of that goal. Overall, it is a thought-provoking piece.

\textsuperscript{15} Section 1.2.
\textsuperscript{16} Section 5.1.
\textsuperscript{17} Section 2.0.
\textsuperscript{18} Section 5.3.
\textsuperscript{19} At 267.
The first two parts of the article lay the ground for such a dialogue by providing an overview of the relevant feminist and critical race scholarship and an overview of the current system of revenue allocation. Brooks then applies a feminist analysis to the problem of inequities in international revenue allocation (for example, inadequate allocation to low-income countries). She suggests that feminists should (1) push for the presence of more female treaty negotiators; (2) explore whether tax treaties might be used, or useful, as instruments to temper the effects of neo-liberalism; and (3) require states to be accountable for distributive inequities.

As Brooks notes, while the problem of growing distributive inequities is obvious, the solution is not. In the absence of a world government with taxing powers, there is no effective legal instrument or mechanism for redistributing income from high-income nations to low-income nations. Bilateral tax treaties are perhaps the only potential legal instrument, but are not designed for inter-nation redistribution purposes. It is up to high-income countries to help solve the problem by not offering corporations and other businesses resident in another jurisdiction safe refuge from taxes and by not encouraging tax competition among low-income countries. It is an uphill battle for feminist and progressive scholars to convince high-income countries to move in this direction. This article makes a good case for engaging in the battle.

J.L.

United States, Joint Committee on Taxation, *Technical Explanation of the Revenue Provisions of the “Reconciliation Act of 2010,” as Amended, in Combination with the “Patient Protection and Affordable Care Act,”* document no. JCX-18-10 (Washington, DC: Joint Committee on Taxation, March 21, 2010), 157 pages


Both of these publications discuss the common-law “economic substance” doctrine. The report of the US Joint Committee on Taxation provides a technical explanation of the revenue provisions related to the Health Care and Education Reconciliation Act of 2010\(^20\) signed by President Obama on March 30, 2010. Among these provisions is section 7701(o) of the Internal Revenue Code,\(^21\) which codifies the “economic substance doctrine.”

According to the report, new Code section 7701(o) applies to “any transaction to which the economic substance doctrine is relevant.”\(^22\) Therefore, for the provision to apply, courts must first determine that the doctrine is relevant. Whenever the economic substance doctrine is applied, pursuant to section 7701(o) a transaction will be considered to have economic substance only when both of the following requirements

\(^{20}\) Pub. L. no. 111-152.

\(^{21}\) Internal Revenue Code of 1986, as amended (herein referred to as “the Code”).

\(^{22}\) Joint Committee on Taxation, at 152.
are met: (1) the transaction changes the taxpayer’s non-tax economic position “in a meaningful way”; and (2) the taxpayer has a “substantial” non-tax-related purpose for entering into the transaction. By requiring that both the “objective” and the “subjective” tests must be met, section 7701(o) unifies US case law. Previously, some US courts had applied only one of the two tests while others had applied both. The report provides a succinct overview of the common-law doctrine and an explanation of the meaning of the codified doctrine. In the United States, a report by the Joint Committee on Taxation is regarded as an important, if not the sole, source of legislative history on the statutory provision.

The codified doctrine does not, however, specify the relevance of legislative intent—an omission that causes some to worry. Lederman argues that the judicial two-pronged economic substance doctrine provides a poor proxy for the real question, namely, whether the claimed tax results are consistent with the intent of Congress. She maintains that one important drawback of focusing on the taxpayer’s intent and the prospect of pre-tax profit, as opposed to legislative intent, is that the doctrine is much easier for taxpayers to manipulate. Accordingly, the doctrine may not be effective in distinguishing tax shelters and other abusive transactions from legitimate ones. Many avoidance transactions are bundled with business activity. Lederman explains that identifying abusive transactions is often difficult largely because some tax statutes merely try to measure income while others try to provide an incentive for particular behaviour. Identifying which goal is operative in a particular provision requires analysis of congressional intent. However, Lederman does not address how to determine legislative intent; instead, she refers readers to the body of literature that does. The main contribution of her article is to make the case for why courts should examine legislative intent in tax-avoidance cases.


These two articles discuss one of the most recent transfer-pricing cases in the United States, Xilinx Inc. v. Commissioner of Internal Revenue. The Xilinx case deals with the treatment of employee stock option (ESO) costs in cost-sharing arrangements (CSAs).

The case, as Greenwald says, “has been quite a ride.” First, the Tax Court in 2005 rejected the IRS’s assertion that Xilinx had to include ESO costs in its CSAs.

23 Ibid., at 142-56.
24 125 TC 37 (2005); rev’d. docket nos. 06-74246, 06-74269 (9th Cir., May 27, 2009); decision of May 27, 2009 withdrawn January 13, 2010 and original Tax Court decision aff’d. document nos. 06-74246, 06-74269 (9th Cir., March 22, 2010).
25 Greenwald, at 115.
before the transfer-pricing regulations were amended to explicitly require the inclusion of such costs. The Tax Court made this decision on the ground that unrelated parties dealing with each other at arm’s length would not have shared the costs of ESOS, and therefore the arm’s-length standard requires that those costs not be shared under a CSA either. In May 2009, the Court of Appeals (9th Circuit) reversed the Tax Court’s decision. The Court of Appeals explicitly accepted the Tax Court’s factual finding and even went further in explaining why unrelated parties would never share the costs of such options. The majority, however, decided (over a vigorous dissent by Noonan J) to require inclusion of ESO costs in the sharing pool. In response to the 9th Circuit’s decision, Xilinx filed a petition for rehearing. High-tech companies such as Cisco Systems Inc. and Apple Inc. filed amicus briefs in support of Xilinx’s petition. The Court of Appeals withdrew its original opinion on January 13, 2010 and reversed it on March 22, 2010. The majority, championed by Noonan J, held that the “all costs” requirement was irreconcilable with the arm’s-length standard because, as a fact, arm’s-length parties do not include ESO costs in CSAs. 

Avi-Yonah’s article was published before the Court of Appeals reversed its May 2009 decision in March 2010. He was much in favour of the original decision, arguing that it was correct even though the reasoning was too narrow. In his view, the case might be the occasion to prod the Obama administration and Congress to engage in a major “transfer pricing overhaul.”\(^26\) Undoubtedly, the reverse in course by the 9th Circuit would strengthen his view.

Greenwald provides a neat summary of the case and offers his thoughts on how to tweak the transfer-pricing regulations to eliminate the conflict between the requirement that the arm’s-length standard applies “in every case”\(^27\) and the requirement that ESO costs are included in the pool of costs in CSAs.\(^28\)

J.L.


In May 2010, the OECD Committee on Fiscal Affairs released its most recent draft update to the OECD model tax convention.\(^29\) The OECD Council approved these changes on July 22, 2010, and the OECD has since published the 2010 version of the model convention.

The draft 2010 update includes a new article 7 as well as changes to the commentary on a large number of articles to address the treatment of collective investment

\(^{26}\) Avi-Yonah, at 1234.

\(^{27}\) Code reg. section 1.482-1(b)(1).

\(^{28}\) Code reg. section 1.482-7T(d)(1).

\(^{29}\) Organisation for Economic Co-operation and Development, *Model Tax Convention on Income and on Capital* (Paris: OECD) (looseleaf) (herein referred to as “the model convention”). “Article” references in this review are to the model convention; “new article” refers to a revised provision under the draft 2010 update.
vehicles (CIVs), sovereign wealth funds (SWFs), telecommunication transactions, and the exception from source taxation under article 15(2). These changes had been previously released for comments in the following discussion drafts:


According to the Committee on Fiscal Affairs, the draft 2010 update includes changes made in response to the public feedback on the earlier drafts.

**New Article 7 of the Model**

New article 7 as set out in the draft 2010 update reads as follows:

**Article 7**

**BUSINESS PROFITS**

1. Profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the profits that are attributable to the permanent establishment in accordance with the provisions of paragraph 2 may be taxed in that other State.

2. For the purposes of this Article and Article [23A] [23B], the profits that are attributable in each Contracting State to the permanent establishment referred to in paragraph 1 are the profits it might be expected to make, in particular in its dealings with other parts of the enterprise, if it were a separate and independent enterprise engaged in the same or similar activities under the same or similar conditions, taking into account the functions performed, assets used and risks assumed by the enterprise through the permanent establishment and through the other parts of the enterprise.

3. Where, in accordance with paragraph 2, a Contracting State adjusts the profits that are attributable to a permanent establishment of an enterprise of one of the Contracting States and taxes accordingly profits of the enterprise that have been charged to tax in the other State, the other State shall, to the extent necessary to eliminate double taxation on these profits, make an appropriate adjustment to the amount of the tax charged on those profits. In determining such adjustment, the competent authorities of the Contracting States shall if necessary consult each other.

4. Where profits include items of income which are dealt with separately in other Articles of this Convention, then the provisions of those Articles shall not be affected by the provisions of this Article.
The proposed commentary on new article 7 is articulated in 77 paragraphs, occupying more than 20 pages. These changes were intended to achieve better alignment between article 7 (profits of a permanent establishment) and article 9 (associated enterprises) in attributing profits of a multinational enterprise to the jurisdiction in which it carries on business.

**Collective Investment Vehicles**

The term “collective investment vehicle” is used to describe “funds that are widely-held, hold a diversified portfolio of securities and are subject to investor-protection regulation in the country in which they are established.”30 According to the OECD, currently almost US$20 trillion is invested through CIVs worldwide. CIVs are taxed differently in different countries—some treat CIVs as separate entities, others tax CIVs as transparent entities. Inconsistent taxation of CIVs across countries may lead to double taxation and treaty shopping. The proposed changes to the commentary on article 1 deal with the technical questions of whether a CIV should be considered a “person,” a “resident of a Contracting State,” and the “beneficial owner” of the income. In light of the varied approaches under the domestic law, a number of alternative provisions were proposed for countries to adopt in their bilateral treaty negotiations.31

**Sovereign Wealth Funds**

“Sovereign wealth funds” are

special purpose investment funds or arrangements . . . [c]reated by [a State or a political subdivision] for macroeconomic purposes. SWFs hold, manage, or administer assets to achieve financial objectives, and employ a set of investment strategies which include investing in foreign financial assets.32

The international tax treatment of SWFs is inconsistent across countries, largely owing to the different levels of recognition of the customary international law principle of sovereign immunity. According to this principle, a sovereign state (including its agents, property, and activities) is, as a general rule, immune from the jurisdiction of the courts of another sovereign state. However, as the OECD has noted, there is no international consensus on the precise limits of the sovereign immunity principle.33

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31 For more detail, see supra note 30.


Most states would not recognize that the principle applies to business activities, and many states do not recognize any application of this principle in tax matters (though some recognize that it may apply). The draft 2010 update proposes the following change to the commentary on article 1:

The Convention does not prejudge the issues of whether and to what extent the principle of sovereign immunity applies with respect to the persons covered under Article 1 and the taxes covered under Article 2 and each Contracting State is therefore free to apply its own interpretation of that principle as long as the resulting taxation, if any, is in conformity with the provisions of its bilateral tax conventions.34

The proposed changes to article 4 state that

[whether a sovereign wealth fund qualifies as a “resident of a Contracting State” depends on the facts and circumstances of each case. For example, when a sovereign wealth fund is an integral part of the State, it will likely fall within the scope of the expression “the] State and any political subdivision or local authority thereof” in article 4. . . . States may want to address the issue in the course of bilateral negotiations, particularly in relation to whether a sovereign wealth fund qualifies as a “person” and is “liable to tax” for purposes of the relevant tax treaty.35

**Telecommunication Transactions**

The proposed changes to the commentary on article 12 deal with the taxation of some common telecommunication transactions, namely, payments to satellite operators, income from granting indefeasible rights over cable and telephone lines, roaming payments, and payments for spectrum licences. The general thrust of the proposed changes is that none of these payments constitute “royalties.”

Similarly, the general thrust of the proposed changes to the commentary on article 5 is that there are no permanent establishment issues in respect of telecommunication transactions. A satellite does not constitute a permanent establishment for its operator; a telecommunications operator who enters into a roaming agreement with a foreign operator will not be considered to have a permanent establishment in the state where the foreign operator’s network is located; and there is no permanent establishment when an enterprise makes payments to lease the capacity of cables for the transmission of electric power or communications located in another country.

**Exception from Source Taxation of Employment Income Under Article 15(2)**

Paragraph 2 of article 15 provides an exception from the source taxation of remuneration for employment exercised in the source state. The proposed changes to the commentary on article 15 deal with the determination of whether services are provided in the exercise of an employment within the meaning of this provision or

34 Draft 2010 update, at 21.
35 Ibid., at 22.
as part of a business carried on by the employer in the source country. This issue is particularly acute in “hiring-out of labour” cases. A number of examples are given to illustrate whether the exception under article 15 is applicable.

The draft 2010 update emphasizes the relationship between the principles underlying the exception in paragraph 2 and article 7. Proposed paragraph 8.1 of the commentary on article 15 states:

It may be difficult, in certain cases, to determine whether the services rendered in a State by an individual resident of another State, and provided to an enterprise of the first State (or that has a permanent establishment in that State), constitute employment services, to which Article 15 applies, or services rendered by a separate enterprise, to which Article 7 applies or, more generally, whether the exception applies. While the Commentary previously dealt with cases where arrangements were structured for the main purpose of obtaining the benefits of the exception of paragraph 2 of Article 15, it was found that similar issues could arise in many other cases that did not involve tax-motivated transactions and the Commentary was amended to provide a more comprehensive discussion of these questions.36

J.L.


The taxation of capital gains and capital losses is asymmetric, in that current tax rules limit the deductibility of capital losses while imposing current tax consequences for all capital gains. This theoretical study makes the case that this asymmetric treatment plays a role in firms’ attempts to communicate private information to investors. Specifically, the study uses this asymmetry to explain why stock prices rise on “good news” even though the accuracy of the disclosure cannot be verified.

Suppose that a manager has private information about future firm value. If the value is high and the manager credibly communicates that value to investors, the stock price rises at the time of the announcement rather than later on when the extra profits are actually earned. As a result, the effect is just to advance the timing of the capital gain on the shares. On the other hand, if the value is low but the manager reports that it is high, and investors believe the false statement, the effect is to increase the stock price at the time of the announcement but to reduce it later when the lack of profits becomes evident. The effect is to create a capital gain followed by a capital loss. If the loss cannot be used, the effect of this false announcement is to benefit current shareholders at the cost of raising net taxes across periods. These two scenarios generate a separating equilibrium in the model. Thus, the tax consequences of true versus false announcements render verification of the disclosure unnecessary; in this model, only firms with high value would make a good-news disclosure.

A.M.

36 Ibid., at 62.

The question addressed in this study is the effect of a 1997 reduction in US capital gains tax rates. One would expect that the shares of firms with low dividend yields would go up in price relative to other firms because more of their return is in the form of capital gains. This turns out to be the case. However, the more novel question is whether for firms whose shares are cross-listed in both the United States and a home country (such as Canada), the price reaction of the US cross-listed share might be different than the underlying home-country security for some period of time because of limitations on cross-country arbitrage. Using various proxies for the costs of arbitrage, Blouin et al. substantiate this effect for firms with high arbitrage costs.

A.M.


The general theme of this article is the corrosive effect of tax expenditures on the federal budget. There is not much that is new here, but Kleinbard provides a splendid summary of the arguments through a simple example, involving a hypothetical country (“Fredonia”) with 10 fruit and vegetable growers. If the government wishes to induce people to purchase more kumquats by exempting the single kumquat producer from the income tax, the tax paid by the other 9 fruit and vegetable producers must increase in order to maintain the same level of government services. This measure does not increase either tax revenue or government spending, but clearly much has changed—in particular, marginal tax rates and efficiency losses from taxation have increased.

A.M.


This report addresses the tax treatment of a certain group of information technology professionals—those who provide their services to clients through a corporation, have only one or two clients, are involved in a long-term relationship with those clients, and provide their services on site at their clients’ business premises. Not surprisingly, the CRA views the corporation as providing a personal services business and thus denies the deductibility of many expenses, such as the costs of training. This report is noteworthy for the fact that it highlights this issue. However, it is weak in addressing the policy concern that such information technology professionals are effectively in an employment relationship, and thus horizontal equity problems would arise if they received deductions that an employee would not have.

A.M.
John Richards, *Reducing Lone-Parent Poverty: A Canadian Success Story*, C.D. Howe Institute Commentary no. 305 (Toronto: C.D. Howe Institute, 2010), 18 pages

Two groups that are at high risk of poverty are the elderly and single-parent families. Although it is well known that poverty rates among the elderly have declined over the last three decades (primarily because of government transfer programs such as old age security and the guaranteed income supplement), it is less well known that poverty rates for single-parent families have also declined in this period. This paper documents this transformation and attributes it to increases in market income, as opposed to government transfer programs. More particularly, the paper attributes the decline to increased work incentives, both in the administration of provincial welfare programs and in federal initiatives such as the working income tax benefit and the national child benefit supplement (both of which make it more profitable for people on welfare to obtain employment). However, despite this good news, overall poverty reduction for the economy as whole has been similar to that in other OECD countries since the mid-1990s; and, according to one measure, Canada’s poverty rate in the mid-2000s was above that of a typical OECD country.

A.M.


A recent article in the *Globe and Mail*37 profiled brothers Craig and Marc Kielburger, founders of the registered charity Free the Children, and reported that they have now started a profit-making corporation, Me to We, that gives 50 percent of its net profits to the charity. This is an example of a social enterprise—a profit-making organization that has, at least in part, a charitable purpose. The tax treatment of social enterprises is the focus of the paper by Corriveau.

Corriveau points out that the CRA’s current interpretation of the Income Tax Act38 poses substantial problems for entities carrying on a social enterprise. Operating as a non-profit organization is believed by some to be a solution, but CRA policy is that a non-profit organization cannot seek to earn a profit on any project that is undertaken, even if the profits are to be used to undertake a project that will operate at a loss (which might be undertaken for its social benefit). Operating a profit-making project within a registered charity is possible under the CRA’s interpretation of the


38 RSC 1985, c. 1 (5th Supp.), as amended.
law only if the project meets the specific tests that qualify it as a “related business”; this test is not satisfied simply because the profits are used for charitable activities. Limited exceptions are also provided for businesses whose purpose is to provide on-the-job training to workers from a target population or businesses whose purpose is to employ people who have special challenges.

Accordingly, Corriveau concludes that neither a non-profit organization nor a registered charity is an appropriate vehicle for operating a profit-making project, regardless of the social benefits that the project might produce. The best approach is to run the project as a completely separate legal entity and pay corporate income tax on its net income (after the deduction for amounts contributed to charity). Apparently, this is how Me to We currently operates.

Some authors have proposed that the law should be changed to recognize the concept of a for-profit charity, so that contributions to that entity could qualify for the charitable credit. The argument is that activities, not entity attributes, should govern the tax treatment of charitable undertakings. If a corporation engages in demonstrably charitable works, why shouldn’t an investment in it qualify as a charitable contribution for tax purposes? Hines et al. criticize this proposal on several grounds. The major concern is that the proposal would allow taxpayers to effectively get a deduction for private philanthropy (that is, gifts to the owners of the companies) rather than true charitable gifts. Further, tax arbitrage would also be possible to the extent that the donors are in higher tax brackets than the donees.

In addition, Hines et al. note that the economic argument for the equal-treatment proposal is that for-profit organizations are more efficient than charities and non-profits. Hines et al. note that this premise derives from the assumption that for-profits operate in competitive markets while charities and non-profits do not compete at all. Using the more realistic assumption that charities and non-profits are also in competition, especially in the market for donors, the conclusion that for-profit charities would be more efficient disappears.

A.M.


Graduate degrees in taxation for aspiring tax practitioners are generally offered in two forms: master of tax (MTax) degrees, offered by accounting and business programs,

and master of laws (LLM) degrees specializing in taxation, offered by law schools. In Canada, the University of Waterloo offers an MTax degree in English, while tax LLM degrees are offered by York University in English and Université de Montréal (HEC) in French. In addition, the University of Sherbrooke offers a maîtrise en fiscalité (MFisc) degree, which is a hybrid of these two types. In addition, Canadian students may enrol in foreign programs, such as the international tax LLM at New York University and the master of advanced studies in international tax law at Leiden University.

Information about these programs is hard to come by, other than that provided by the individual universities’ Web sites. Thus, these two articles should be helpful in providing information about the various programs and the reasons for attending them, even though the analysis is focused on the United States and on LLM programs.

A.M.

Jean-Yves Duclos, Bernard Fortin, and Andrée Anne-Fournier, “An Analysis of Effective Marginal Tax Rates in Quebec” (2009) vol. 35, no. 3 Canadian Public Policy 343-71

This study uses the database of simulated tax returns provided by Statistics Canada’s Social Policy Simulation Database and Model to analyze effective marginal tax rates of individuals and families in Quebec for the year 2002. Particular attention is paid to modelling Quebec’s many income-tested social programs, which can have a significant impact on effective marginal tax rates.

The most interesting results are the graphs showing the distribution of effective marginal tax rates across income levels for the population as a whole and for the various categories of family status (single parent, two-parent family, single, and childless couple). Although the pattern is difficult to summarize, the mean marginal tax rates of a childless couple and a two-parent family are, respectively, 5 percent and 10 percent higher than for a single adult.40

The paper also deconstructs the mean marginal tax rate for each family status into six components. Evidence of the importance of income-tested social programs is that the first two of the six, federal and provincial tax, represent on average just two-thirds of the effective marginal tax rate.41

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40 At 360.
41 At 362.