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## Citation Information

Bird, Richard M.. "Canada's Vanishing Death Taxes." *Osgoode Hall Law Journal* 16.1 (1978) : 133-145.  
<http://digitalcommons.osgoode.yorku.ca/ohlj/vol16/iss1/5>

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# CANADA'S VANISHING DEATH TAXES

By RICHARD M. BIRD\*

Interest in the design and improvement of death taxes continues to be high throughout the world. In the United Kingdom, for example, an integrated capital transfer tax, in which the tax rate applicable to an estate is determined by the cumulated total of a decedent's lifetime gifts plus his estate, came into force in 1975, replacing the estate duty originally levied in 1894<sup>1</sup>. Similarly, in the United States, the Tax Reform Act of 1976 substantially altered federal estate and gift taxes, by introducing a unified rate scale for transfers at gift or death, replacing the basic exemption by a credit against tax, and by making various other structural changes.<sup>2</sup> Death taxes continue in these countries to be the subject of legislation and debates on philosophical and policy issues.<sup>3</sup>

In Canada, in sharp contrast, there has been little discussion of these matters; and the direct taxation of wealth transfers has almost ceased to exist. Tax practitioners continue to be as interested as before in techniques of "estate freezing,"<sup>4</sup> presumably because any slack arising in this thriving industry as a result of the disappearance of the original rationale for the exercise (the death tax) has been taken up by the threat of capital gains taxes on realizations at death. Even those few practitioners who have reacted to the strange disappearance of Canada's death taxes have for the most part confined themselves to polite applause—a not unexpected reaction, perhaps, from those most familiar with the inevitable complexity and arbitrariness of most death tax legislation. More surprising, however, has been the silence of society as a whole in the face of this major change in Canada's tax structure. Indeed, next to the indexation of the personal income tax, I suggest that the abolition of the federal estate tax in 1971 was the most important reform of tax legis-

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<sup>1</sup> J. Chown, *Capital Transfer Tax in the United Kingdom* (1975), 23 Can. Tax J. 494.

<sup>2</sup> C. Shoup, *The Major 1976 Gift and Estate Tax Changes: An Evaluation*, Tax Notes, Special Report No. 34 (Washington: Tax Analysts and Advocates, 1977) at 2.

<sup>3</sup> For arguments in favour of death taxes, see, in addition to *id.*, U.S. Treasury Department, *Blueprints for Basic Tax Reform* (Washington, 1977) at 139 where it is suggested that the estate and gift tax would continue to be a logical part of the tax structure even if the income tax were to be replaced by a personal consumption tax. A similar view is taken in P. Mieszkowski, *The Cash Flow Version of an Expenditure Tax* (Washington: Office of Tax Analysis, U.S. Treasury, 1977) at 10, which also favours the accessions form of estate tax. On the latter, see also W. Andrews, *The Accessions Tax Proposal* (1967), 22 Tax L. Rev. 509 in U.S. and C. Sandford, J. Willis, D. Ironside, *An Accessions Tax*, (London: Institute for Fiscal Studies, 1973) in U.K. For a recent strong argument against any death taxes, see R. Wagner, *Inheritance and the State* (Washington: American Enterprise Institute for Public Policy Research, 1977).

<sup>4</sup> Judging from the continued appearance and reported popularity of the bimonthly Can. Tax J. feature on "Estate Freezing in Canada."

lation in Canada since the Second World War—important in terms not of revenue but of what it symbolized: a retreat from decades of attempts to alter wealth distribution through taxation. The general lack of reaction to this move is even more striking since, as suggested above, Canada is virtually alone in the world in abandoning death taxes.<sup>5</sup> Indeed, pressure is growing to remove the few remaining vestiges of taxes levied at death in this country. The continued whittling away of the remnants of death taxation in Ontario and Quebec, the general dislike of deemed realization of capital gains at death, and, most recently, the uproar caused by the proposal in the March 1977 budget to tax a certain component of life insurance at death,<sup>6</sup> all bear witness to these pressures. Canada, it appears, is coming closer every day to the fiscal paradise that one recent U.S. writer envisaged would emerge in the United States if that country abolished the death tax.<sup>7</sup>

In these circumstances, it may be of interest to review the history of death taxes in order to understand the present position in Canada. This paper will largely focus on this task, while briefly considering a few implications of the abolition of Canada's only taxes on personal wealth.<sup>8</sup>

#### THE RISE AND FALL OF DEATH TAXES<sup>9</sup>

The first death taxes levied in Canada took the form of succession duties imposed by four provinces (Ontario, Quebec, New Brunswick and Nova

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<sup>5</sup> While in few countries are death taxes as important as in the U.K. and the U.S., almost all countries have some such levies: the closest parallel to Canada's 1971 action appears to be Mexico's 1962 abolition of all taxes on inheritance in the federal district and territories.

<sup>6</sup> A recent brief from the Canadian Fraternal Association of Insurance Companies, for example, deplored the attempt of the Federal Government to levy income tax on policy gains at the time of death—quite a reasonable proposition from the economic point of view (N. Cameron, *The Taxation of Policyholders' Life Insurance Income* (1977), 2 Can. Pub. Policy at 129)—on the grounds that it was "a grave mistake" for the Federal Government to step in at "a time of emotional suffering and possible financial hardship." The proposal was also condemned on the grounds that it "effectively undermines the security of the family unit." (Welsh, *Low-Profile Fraternal Claim Proposals Undermine Family*, *Globe and Mail*, Aug. 13, 1977 at B3, Col. 1. Another letter on the same subject claimed that "death is the worst possible time and circumstance to be levying new taxes." *Globe and Mail*, June 17, 1977).

<sup>7</sup> R. Wagner, *supra* note 3, at 87 suggests that the abolition of death taxes is (to quote his subtitle) a necessary tax principle "for a free and prosperous commonwealth."

<sup>8</sup> It may be argued that the most significant taxes on wealth in Canada—though this assertion represents more of a foray into the field of economic theology than I want to make in this paper—are the corporate income tax and the property tax. In both cases, however, the taxes are "blind" with respect to the persons upon whom they impinge, even if in terms of broad income classes their ultimate incidence (as calculated by bolder economists than I) may appear to be progressive. There can thus be no argument with the assertion that death and gift taxes represented our only attempt, however feeble, to tax *personal* wealth. Other approaches are, of course, possible: see A. Tait, *The Taxation of Personal Wealth* (Urbana: University of Illinois Press, 1967) and J. Cutt, *A Net Wealth Tax for Canada?* (1969), 17 Can. Tax J. 298. But the prospect of following these roads seems exceedingly dim at the present time.

<sup>9</sup> For the most part, this section of the paper is a revised and updated version of material appearing in R. Bird and M. Bucovetsky, *Canadian Tax Reform and Private Philanthropy*, Can. Tax Paper No. 58 (Toronto: Canadian Tax Foundation, 1976).

Scotia). Within the next few years all the other provinces introduced similar duties. As a rule, these taxes, although modelled after the inheritance taxes enacted a few years earlier in New York and Pennsylvania, imposed rates in accordance with the aggregate value of the *estate*, with the rates varying by class of beneficiary, as well as by the size of the individual legacy.<sup>10</sup> When estates were subject to tax in different provinces, the application of this complex structure gave rise to considerable difficulty and was a cause for concern in the 1920's and 1930's.<sup>11</sup> Most problems in this area, however, were resolved after the federal government imposed a death tax in 1941.<sup>12</sup> The federal tax also, initially took the form of a succession duty until it was changed to an estate tax in 1959.<sup>13</sup>

In exchange for a "rental" payment from the federal government equal to the revenues they had collected in 1940, all provinces renounced their succession duties for the wartime period. After the war, only Quebec and Ontario again levied their own inheritance taxes, in much the same form as before, with credit being given for these taxes against the federal tax up to a maximum of one-half of the latter. The other provinces continued to receive a share (for many years, 50 percent) of the federal estate tax collections which were allocated to them.<sup>14</sup> In 1963, however, British Columbia withdrew from this agreement and reintroduced its own succession duty, largely on the grounds that the province had been losing revenue owing to the particular way in which the *situs* rules of the federal act operated.<sup>15</sup> The next year, when the federal government increased the share of the estate tax yield going to the provinces to 75 percent, both Ontario and Quebec accepted 25 percent of estate tax collections on a direct federal payment. British Columbia, however, increased its succession duty rates to pick up the full 75 percent abatement and also took the occasion to introduce a considerably simplified rate schedule.<sup>16</sup>

The situation at the time of the Carter Report<sup>17</sup> in 1967 was therefore that the federal government levied an estate tax but paid 25 percent of the

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<sup>10</sup> J. Perry, *Taxation in Canada* (3d ed. Toronto: University of Toronto Press, 1961) at 183.

<sup>11</sup> See *id.* at 186 and Can. 2, *Report of the Royal Commission on Dominion-Provincial Relations*, (Ottawa: J. Patenaude, Printer to the King, 1940).

<sup>12</sup> A federal gift tax had been imposed earlier, in 1935 (Perry, *supra* note 10, at 102). Gift taxes are not separately discussed in the present paper.

<sup>13</sup> The 1959 Act is outlined in I. Linton, *A Review of the Estate Tax Act*, Can. Tax Paper No. 14 (Toronto: Canadian Tax Foundation, 1961). As Perry, *supra* note 10, at 103 notes, the difference in practice between the two forms of death tax was minor.

<sup>14</sup> The various changes which took place in these arrangements over the post-war period are described in A. Moore, J. Perry, and D. Beach, *The Financing of Canadian Federation*, Can. Tax Paper No. 43 (Toronto: Canadian Tax Foundation, 1966).

<sup>15</sup> Fact and Opinion (1963), 11 Can. Tax J. 87. The problem caused by the differing *situs* rules under the provincial acts is discussed by Perry, *supra* note 10, at 188.

<sup>16</sup> Fact and Opinion (1964), 12 Can. Tax J. 145 at 150.

<sup>17</sup> Can. *Report of the Royal Commission on Taxation (Carter Report)* (Ottawa: Queen's Printer, 1966).

yield from provincially-domiciled estates to all provinces except British Columbia and an additional 50 percent to all other provinces except Ontario and Quebec. These three provinces levied their own succession duties, with the duty being credited against the federal tax up to a maximum of 50 percent (Ontario and Quebec) or 75 percent (British Columbia). In 1966, for example, total death taxes collected were \$219 million, with \$118 million being collected directly by the three taxing provinces (\$58 million by Ontario alone) and the balance by the federal government, with the latter transferring close to half the proceeds to the provinces (for example, \$20 million to Ontario).<sup>18</sup>

Against this background, the Carter Commission Report recommended in early 1967 that gifts and bequests should be treated like any other form of income to the recipient, and that the separate taxes on gifts and estates be dropped.<sup>19</sup> Shortly after the Royal Commission delivered its report, however, two significant events took place in the death tax field.

The first was the introduction by Alberta in 1967 of an *Estate Tax Abatement Act*,<sup>20</sup> by which, in effect, that portion of the federal estate tax on Alberta estates which was transferred to the provinces by the federal government (75 percent) was to be rebated to the estates by the province. Death taxes in Alberta thus became at most 25 percent of those levied elsewhere in the country. A similar step was taken by Alberta's neighbour, Saskatchewan, in 1969.<sup>21</sup> Furthermore, the third prairie province, Manitoba, also announced its intention to rebate estate taxes in that year unless the federal government resolved this "competition for economic advantage" satisfactorily.<sup>22</sup> The tax was never rebated, presumably because an N.D.P. government came to power in that province in the interim.

The second event, which appeared even more significant at the time, was that the federal government substantially revised its transfer tax system in 1968 by exempting interspousal transfers, raising rates on other transfers to maintain revenues, and integrating estate and gift taxes into a cumulative progressive tax.<sup>23</sup> In taking this step, the government appeared to have rejected decisively the Royal Commission's argument for taxing bequests and

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<sup>18</sup> Data from various publications of Dominion Bureau of Statistics, Government Finance Series (later Statistics Canada, Financial Management Series).

<sup>19</sup> *Supra* note 17, Vol. 3. This linking of these two moves was effectively criticized by G. Jantscher in *Proceedings of the 20th Tax Conference* (Toronto: Canadian Tax Foundation, 1967) at 417. It is perhaps also worth noting that the intellectual parent of the Carter Report, Henry Simons, himself favoured both including gifts and bequests in income and subjecting them to a separate tax. See *Personal Income Taxation* (Chicago: University of Chicago Press, 1938) at 144.

<sup>20</sup> R.S.A. 1970, c. 126.

<sup>21</sup> *An Act to Amend the Estate Rebate Act 1969*, s.s. 1970, c. 17.

<sup>22</sup> (1969), 17 Can. Tax J. 163.

<sup>23</sup> W. Linton, *The 1968-69 Gift and Estate Tax Amendments*, Can. Tax Paper No. 48 (Toronto: Canadian Tax Foundation, 1969). These changes were generally well-conceived—and, indeed, closely related to the more recent changes in the U.K. and the U.S. noted in the introduction to the present paper.

gifts as income.<sup>24</sup> These changes, though far less radical than the Carter proposal, gave rise to considerable public outcry, to the point where it appears the whole experience may have made the government particularly cautious in this area when designing its major tax reform over the next few years.<sup>25</sup>

Nevertheless, in 1969 the federal government once again made a statement on the need for a strong federal role in the death tax field.<sup>26</sup> Six reasons were given in support of this: (1) Parliament must retain its constitutional right to impose such taxes, which were "a reasonable and an equitable way to raise public revenues";<sup>27</sup> (2) death taxes had to be linked to gift taxes to avoid evasion and only the federal government could really do this; (3) death taxes acted as a check on income tax avoidance; (4) the federal death tax limited the chances of avoiding the death taxes of those provinces which imposed them; (5) it also enabled the collection of the tax for those provinces which did not want the complications of levying their own; and (6) only the federal government could deal with the international aspects of death taxation.

In light of this position, the announcement by the federal government that it would vacate the estate and gift tax field at the end of 1971 came as a complete surprise. Three reasons were offered for this decision: the abatement movement in the prairie provinces, the low revenues received by the federal government from estate taxes,<sup>28</sup> and, most important, the desire to avoid "substantial tax impact arising on the death of a taxpayer as a result of the new capital gains tax on deemed realizations at death."<sup>29</sup> The first of these factors was said to make national uniformity impossible, while the second factor was considered—for some reason that is far from obvious—to make it impossible to allow adequately for the third factor, short of abolishing the whole tax. The federal government subsequently offered to continue to collect succession duties for three years for those provinces which decided to re-enter the field, provided at least four provinces imposed more or less uniform taxes. The nature and firmness of the federal decision to leave the death tax field completely was made clear by one condition imposed on those who would take advantage of this offer: "that the presentation to the public would make clear that it is a provincial not a federal tax."<sup>30</sup>

The immediate academic reaction to this action was generally one of surprise and of denial of the postulated connection between death taxes and

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<sup>24</sup> It also appeared, this time more in accordance with the Commission's urging, to have opted for a modified "family unit."

<sup>25</sup> This interpretation was drawn in R. Bird, *The Tax Kaleidoscope: Perceptives on Tax Reform in Canada* (1970), 18 Can. Tax J. 458.

<sup>26</sup> E. Benson, *The Taxing Powers and the Constitution of Canada* (Ottawa: Dept. of Finance, 1969) at 30.

<sup>27</sup> *Id.* at 34.

<sup>28</sup> By 1971 the federal take was only \$66 million (or about 25 per cent of total death taxes collected in that year): see *supra* note 18.

<sup>29</sup> E. Benson, *Summary of 1971 Tax Reform Legislation* (Ottawa, Dept. of Finance, 1971) at 33.

<sup>30</sup> Statement by P. M. Mahoney, Parliamentary Secretary to Minister of Finance, *Can.: H. of C., Debates*, October 19, 1971, at 8851.

capital gains taxes levied at death.<sup>31</sup> Yet with the benefit of hindsight, it is now clear that there was already a good deal of evidence demonstrating that both Canadian taxpayers and politicians *do* in fact see a clear connection between these levies, whatever the economist might say. Even a minority report to the Royal Commission Report had labelled this situation "double taxation."<sup>32</sup> Although little noticed at the time, Mr. Beauvais' attitude turned out to be more representative of the bulk of "informed Canadians" (to use one of the Commission's favourite terms) than the cavalier disregard of this position in the majority report.<sup>33</sup>

It became evident in the course of the tax reform discussion that, while more far-reaching social purposes were occasionally mentioned, revenue was clearly the main purpose of death taxes so far as most Canadians and Canadian governments were concerned. The only other widely-accepted rationale for taxing at death was to make up for some of the inadequacies of the income tax. This point of view was expressed, for example, in the 1969 federal defence of the federal death tax cited above. In an earlier discussion in 1940, the Royal Commission on Dominion-Provincial Relations had essentially stated this position very simply: "[C]apital gains are best taxed through the succession duties."<sup>34</sup> It follows, then, that when capital gains were taxed directly, as in the 1971 Act, there was much less need for death taxes for either revenue or "catch-up" reasons.<sup>35</sup> Whatever the explanation, it is clear that none of the Canadian academic proponents of taxing capital gains at death gave sufficient weight to the strong political pressures which emerged to offset this "new" tax by getting rid of the ancient death tax.

The subsequent peregrinations in the provincial succession duties demonstrated that these pressures did not stop at the federal level.

The immediate reaction of most provinces was one of great uncertainty, even though some of them, notably Quebec,<sup>36</sup> had long urged the federal

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<sup>31</sup> For a good example of this reaction, see M. Bucovetsky and R. Bird, *Tax Reform in Canada* (1972), 25 Nat. Tax J. 37; also Carter, *Federal Abandonment of The Estate Tax: The Intergovernmental Fiscal Dimension* (1973), 21 Can. Tax J. at 239.

<sup>32</sup> Mr. Beauvais, in Can.: 1, Royal Commission on Taxation, *Report*, 1966 at 62.

<sup>33</sup> Can. Standing Senate Committee on Banking, Trade and Commerce, *Proceedings*, (Ottawa, 1964-70) for example, offer a number of examples: James Richardson and Sons Ltd. (No. 22, May 7, 1970, at 68-69), Board of Trade Metropolitan Toronto (No. 35, June 18, 1970, at 122), Trust Companies Association of Canada (No. 37, June 24, 1970, at 110-111), Canadian Institute of Chartered Accountants (No. 32, June 11, 1970, at 103), Canadian Bar Association (No. 34, June 17, 1970, at 86).

<sup>34</sup> Can. 2, *Report of The Royal Commission on Dominion-Provincial Relations*, (Ottawa: J. Patenaude, Printer to the King, 1940) at 160. It is of interest to note that the position recently taken by Ontario (see below) could be put more or less the other way, that is, "successions are best taxed through capital gains taxes".

<sup>35</sup> In addition to the references in note 33 *supra*, this argument appears in various forms in, *inter alia*, Can. H. of C. *Debates*, Feb. 26, 1971 at 3803; C. MacNaughton, *Ontario Proposals for Tax Reform in Canada* (Toronto: Dept. of Treasury and Economics, 1970) at 29; Can. H. of C., Standing Committee on Finance, Trade and Economic Affairs, *Proceedings*, 1970, No. 79 (Professional Art Dealers Association) at 138; and Ontario Advisory Committee on Succession Duties, *Report*, (Toronto, 1973) at 14.

<sup>36</sup> E. Benson, *supra* note 26, at 34.

government to leave death taxation to the provinces. Ontario's reactions to the federal move have been particularly interesting and are discussed at more length below. Alberta, having already in effect opted out of the estate tax, was indifferent to the whole issue and decided to stay out of the death tax field.

Saskatchewan, however, where an N.D.P. government had recently come to power, decided initially to join Manitoba and the four Atlantic provinces in imposing a new, more or less uniform death tax (which, as noted above, the federal government had offered to collect for them, under certain conditions, for three years). Again, however, according to an authoritative account, not social philosophy but "revenue considerations were of primary concern to these six provinces; they concluded that they simply could not afford to give up this source of revenue."<sup>37</sup> This was particularly true in the case of the poor Atlantic provinces, which were apprehensive about getting into the death tax field, and which imposed the new tax only as a transitional measure "until capital gains take full effect."<sup>38</sup>

In 1972, then, immediately after the tax reform, the federal government was collecting a new uniform succession duty for six provinces, while three continued to levy their own duties, and one (Alberta) had no death taxes at all. Although in all cases (except Ontario, where the provincial rates were raised to make up for the federal withdrawal) the new death tax rates were generally lower than before 1972,<sup>39</sup> this change appeared to be unimportant because the provinces had made up for the federal lapse in this field. The situation was not static, however.

Since 1972, for instance, all four Atlantic provinces, concerned by the prospect of capital flight,<sup>40</sup> have withdrawn from the death tax field. In fact, Prince Edward Island never collected the tax in 1972, and its early withdrawal led directly to that of the three neighbouring provinces, who apparently feared a loss of investment to the Island "tax haven."<sup>41</sup> Several of the other

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<sup>37</sup> W. Goodman, *The New Provincial Succession Duty System*, Cdn. Tax Paper No. 56 (Toronto: Canadian Tax Foundation, 1972) at 1.

<sup>38</sup> Mr. Simard, New Brunswick Minister of Finance, N.B., *Debates*, 1972, at 18.

<sup>39</sup> As early as 1973 total death tax collections fell below \$200 million for the first time since 1964 (see *supra*, note 18): preliminary calculations by M. Bucovetsky and R. Bird (see *supra*, note 9, at 54) suggested that this loss in death taxes was *not* offset by the new revenue collected through income taxes on gains deemed at death. Although over time one would indeed expect the federal revenue from the latter source to exceed that foregone through the death tax, it is by no means farfetched to view the provinces as continuing to be net losers in revenue terms alone for many years to come, perhaps forever: see J. Bossons, *Economic Overview of the Tax Reform Legislation*, Proceedings of the 23rd Tax Conference (Toronto: Canadian Tax Foundation, 1972) at 56.

<sup>40</sup> Even though the basis of the new succession duties made avoidance of the tax possible only if the heirs moved too. See J. Bossons, *The Effect of Income Tax Reform on Estate Taxes in Canada*, Proceedings of National Tax Association, Tax Institute of America, 1973 (Columbus, 1974) at 150.

<sup>41</sup> For references to the "tax haven" problem, see "*Maritime Premiers Discuss Tax*," Canadian News Facts, (Toronto: Dec. 1-15, 1972) at 933, and the exchange between an opposition member and the Nova Scotia Minister of Finance, N. S. House of Assembly, *Debates and Proceedings*, Feb. 23, 1973, at 936. (Incidentally, Prince Edward Island estimated that total collections from the new death tax over three years would amount to only \$240,000, which may explain why it decided not to levy the tax at all.)



taxing provinces also reduced the rates of their succession duties substantially, or raised the exemptions, in the first few years after federal withdrawal from the death tax field.

More recently, similar fears of the attractiveness of Alberta as a "tax haven" appear to have been an important motive in the abolition of the succession duties in British Columbia (1977 Budget) and in Saskatchewan (1976 Budget), although that province has an N.D.P. government. The Finance Minister of British Columbia, for example, reportedly argued "that capital which might otherwise have been invested in British Columbia has been invested elsewhere and that the removal of succession duty was designed to encourage the investment climate in the province."<sup>42</sup> Even the N.D.P. government in Manitoba, despite a statement by the Finance Minister that "the government still believes that people who inherit large sums of money should pay tax on it," announced changes in the provincial succession duties to basically halve the revenue from the succession taxes (by exempting a spouse's share of marital assets and raising the basic exemption level).<sup>43</sup> Almost the first act of the new Conservative government in that province was to live up to its campaign promise of abolishing the death tax. Although Quebec has not abolished the tax, it has not only raised exemptions in 1972 and 1973, but has steadily reduced its rate structure to the point where the 1977 rates are only 20 percent of those that were in force at the time of the abolition of the Federal Estate Tax: the maximum rate is now only 7 percent for strangers and 5 percent for the beneficiaries in the direct line of inheritance. Indeed, the tax was scheduled to be eliminated in 1978 until the Parti Québécois government, elected in 1976, decided to give the matter further study.

The 1967 report of the Ontario government's Taxation Committee noted that a reasonable taxation of wealth in general, and death taxes in particular, had a significant role to play in controlling extremes of wealth.<sup>44</sup> While unexceptionable, this passage is noteworthy as being perhaps the most explicit nonrevenue rationale ever put forward officially for taxing wealth at death.<sup>45</sup> The Report went on to make detailed proposals for the revision of the Succession Duty Act (which was in form very similar to that first introduced in 1892). It further suggested that the federal government should withdraw from the death tax field because it got little revenue from this source.<sup>46</sup> The recommendations of this Committee were considered in detail in 1968 by a Select Committee of the Legislature, which generally agreed with this part of the Report.<sup>47</sup>

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<sup>42</sup> 1977 *British Columbia Budget*, (Price Waterhouse & Co. Tax Bulletin, Jan. 25, 1977) at 2.

<sup>43</sup> S. Hoeschen, *Manitoba Retains Succession Duties but Raises Exemptions*, *Financial Post*, May 14, 1977, at 35.

<sup>44</sup> Ont. 3, Committee on Taxation, *Report* (Ottawa: Queen's Printer, 1967).

<sup>45</sup> An earlier instance may be found in *supra* note 34, vol. 2, at 119 and 157.

<sup>46</sup> Ont. 3, Committee on Taxation, *Report*, at 207. No mention was made of the danger of a return to the "tax jungle" of the 1930's, although this may have been what one reviewer of the Report had in mind when he drew the opposite conclusion, namely, that Ontario should get out of the field and leave it to the federal government—see M. Jameson, *Death and Gift Taxes* (1967), 15 *Can. Tax J.* 543.

<sup>47</sup> Ont. *Report of Select Committee on Taxation* (Toronto, 1960).

Nevertheless, in 1969, following the revision of the federal estate tax, noted above, the province proposed to take the opposite path to that recommended by the Committee and to relinquish its own succession duty in exchange for 75 percent of the revenues from the federal tax. At the same time, however, the provincial government noted that *all* death taxes should be eliminated "as capital gains taxation becomes fully mature in the years ahead."<sup>48</sup> When the actual federal proposals came out in 1969, Ontario immediately criticized them as not involving "compensating changes in estates [sic] taxation, which we believe is in critical need of reform in terms of the total taxation of wealth."<sup>49</sup> "Our principle is simple," said the Ontario Treasurer around this time, "if capital accumulation is taxed on a pay-as-you-go basis it should not be taxed heavily again at death."<sup>50</sup> As "immediate relief"—from the debilitating effects of contemplating a capital gains tax?—the province in 1970 therefore increased exemptions for spouses to \$125,000 from the previous \$75,000.

By the following year, when the federal withdrawal from the death tax field had been announced, the province continued to be concerned with the need "to establish a connection between estate taxation and capital gains taxation." It therefore stated its intention to retain death taxes in order to maintain this connection and to get a fair share of the revenue.<sup>51</sup> Although the intention to eliminate the succession duties within five years in order to avoid "confiscatory taxation of wealth" was reaffirmed, the reduction was to be gradual and progressive. Later in 1971 the spousal exemption was doubled (to \$250,000) and several other changes were made, presumably in furtherance of this goal.<sup>52</sup> By the end of the same year, the provincial government, despite the trend in the rest of the country, had decided to double its own tax rates to compensate for the lost revenue and, interestingly enough, for "equity reasons," as the capital gains tax was not yet fully in operation.<sup>53</sup> To soften the blow, however, the general exemption was raised to \$100,000 and the spousal exemption to \$500,000, reducing the number of dutiable estates to about 2,000 a year.

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<sup>48</sup> 1969 *Ontario Budget* (Toronto, 1969) at 58. Although the capital gains taxes referred to here were those which the province had announced its intention of imposing as part of its own income tax, this statement, as noted below, apparently still represents Ontario's policy today.

<sup>49</sup> 1970 *Ontario Budget* (Toronto, 1970) at 29.

<sup>50</sup> MacNaughton, *supra* note 35, at 29.

<sup>51</sup> 1971 *Ontario Budget* (Toronto, 1971) at 27.

<sup>52</sup> D. McKeough, *The Reconstruction of Economic and Fiscal Policy in Canada* (Toronto: Dept. of Treasury and Economics, 1971) at 25. At this time additional measures were also taken to relieve small firms and, especially, family farms, from the estate tax pressures they were allegedly suffering: as mentioned below (*infra*, note 58) these pressures appear to be more alleged than real but there is no denying the powerful psychological appeal of relief to small business and especially farms: for some further reflections on this point, see R. Bird, *The Case for Taxing Personal Wealth*, Report of the Proceedings of the 23rd Tax Conference (Toronto: Canadian Tax Foundation, 1972) at 20.

<sup>53</sup> D. McKeough, *Introduction to Supplementary Estimates and Tax Legislation* (Toronto: Ont. Dept. of Treasury and Economics, Taxation and Fiscal Policy Branch, 1971) at 27.

Ontario's reactions continued to be somewhat guarded in 1972: although the policy of reducing the level of succession duties as the capital gains tax matured was restated,<sup>54</sup> no changes were actually made and a special advisory committee was set up to examine the succession duty field. This advisory committee reported early in 1973. Its Report accepted without question the proposition that the capital gains tax plus the succession duty constituted a "double tax burden,"<sup>55</sup> and suggested that the best way to alleviate this problem was for the federal government to eliminate deemed realization at death and allow either a tax-free transfer at death or the carryover of basis.<sup>56</sup> A less desirable, but presumably more feasible, solution suggested was to allow a credit against the succession duty for taxes paid on deemed realizations and recaptured depreciation.<sup>57</sup> In addition, the Report recommended sharp cuts in the rates of duty and liberalization of the exemptions, especially for farms, as well as an extension of the payment period to ten years (with interest at the general borrowing rate). As these recommendations suggest, the entire Report was overwhelmingly concerned with solving "the problem of the deeply-felt burden of two, separate, unintegrated different death taxes."<sup>58</sup>

Without responding explicitly to this Report, the government felt it necessary to restate in its 1973 budget its policy of decreasing death taxes, both because of the "undesirable impact on small businesses, family farms and Canadian ownership" and because other provinces were vacating the field.<sup>59</sup> In addition, further alleviations were introduced, including complete inter-spousal exemption and several special provisions for farmers.

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<sup>54</sup> 1972 *Ontario Budget* (Toronto, 1972) at 37.

<sup>55</sup> Ont. Advisory Committee on Succession Duties, *Report* (Toronto: 1973) at V.

<sup>56</sup> *Id.* at 10. Although a similar carryover of basis was introduced in the 1976 *U.S. Tax Reform Act*, this provision—which had also been suggested in the 1969 Canadian tax reform proposals—is seriously deficient in several important respects: see J. Katchen, *Deemed Realization: A Proposal* (1970), 18 *Can. Tax J.* 342.

<sup>57</sup> Precisely the opposite solution—the crediting of death taxes against capital gains taxes—had been considered by the Commons Committee, and rejected on the grounds that it would make the deemed realization proposal pointless. *Eighteenth Report of the Standing Committee on Finance, Trade and Economic Affairs Respecting the White Paper on Tax Reform* (Ottawa, 1970). One may perhaps infer that the Advisory Committee had a similar end result in mind.

<sup>58</sup> Advisory Committee, *Report*, *supra* note 55, at 14. This line of reasoning is especially hard to follow because the Report itself makes it clear that *at most* very few estates were likely to encounter any substantial tax or liquidity difficulties. Appendix C of the Report, for example, which reports on a study of all estates in 1970 and 1971 (when many more estates were taxed than in later years) found almost no evidence at all of the oft-alleged tax-induced sales of family businesses and firms: only 4 per cent (10) of the farms and 10 percent (12) of the family-controlled businesses included in the dutiable estates in 1970 and 1971 were reportedly sold to pay taxes. (Fewer than 600 of the 10,000 estates taxed in those two years reported such assets). *In no case* were these sales to foreign owners. This evidence is not cited in the body of the Report itself, however, which instead appears to be concerned entirely with the (totally undemonstrated) possible deterrents to "active risk-taking entrepreneurs" (p. 5), of whom there are said to be "only a few" (p. 10). In thus ignoring its own evidence the Advisory Committee followed the precedent set by other commentators on this subject: facts, it appears, can never shake beliefs. (For further examples, see R. Bird and M. Bucovetsky, *supra* note 9, at 146).

<sup>59</sup> 1973 *Ontario Budget* (Toronto, 1973) at 29.

By 1974, although there was an apparent reversal of the *stated* goal of policy in this area ("we intend to continue to tax large accumulations of wealth"<sup>60</sup>), exemptions continued to be liberalized.

Estates of less than \$150,000 (compared to the previous \$100,000) were exempted and various exemptions for dependents were increased, as was the scope of the forgivable farm duty introduced in the previous year. The 1975 budget extended still further the "alleviations" of the prior two years, and not only raised the basic exemption to \$250,000, but also made this amount a deduction from aggregate value in determining applicable rates.<sup>61</sup>

While the 1977 Budget stated that the succession duties should be retained because "they add a valuable degree of equity to the Province's tax structure," the province then proceeded to make capital gains tax payable on deemed realizations at death creditable against succession duties, as had been earlier suggested by the Advisory Committee.<sup>62</sup> In addition, the burden of the succession duty was further alleviated by raising the basic exemption to \$300,000 and by providing that the additional rate would not apply to receipts of less than this amount by any individual. The government further noted that: "It is expected that this credit mechanism will result in ever-increasing reductions in succession duty over time, as the value of capital assets increases and the Succession Duty Act is amended periodically to recognize the effect of inflation."<sup>63</sup> Ontario had thus held consistently to its 1969 position of the effective elimination of death taxes as capital gains taxes "matured." Whatever degree of equity the death tax added could as well be achieved through the taxation of capital gains at death, or so the province seemed to be arguing.<sup>64</sup>

To sum up, the situation at present is that there are succession duties in only two provinces. Even for these provinces, retention of death taxes is uncertain, apparently almost regardless of the political colouration of the government in office. What will happen over the next few years remains unclear, but it seems improbable that the general downward trend in death taxes will be reversed. Five years of experience has shown that the federal abandonment of the estate tax has both considerably increased national disparity in death taxes and substantially lowered the general level of taxes levied on personal wealth in Canada. Death taxes will vanish soon unless some *federal* action is taken to offset this trend—and there seem to be no signs of any such action.

## CONCLUSION

The final question to be considered is whether this prospect is to be deplored or applauded. Did the abolition of the federal estate tax (and the con-

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<sup>60</sup> 1974 Ontario Budget (Toronto, 1974) at 12.

<sup>61</sup> 1975 Ontario Budget (Toronto, 1975) at 27.

<sup>62</sup> 1977 Ontario Budget (Toronto, 1977) at 18.

<sup>63</sup> *Id.*

<sup>64</sup> That this statement is clearly erroneous was demonstrated at the time of tax reform by Bossons, *supra* note 39. There is no way in which levying a tax on certain gains accrued since 1971 can offset the basic inequity created by the initial removal of all taxes on wealth accrued prior to that date.

sequent dissolution of the provincial succession duty structure) bestow a great benefit on the rich<sup>65</sup> or was it instead an essential move toward liberation of the entrepreneurial spirit from the oppressive hand of the State?<sup>66</sup> As I see almost no merit at all in the second of these positions and have elsewhere argued at length the case for taxing personal wealth at death,<sup>67</sup> my own answer to this question is clearly that Canada has gained few, if any, benefits from its move away from death taxes and has paid a significant price in terms of reduced equality of opportunity,<sup>68</sup> probably increased inequality of wealth, and certainly increased fossilization of the structure of wealth.<sup>69</sup>

A close examination of recent Canadian data on the distribution of wealth provides no reason to alter these earlier conclusions.<sup>70</sup> Consideration of recent studies in other countries<sup>71</sup> similarly supports the importance of intervening in the process of the intergenerational transmission of wealth—perhaps with differently structured fiscal instruments that those now commonly used<sup>72</sup>—in order to reduce the potentially pernicious economic, social, and political consequences of permitting the tax-free transfer of wealth between

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<sup>65</sup> Bossons, *supra* note 39, at 54 estimated that the elimination of the estate tax amounted to the equivalent of a lump-sum transfer of \$4.5 billion to those relatively few families who owned wealth in 1971 that would have been subject to the tax in future years.

<sup>66</sup> This is the spirit of Wagner's argument, *supra* note 3.

<sup>67</sup> *Supra* note 9. The references in the following notes are to items other than those cited in this earlier paper.

<sup>68</sup> "Equality of opportunity" is admittedly a rather fuzzy concept: see K. Klappholz, "Equality of Opportunity, Fairness and Efficiency" in M. Peston and B. Corry, eds., *Essays in Honour of Lord Robbins* (London: Weidenfeld and Nicolson, 1972) at 246. Nevertheless, there can be little question that the emotion is a powerful one in shaping public policy. Indeed, a recent anti-death tax writer (Wagner, *supra* note 3) himself relies on this argument, more or less viewing life as an equal-opportunity lottery in which some big prizes are necessary to keep people participating—though he of course argues that the prizes are "merited" in some sense. Life may indeed be viewed as a lottery, a conception which may be gaining favour with Canadians these days if one judges by the current popularity of lotteries, but if there is one thing that is known about the psychology of people who take part in lotteries, it is that they must believe that lottery is fairly run. And if there is one thing that we know about the lottery of life, it is that it is not fairly run: to paraphrase something I said some years ago, some people stand not on their own feet, but on their fathers' shoulders.

<sup>69</sup> One can argue against high *income* taxes as protecting the charmed circle of those already wealthy but only very confused reasoning (*Id.* at 38) can use this same argument against *death* taxes, which have precisely the opposite effect.

<sup>70</sup> See J. Poduluk, *Measurement of the Distribution of Wealth in Canada* (1974) Review of Income and Wealth at 203, and M. Wolfson, *Wealth and The Distribution of Income*, Canada 1969-70, Paper presented at June 1977 meeting of the Canadian Economics Association (unpublished).

<sup>71</sup> A. Atkinson, *The Economics of Inequality* (Oxford: Clarendon Press, 1975) and, especially, J. Brittain, *The Inheritance of Economic Status* (Washington: The Brookings Institute, 1977).

<sup>72</sup> See *supra* note 3.

generations.<sup>73</sup> There are, of course, many problems in taxing wealth,<sup>74</sup> and no tax system can offset all the possible undesirable consequences of undue wealth concentration,<sup>75</sup> but the inability to achieve perfection has never been an acceptable excuse for failing to do what is right.

My own conclusion is clear. There are few good fiscal instruments and the death tax—on the whole a highly progressive and economically relatively innocuous tax<sup>76</sup>—was one of the few. It may be too late to reverse the considerable shift in social policy implied by the decision to let all wealth accumulated before 1971 be forever free of tax, but it is perhaps not too late to plea for a more open and objective public discussion of the strange phenomenon of Canada's vanishing death taxes.

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<sup>73</sup> For a brief catalogue of some of these effects, see A. Okun, *Equality and Efficiency: The Big Tradeoff* (Washington: The Brookings Institute, 1975). See also, for related Canadian discussion, W. Clement, *The Canadian Corporate Elite* (Toronto: McClelland and Stewart, 1975).

<sup>74</sup> Perhaps particularly the treatment of "human capital." As Brittain says (*supra* note 71, at 7): "High estate taxes may, of course, discourage bequests and encourage investment instead in a son's education and the inter-generational transmission of human capital. Given the major role found here for human capital in the generation of human inequality such a tax policy might even aggravate the problem. At the same time, the social gain from the rapid accumulation of human wealth could be an offsetting factor."

<sup>75</sup> Okun, *supra* note 73, at 30 argues, quite correctly, that societies concerned with the use of money to acquire power, particularly political power, can and should formulate and enforce specific rules to prevent spending money in undesired ways. I would add, however, that, to paraphrase Admiral Mahan's doctrine of seapower, the importance of "money in being" (that is, large blocks of wealth whether spent or not) must not be underestimated: in contrast to Okun, then, I would prefer to support such rules by taking some of this "potential power" away through wealth taxes.

<sup>76</sup> For extensive arguments on this point, see paper cited *supra* note 52.

