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Reassignment and the Power to Tax in a Federal State: Canada, 1867–2024

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Abstract

Although reassignment of policy instruments among governments in many federations is a recurring event, there is no widely accepted, *positive* model of the phenomenon. This stands in contrast to the well established body of work on the normative theory of the efficient federal assignment. In this paper, I study reassignment of the power to tax in the Canadian federation by considering three elements that are likely to be part of any complete, positive analysis. These are: the facts that characterize the fiscal history of reassignment in the Canadian federation; the logic behind the demand for tax and other instruments by provincial and national governments; and the analysis of intergovernmental trade in governing instruments, which adds the supply of instruments and closes the model. While the story I tell is constructed to deal with the Canadian case, I hope that some of the ideas and issues I raise will generalize.

Keywords: decentralization, tax assignment

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1. Introduction

Although the constitution of a liberal, democratic federal state usually includes an assignment of policy instruments among the governments that make up the federation, the effective assignment of these instruments appears to be malleable when viewed from a longer term perspective. Reassignment in a federation - that is, a change in the structure of the federation - can occur as an invasion by one level of government of another's authority, such as when one government begins to levy a tax on a base that is already taxed by another government.¹ It can involve the seizure, occupation and domination of a particular policy instrument or policy field by one level of government. Or it sometimes results from the voluntary withdrawal by one government in favor of another. Reassignment can arise as a result of formal or de jure amendments of the federal constitution. Or it may occur de facto, without a formal constitutional revision. It can move governmental authority upwards, or downwards, in the federation.

As Breton and Scott (1978, 65) observed almost half a century ago, "There has historically been enough delegation of powers from one jurisdiction to another that one need not underline the importance [of reassignment]". But I think that it does need to be underlined. To the best of my knowledge, there is no widely accepted conceptual framework that can be used to study the reassignment of governing instruments across levels of government in a liberal democratic federation. This fact, if I may call it that, stands in contrast to the normative economic theory of the assignment of policy instruments in a federal system as set out, for example, in the work of Oates (1972, 1999), Wellisch (2000), and Boadway and Shah (2009) and in the papers found in Ahmad and Brosio's (2015) handbook.² This well-developed body of work has been extended to encompass collective choice issues in the design of federations, as in Brennan and Buchanan (1980) and Inman and Rubinfeld (2020). A distinct branch of the literature focusses on the benefits and costs of decentralization as a means of making government more responsive and efficient (e.g., as in Treisman 2007) and on the role of decentralization in economic development (e.g., Martinez-Vazquez et al 2017 and Bahl and Bird 2018).

However, a normative theory of the socially efficient assignment does not explain how such an assignment is achieved, or fails to be implemented, as the outcome of an equilibrium of the economic and political processes that are at work. Consideration of why federations might fail to achieve the efficiency standard set out in the theory, for example due to commitment problems and common pool issues that are often discussed in the normative literature may help to show the way towards a positive framework. But such analyses do not by themselves constitute a positive model of an evolving equilibrium in which these problems arise.

I hasten to say that I am not able to provide a fully drawn and generally applicable positive model of the federal assignment in this paper. Rather, my purpose here is to raise the problem I have pointed

¹ Here and below, I make use of Albert Breton's (2015) terminology.

² For example, see the prescription regarding the assignment of tax instruments to central and sub-central levels of government in Boadway and Shah (2009, 91-92). I note that there a literature in which the federal assignment of tax of other policy instruments is endogenous. But it has not produced a canonical model that rivals the one the has emerged from the application of social planning to federalism. Weingast (2005) reviews some of the literature in this tradition.

to, and to consider - in the context of a study of the power to tax in the Canadian federation over the history of the modern state - three related elements that are likely to be part of any complete, positive model of reassignment. These elements are: the stylized facts that characterize the history of the reassignment of tax and other governing instruments; the logic behind the demand for tax and other powers by subnational and national governments, and a theory of intergovernmental trade in governing instruments, which adds the supply of policy instruments and, in principle, completes the model. The discussion of each element constitutes sections two, three and four of the paper. Section five concludes.

Throughout the paper, I focus on the relationship between reassignment and the power to tax of the Canadian provinces, giving less (but still some) attention to what is happening to tax structure at the federal level and with respect to other, non-tax, governing instruments including public expenditure and intergovernmental transfers. The reason for this focus on subnational taxation is that without meaningful decentralization of the power to tax, our interest in federalism is much diminished.

The federal fiscal history I document and explore in the course of the analysis is that of Canada, with only occasional reference to other countries, because it is the one that I know in some depth. No doubt the story I tell is influenced, and perhaps limited, by this narrowing of the discussion. My hope is that some of the ideas and issues I point to in the paper will generalize. But I cannot be more definite than this since the historical setting and institutional arrangements that characterize each particular federation are both unique and consequential.

2. A brief history of reassignment

It is useful to begin a discussion of the reassignment of tax instruments within the Canadian federation with a brief outline of the constitutional division of powers set out in the British North America Act of 1867.³ This establishes a baseline that can be used in the identification of significant reassignments.

Section 91 of the BNA Act grants the federal government the right to tax by any means as well as all residual power beyond the provincial powers explicitly enumerated in the next section, provided that any new federal powers are of a general nature. These rights are intended to help the federal government fulfill its responsibility to insure 'Peace, Order and Good Government', as section 91 is known.⁴ Section 92 sets out provincial powers. As far as taxation goes, the provinces are allowed to levy direct taxes.

³ The BNA Act was renamed the Constitution Act when constitution was fully repatriated from the United Kingdom in 1982.

⁴ I think it fair to say that 'Peace, Order and Good Government' referred to in section 91 was assumed by the framers to flow from the proper exercise of state power by sensible people. This Canadian approach to the foundation of the state may be contrasted with the centrality in the United States of the protection afforded to individual rights as enumerated in the Bill of Rights, as the first 10 amendments to the U.S. constitution of 1791 are known. Canadian society appears to change with the constitution of 1982 to an extent that is still evolving. The new constitution includes a Charter of Rights that gives individuals defending their own rights standing before the Supreme Court in Ottawa for the first time since 1867. The Charter opens up the possibility that, as in the U.S., the Canadian court will create for itself an active role vis a vis Parliament on behalf of civil liberty.

Provincial expenditure responsibilities are inferred from sections 91 and 92, both in the text and via subsequent judicial interpretation: provinces are responsible for health, education and social security, while the federal level is responsible for other goods and services with a national span, such as defense and foreign affairs. The provinces and the federal government share responsibility in some policy fields including agriculture, immigration, and old-age pensions.

Rather than assigning authority over types of resources, such as soil, water or fish, the BNA Act assigns authority over categories of legal ownership. Provinces are assigned powers over publicly owned lands, including their use and the revenues that flow from exploitation of resources on them. Since the Civil Code applies in Quebec, all provinces are granted rights over private property and civil rights. In addition to these explicit assignments, federal authority for direct taxation, for interprovincial and international trade and commerce, and generally for Peace, Order and Good Government, creates a role for the federal government in the regulation and taxation of natural resources and with respect to the environment: these effectively become areas of shared responsibility.

With this division of powers originating in the BNA Act of 1867, I turn to Table 1 which records important events in the development of provincial taxation from 1867 to the present, along with some other events that I think are helpful to an understanding of the evolution of the assignment of tax powers in the federation. This table is a more complete and up to date version of the ones found in some previous papers of mine (Winer 1992, 2000). To the best of my knowledge, a similar, succinct history of the power to tax in the Canadian federation is not available elsewhere.⁵

[Table 1 here]

The episodes recorded in Table 1 reflect that fact that reassignment of tax instruments is a recurring event in the fiscal history of the country. Most of these have taken place without a corresponding constitutional amendment. As La Forest (1981) and Breton and Scott (1978) have also pointed out, there evidently is wide latitude within the existing constitutional framework for de facto reassignment among government levels.

2.1 Interesting episodes in federal fiscal history

To reinforce the claim that reassignment of the power to tax is a normal event, it is useful to briefly explore six episodes in Canadian fiscal history covered in the table.

i) Provincial taxation of retail sales

The BNA Act of 1867 does not permit the provinces to levy indirect taxation. However, In the 1920's and 1930's the provinces brought a succession of cases before the Judicial Committee of the Privy

⁵ The list can be extracted at some cost from books on Canadian tax history. See Perry (1955) on the 1867-1945 period, Gillespie (1991) on 1867-1990, Winer and Hettich (1991) on 1867-1913, Heaman (2017) on 1867-1917, Tillotson (2017) on 1917-1971 and Hale (2002) on the 1970-2000 period. See also Perry (1990).

Council in the U.K., which heard appeals from the Supreme Court of Canada until 1949.⁶ A major impetus for these repeated assaults on the constitutional assignment of 1867 was the provinces' need in the 1920s for revenues to finance public utilities and economic development, followed in the 1930s by the collapse of direct tax revenues during the Great Depression. A series of court decisions eventually led to the adoption of John Stuart Mill's definition of a direct tax, which prepared the ground for sales taxation to be considered within the powers of direct taxation granted to the provinces under the constitution.⁷ It only remained for the provinces to declare that retail merchants were their collection agents to have the sales tax judicially acknowledged as a direct tax under section 92. Alberta and Saskatchewan then implemented their own sales tax quickly, in the mid-1930s. The other provinces followed, but slowly, and only after the second world war.⁸

The sales tax episode illustrates what happens when the courts are repeatedly challenged by provinces struggling to finance the demands of their voters. Eventually, and without a formal change in the constitution, the privy councillors went along with the invention of a provincial power to levy indirect taxation.

ii) Wartime tax rentals and the reclamation of the provincial power to tax income

In contrast to the previous episode, the power to tax in this case initially goes up instead of down, and then goes downwards again. The courts remain uninvolved throughout.

The substantial economic burden of rearming and fighting the second world war led the provincial governments to voluntarily cede their powers to tax personal and corporate incomes to the federal government in exchange for 'tax rental' payments.⁹ When the war ended, Quebec immediately reestablished its own personal and corporate taxes, which it also self-administered. (It remains the only province to have continually self-administered both taxes in the post-war era.)

The other provinces moved more gradually, often making an arrangement with the federal government to administer a provincial personal or corporate tax on their behalf. Under the post-war Tax Collection Agreements, when the federal government collected a provincial tax, thus saving the province the considerable cost of its administration, restrictions applied concerning the extent to which the structure of the provincial tax could deviate from its federal counterpart.¹⁰ Later on, these restrictions led some provinces to partially withdraw from the tax agreements in order to

⁶ In 1933 Canada passed the Statute of Westminster granting itself legislative independence. The Supreme Court Act in 1949 abolished appeals to the Judicial Committee in most cases.

⁷ In his *Principles of Political Economy*. Mill defined direct taxes as those that are demanded from the persons who it is intended should pay them, contrasted with indirect taxes which are levied on one person but ultimately paid by another through higher prices. See La Forest (1981, chapter 4) and J. Harvey Perry (1990, chapter 12) for details of the relevant cases brought before the Judicial Committee.

⁸ Alone among the provinces, Alberta dropped its sales tax soon after it was introduced, never to reinstate it (as of 2024). Provincial sales taxes applied to final or retail sales and so differed from the manufacturer's sales tax at the federal level previously established in 1920. The federal tax did not apply at the retail level, though of course consumers effectively paid much of the tax.

⁹ The same development occurred in Australia.

¹⁰ The restrictions imposed on provinces under the Tax Collection Agreements are discussed in Gagné-Dubé (2023)

(re)establish their own corporate tax administrations.

The provinces desire to increase their control over the structure of the personal income tax is also evident in Table 1. The reclamation by the provinces of the power to tax personal incomes proceeded in several steps, with tax collection agreements being amended accordingly. The provinces typically first agreed to a federally administered provincial tax on income levied as a percent of federal income tax collected in the province - a 'tax on tax' as it was called. The provinces later successfully negotiated to levy their income tax directly on provincial incomes. Eventually the federal government even agreed to administer some provincially mandated special provisions.¹¹ This gradual shift downwards of the power to tax personal income occurred over several decades, depending on the province, and the process was not complete until the early 2000s.

The second world war evidently cast a long shadow on fiscal federalism.

iii) Succession duties

For an example of a failed reassignment that was voluntarily agreed to by both levels of government, it is instructive to consider the federal tax reform of 1972 that followed on from the Royal Commission on Taxation (1966).

The main component of the tax reform was federal half taxation of realized capital gains. Perhaps to offset the now heavier federal taxation of wealthy asset holders, the reform package also included the transfer of federal succession duties to the provinces.¹² The unsurprising result of this change was that taxation of wealth transfers was, sooner or later, competed away by provinces eager to gain and retain rich taxpayers.

One should note that from time to time other complete reassignments - occupations in Breton's terminology - have been recommended by policy advisors. For example, as noted in Table 1, the Royal Commission on Dominion-Provincial Relations (1940, vol. 2) recommended that all direct taxation be reassigned to the federal level.¹³ Essentially the same proposal has been made a few times over the decades, partly on the basis of the argument that the federal government is better equipped to cope with the consequences of the tax-elasticity of direct taxes on income. None of these proposals have been implemented.¹⁴

¹¹ These special provisions are not listed in Table 1.

¹² Succession duties had long been levied at the provincial level.

¹³ This Commission is also known as the Rowell-Sirois Report. The Report also recommended increased transfers to the provinces through equalization payments and grants, which did occur after the war.

¹⁴ The latest failure of a planned reassignment concerns the federal government's attempt to create a national capital market regulator in place of the existing set of provincial regulatory systems. The plan, in development for some decades, was formally introduced by the Harper government in 2009. After the Supreme Court declared it unconstitutional in 2011, a Quebec Court of Appeal ruled in 2016 that a subsequent cooperative approach with the provinces was also unconstitutional. The organization set up to implement the cooperative approach, which had been agreed to by several provinces including Ontario, was then dissolved in 2021 and all implementation efforts were suspended.

iv) The National Energy Program, provincial access to indirect taxation of resources, and the Notwithstanding Clause

This episode involves reassignments both upwards and downwards. It begins with the federal National Energy Program (NEP), introduced in 1980 following the dramatic increase in the price of oil after the OPEC embargo of 1973 and the Iranian revolution in 1979. The NEP allowed the federal government to increase its share of the difference between the pre-OPEC price of oil and the new, much higher international price, in order to finance imports of oil used on the East coast and to help Ontario and Quebec adjust to the higher price of energy. The NEP inflamed western passions. Court battles followed as the provinces tried to further invade the field of indirect taxation to increase their capture of oil rents, only to be rebuffed.

Then the Prime Minister decided to repatriate the Canadian constitution fully from the U.K., for which provincial assent was required. This led to Section 92A of the new constitution of 1982 allowing the provinces to levy indirect taxes on the output of natural resource firms *not situated* on crown-owned lands. (Recall that the BNA Act of 1867 assigned authority over *public* land to the provinces.) This reassignment of the power to tax downwards, part of the payoff to the provinces for their assent to repatriation, allowed them to substitute simpler and more certain royalty or rental charges for the extraction of natural resources for the more complicated and less certain taxation of corporate profits.

Another part of the deal with the provinces was the insertion in the new constitution of section 33 - the Notwithstanding Clause - permitting them to shelter provincial legislation from parts of the new Charter of Rights for a renewable 5-year period. I will return to this unusual constitutional provision later, explaining why it is relevant to an understanding of the federal assignment.

v) The harmonized value added tax

This is an example of a reassignment upwards, one that partially reversed the effects of the judicial interpretations in the 1930's that allowed the provinces to levy sales taxes.

In 1991 the federal manufacturer's sales tax was replaced by the Goods and Services Tax (GST), a value added tax that eliminated tax cascading, reduced taxation of capital inputs and extended federal sales taxes to services. The rate of the new tax was 7%, lowered to 5% in 2008. This was a major reform that I shall simply take as a starting point for the purposes of the present discussion. The federal government had tried for some years prior to the GST to interest the provinces in a national consumption tax that would be jointly administered. However, because such a tax would attenuate provincial control over the level and structure of sales taxation, only Quebec agreed to harmonize the base and rate of its own sales tax with that of the GST and, in this case, Quebec successfully insisted on the right to maintain its own tax collection while also being paid to administer the federal GST on domestic sales within Quebec.¹⁵

¹⁵ The federal government only collects the Quebec tax owed on international imports along with its own GST on imports. As of 2024, the Quebec QST rate is 9.975%.

It took until 1997 for Ottawa and three of the four Atlantic provinces to implement a Harmonized Sales Tax (HST). (The fourth and by far the smallest of the Atlantic provinces, Prince Edward Island, only adopted the HST in 2013.) The base of the new HST is basically that of the federal GST.¹⁶ A limited number of rebates that effectively create distinct provincial tax treatments is provided to participating provinces, though these are fewer in number than were the special provisions that existed under the provinces' administration of their own retail sales taxes.

To deal with the threat posed by interprovincial competition over the rate of the HST, reductions in the HST rate are to require the unanimous approval of all participating provinces, while increases in the rate need the approval of the federal government and the affected province(s).

From its inception, the HST was administered and collected by the federal government at no financial cost to the participating provinces, and provincial sales tax administration was eliminated. In addition to saving these provinces the cost of administration, the federal government paid the three participating provinces about one billion dollars over the first four years of the agreement to mitigate revenue losses due to the lowering of the overall sales tax rate applying in each province to 15% (= an 8% provincial rate plus 7% GST), and the granting of input tax credits under the credit-invoice value added tax system. In addition to these inducements, the federal government allowed firms in participating provinces to partly offset any future increases in provincial capital taxes at the expense of the federal treasury.

Despite the favorable terms offered by the federal government, however, other provinces took their time adopting the HST with federal administration: Ontario agreed to join the HST system in 2010, two decades after the tax was introduced at the federal level, while PEI joined in 2013.¹⁷ British Columbia joined the harmonized vat system in 2010 but withdrew a few years later in favor of its old sales tax, and Manitoba and Saskatchewan also continue to levy their own sales taxes. (Alone among the provinces, resource-rich Alberta does not levy a sales tax.¹⁸)

vi) Conflict over carbon emission taxes

Federal-provincial conflict over the power to tax carbon emissions is reminiscent of the struggles by the provinces to gain the power of indirect taxation of sales and of natural resources. This conflict is ongoing. Its longer run consequences for the federal assignment are not yet clear.

The fact that production and consumption of oil and gas are separated and concentrated in producing and consuming provinces creates a heightened level of discord, in this case over the related issues of natural resource development and carbon emissions taxes as a response to climate warming. It is hardly surprising that producing provinces want high levels of natural resource development and lower taxes on carbon emissions, and that the environmental movement in Parliament, supported predominately by voters who live in non-oil-producing provinces, wants the opposite. The

¹⁶ HST revenues are divided among participants on the basis of each province's share of taxable consumption in Canada as a whole.

¹⁷ Ontario still has retail sales taxes on insurance and private sales of used motor vehicles.

¹⁸ Only the federal GST is collected in the territories Yukon, Northwest Territories and Nunavut.

longstanding view of many Albertans that they are overburdened net contributors to the Equalization system on account of the relative abundance of oil and gas tax revenue in Alberta adds to political unrest in western Canada.¹⁹

The carbon tax drama is revealed by a sequence of federal and provincial actions and counteractions (described in the present tense) that are also recorded along with other related events in Table 1:

- The federal Greenhouse Gas Pollution Pricing Act of 2018 establishes a backstop to apply in provinces and territories that do not implement a compliant carbon pricing scheme, with any federal emissions taxes collected within a given province to be rebated to taxpayers in that province. Soon after this legislation comes into force in 2019, Alberta, Saskatchewan and Ontario formally challenge the constitutionality of the federal carbon pricing system;
- Before the court is able to decide the case, in 2020 Alberta introduces its own system of emissions reduction in a bid to reduce the impact of carbon taxes on producers. (After some tightening, this Technology Innovation and Emissions Reduction System is accepted by the federal government a few years later);
- The provinces lose their Supreme Court case in 2021. The majority of the court rules that because the carbon tax is national in scope and importance, it is justified under the *Peace Order and Good Government* clause; it argues that the *National Concern Doctrine* justifies federal action because the matter is beyond the capacity of any individual province to effectively address; and that the federal action only establishes *Minimum National Standards* which do not interfere with the ability of the provinces to implement their own carbon pricing schemes;²⁰
- Partly in response to the Supreme Court decision, in 2022 Alberta passes its Sovereignty Within a United Canada Act. This Act allows it to direct provincial entities to ignore provincially designated federal laws that the legislature considers to be unconstitutional or detrimental to Alberta! (As of the date of this paper, this legislation has not been invoked or tested before the Supreme Court);
- A planned increase in the federal carbon tax to 65\$ a ton in 2023 from 50\$ in the previous year comes into force and, at about the same time, the federal government announces a three-year pause on the carbon tax for home heating oil. This form of heating is particularly important in the Atlantic region, which sends a large number of representatives of the governing party to Parliament. With the intention of providing analogous relief to Saskatchewan voters for natural gas heating used widely in that province, the provincial government passes The SaskEnergy Carbon Tax Fairness for Families Amendment Act giving it sole authority over decisions regarding the collection and remittance of the federal carbon tax on SaskEnergy bills;

¹⁹ The unfairness felt by many Alberta voters persists despite the fact that Equalization is a federal program entirely financed by a federal tax system uniformly applied throughout Canada.

²⁰ The dissenting minority argued that the federal action overstepped the constitutional boundaries of federal power.

- The Prime Minister wishes Saskatchewan well in dealing with the Canada Revenue Authority, and in 2024 Saskatchewan files for an injunction to prevent the CRA from garnishing the province's bank accounts over non-payment of the carbon tax.

Will Saskatchewan win its case if it goes to the Supreme Court? The court's decision of 2021 suggests the answer is no. I also note that the rising popularity of the national Conservative party, which opposes the carbon emissions tax, suggests that the case may be mute before it is heard.

3. Tax structure in a liberal democratic federation

To develop a deeper understanding of the fiscal history recorded in Table 1, I rely on a model due to Hettich and Winer (1988, 1999) that explains how a fiscal system is formed and evolves over long periods in a heterogeneous, liberal democracy.²¹ The model deals primarily with tax structure, by which I mean sets of economic activities grouped into tax bases, corresponding rate structures imposed on these bases, and numerous special provisions that create differences between nominal and effective tax rates. Public expenditure is also included since we would never observe taxes in a democracy unless they financed the supply of goods that citizens want. However, in keeping with the emphasis in this paper on taxation, I will simplify the expenditure side of the budget by assuming that there is only one pure public good.²²

Any tax instrument results in a loss of political support reflecting the welfare losses, including excess burdens, resulting from economic adjustments by voters to the use of the instrument and the costs of organizing opposition to taxation. Governments that are forced by electoral competition to maximize expected support will thus want to implement a tax system that equalizes the marginal losses in political support associated with raising another dollar of revenue across the tax instruments it employs, thereby minimizing the total loss in expected support from the raising a public budget of any given size. This logic will be familiar to those who adopt the optimal tax (OT) approach to fiscal design, although in an OT framework there is no need to incorporate political margins nor to characterize a political equilibrium. Also familiar is the complexity of the tax system emerging in the equilibrium that stems from the fact that it 'pays' to tax uniquely each activity of each voter where economic or political responses to taxation differ from those of their fellow citizens.

Of course, tax systems do not single out each individual economic activity of each individual taxpayer. It is costly to acquire information about the economy and about individuals, and equity norms widely held among voters also impose constraints on policy formation. Consequently, any governing party will group related activities into composite bases to lower the transaction costs of raising revenue - the costs of becoming informed about taxpayers, of designing tax structures, and of enforcing tax laws. It will combine sets of taxable activities into tax bases on which simplified rate structures are imposed, rather than tax each individual activity at a unique rate. Such grouping or sorting will be designed to optimize the loss in political support when taxes are imposed relative to what would be possible with more differentiated treatment in a frictionless world, by balancing the loss from sorting against the gain from spending fewer resources on administration.

²¹ This description makes use to some extent of the one presented in Winer (2019, 460-462).

²² Non-fiscal policy instruments are also ignored.

A similar argument can be used to explain the existence of special provisions which exist in substantial numbers throughout any tax code. (These special provisions play an important role in tax collection agreements among governments, to which I shall return.) If there is a group which offers effective opposition to the inclusion of a specific activity in a particular base, it is usually cheaper to address it with a special provision, rather than with the creation of a separate base for the disputed item. For example, capital gains may become part of a broadly defined income tax, while being taxed at a rate that differs from the rate applied to other types of income. In other words, special provisions are a response by governments which expect to compete with opposition parties in the future. They are not deviations from some ideal tax base designed to satisfy normative criteria, which in actuality may have limited support among voters.

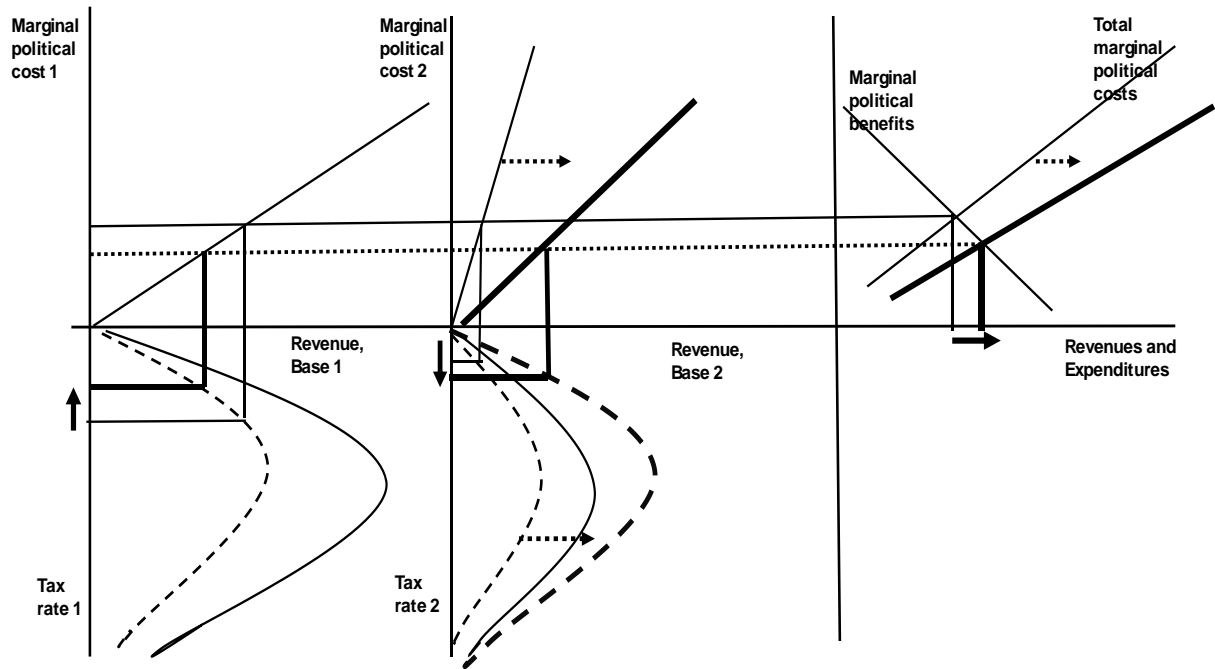
The above arguments show that a tax structure can be described as a sorting equilibrium formed in the face of information and administration costs under the pressure of electoral competition. In this framework, a significant change in the political saliency of an existing economic or political margin will lead to an adjustment of the tax skeleton. For example, if the size of an activity within a tax base expands, the marginal political cost of relying more heavily on the now larger base will fall, and use of this tax source will expand in relative size along with the overall size of the public sector. (This is the base effect observed for many countries in the world by Kenny and Winer 2006). The tax mix shifts toward the relatively larger base for two reasons. First, the marginal excess burden of relying more heavily on the expanding base falls relative to that of other bases. Second, relying more heavily on the now larger base disperses political opposition across a wider economic space. The public sector grows at the expense of the private sector as total political costs of taxation decline.

Figure 1 illustrates the comparative static result just described when there are two bases with associated upward sloping marginal political cost schedules, and one public good that generates political benefits that decline at the margin with public sector size. Here the effective Laffer curves for each base, shown by the dashed lines in the lower part of the figure, are drawn net of administration costs. Public sector size is determined in the third panel by the equality of the marginal political benefit and total marginal political cost of taxation schedules, the latter formed by the horizontal sum across tax sources of associated marginal political costs. The tax mix and corresponding tax rates, are determined by working backwards from the third panel so that marginal political costs are equalized across tax sources, as indicated in the figure. Note that special provisions are not represented in this simple illustration of an equilibrium tax structure.

[Figure 1 here]

It can be seen in the figure that when the size of the second base expands, its marginal political cost schedule shifts downwards leading to a new equilibrium in which taxes on the now larger base provide a larger share of total revenues. Tax rates adjust accordingly, while the downward shift of the total marginal political cost schedule leads to growth in total public sector size.

Figure 1
A single representative government in a fiscal equilibrium



3.1 *The demand for reassignment*

To adapt the model of fiscal structure I have outlined for the analysis of reassignment, two important aspects of federalism must be incorporated. First, the role of federal structure in determining the outcome of electoral competition at provincial and national levels has to be integrated into the analysis. Second, an understanding of intergovernmental trade in governing instruments is required.

Electoral competition in a federation has two key dimensions: a ‘local’ dimension, among governing and opposition parties in the various provinces and at the national level, and a federal-provincial or ‘intergovernmental’ dimension.²³ Migration and yardstick competition enhance both dimensions of competition in a federation. Electoral competition at any level that arises because of actual or threatened migration in response to inter-jurisdictional policy differentials is often referred to as voting with the feet. Yardstick competition refers to local political pressure that arises even in the absence of migration because voters and businesses in any jurisdiction expect, and will demand, the net public benefits that are observed elsewhere, or that might be provided by another government in the same place.²⁴

The intergovernmental dimension of electoral competition, which is also essential to an analysis of the federal assignment, is shaped by the facts, as I see them, that (i) people generally do not care which level of government provides the goods and services they desire, which does not mean that they assess the current or future performance of different governments equally, and that (ii) there are only a few public goods that could not, as a technical matter, be provided by either level of government. Under these conditions, electoral competition at both provincial and federal levels will sometimes resolve around claims that this or that governing party could outperform the other government level in some manner, with actions taken accordingly. Otherwise, opposition parties at each level will claim to be able to deliver better performance.²⁵ Analogously, when provincial and national politicians do better by coordinating their activities, electoral competition forces them to cooperate. For in this case, lack of intergovernmental cooperation will give opposition parties at each level a competitive advantage in upcoming elections.

It is reasonable to expect the intergovernmental competition in the federation to become more intense as the federal assignment becomes looser, in the sense that governments at different levels effectively share the responsibility for more activities or share more fully the responsibility for a given activity. Intense tax or expenditure competition will occur, for example, when the existing federal assignment grants all governments equal access to the same tax base or assigns equal responsibility for some public service such as health care.

²³ This classification differs from the often used horizontal vs. vertical one, in which horizontal competition refers to conflict between governments at the same level in a federation, while vertical competition involves conflict between federal or national and subnational governments. On voting with the feet see, for example, Somin (2020). On yardstick competition see, for example, Salmon (2020). Both of these books cover the vast, associated literatures.

²⁴ The role of international competition as opposed to competition among governments within the federation is not directly acknowledged in the discussion so far. Since international migration is generally more difficult than interregional migration, a federal government has some advantage in the collection of taxes on highly mobile revenue sources. This advantage will be acknowledged at some points in the following discussion.

²⁵ I think that this line of argument is also implied by the analysis of Canadian federalism by Riker (1964, 117-119).

I shall leave aside the analysis of intergovernmental trade in governing instruments for now. That is the subject of the next section. In the rest of this section of the paper I want to see how far towards an understanding of the federal assignment we can go when the model of tax structure I have outlined is applied while taking local and intergovernmental competition in the federation into account. This will be an analysis of the demand side of the federal assignment. By the demand side, I mean what governments at various levels in the federation *would like to do* with respect to various governing instruments. My focus remains on the power to tax

The positive model of fiscal structure I have briefly sketched explains why any government will try to use all available tax (and other) policy instruments, conditional on administration and information costs, and also to expand the list of policy instruments under its control. This is the best way to minimize the loss in political support from financing a public sector of given size. It is possible that use of a particular tax base may not be a productive part of a political platform at an early point in fiscal history (despite the reliance on both tax bases illustrated in Figure 1) if the associated administration costs are high relative to projected revenues. However, as provinces develop and their formal economies grow, tax bases expand and the provincial public service gains experience. The expansion of potential tax bases reduces the economic and political costs of relying upon them, and the ongoing decline in administration and information costs adds to their attractiveness as revenue sources. For these reasons, under the pressure of electoral competition we should expect provincial (and federal) governments to broaden the types of economic activity they would like to access as a source of revenue as time passes, while adjusting their tax mix to favor heavier reliance on those bases that are growing faster.

The pressure to move the tax mix towards relatively larger bases must have played a large role in times of substantial change, and in a similar manner at both provincial and federal levels: in the Depression when economic activity declined sharply; when post-war growth led to large increases in wages and salaries and thus in the political 'profitability' of income taxation; and again when the growth in the service sector and in international trade made taxation of services via a broad base value-added tax more valuable at the federal level. When the constitutional assignment of fiscal instruments constrained the policy choices of the provinces, as section 91 did with respect to the taxation of retail sales in the 1920s and 30s, for example, it made sense for the provinces to 'assault' the courts in the hope that they would eventually give way.

After the second war, and into the 1960s and 70s, the provinces would have liked to use their power to levy income taxation to differentiate among provincial taxpayers through the introduction of graduated tax schedules separate from those of the federal government and levied directly on income, and through provincially specific special provisions. The federal government resisted - each level of government has an interest in opposing any other government's attempt to expand its use of a jointly shared tax base - offering the provinces the inducement of tax collection agreements. These agreements required a participating province to accept the federal definition of the tax base, thus preventing the province from tailoring its tax structure more closely to its own voting public. At the same time, it is important to note that the federal government's own income tax code was steadily growing more complicated.

Analogously, in the 1970s and 80s the oil and gas producing provinces fought hard in the court of

public opinion against federal controls on the price of oil and against a federal National Energy Program designed to increase the federal government's share of what the provinces regarded as 'provincially owned' natural resource rents.

Throughout the fiscal history recorded in Table 1, the sequencing of tax policy choices by different levels of government matters. Prior occupation of a tax base by one government makes it more difficult for other governments to rely on the same tax source by raising the marginal political cost of accessing it. This sequencing effect is not apparent from a first look at Figure 1. But it is sensible to argue that the introduction of a personal income tax by the federal government during the first world war and its manufacturers sales tax shortly after - driven by the cost of the war, and then by the need to service war debt - made it more costly for the provinces to move further into provincial taxation of income or to establish their own sales taxes by shifting their relevant political costs upwards, just as the early use of the income tax by British Columbia probably increased opposition there to the federal income tax.²⁶

Before turning to the market for governing instruments, I want to say something about demands by voters for federal and provincial public goods and services: as I pointed out earlier, the demand for public goods must be part of any model of fiscal structure in a democracy. To do so, we need to think about how the marginal political benefit schedules for provincial and federal goods illustrated in the third panel of Figure 1 have been shifting over time.

What actually happened in the Canadian federation is shown in Figure 2, where own source tax revenues of federal and provincial governments - viewed here also as a proxy for the long run demand for public services provided by each of these government sectors - are graphed for the period from 1926, when provincial public accounts first become easily available, until 2022. Provincial revenues are shown before and after federal transfers.

[Figure 2 here]

Whether or not federal transfers are included at the provincial level, the figure shows that the relative tax size of the provinces grew substantially following the second world war, levelled off after the OPEC oil embargo in the early 1970s until about 2000, a period which includes the serious recessions of the early 1980s and the early 1990s, and then grew again. The tax, and corresponding expenditure, size of the provincial sector is now much larger than that of the federal government, making Canada by this measure one of the most decentralized federations in the OECD.²⁷

Depression, world war, and then growing demands for health, education and social services which

²⁶ Empirical evidence on the effects of prior use of a tax base by one level of government on another level in a federation seems scarce. Winer and Hettich (1991) show that prior issue of public debt by the provinces reduced the issue of federal debt for the 1867-1913 period.

²⁷ Despite the absence of public debt in Figure 2, the decentralization of taxation shown is indicative of substantial post-war decentralization of public expenditure in the federation: provincial expenditure rose from about 30% of the all-government total in 1950 to about 50% in 2000. It should also be noted that Figure 2 illustrates considerable total public sector growth over the post-war period at the expense of the private sector: federal plus provincial total tax size as a fraction of GNI rose from about 22% in 1950 to about 38% in 2022.

are constitutionally mandated responsibilities of the provinces, interrupted by adverse economic shocks, constitute a history that correlates well with the fiscal patterns revealed by Figure 2. But that correlation provides a satisfactory understanding of these patterns only if we assume the assignment of expenditure functions is fixed over time *despite the fact that the assignment of tax powers clearly was not*. It still remains for us to explain, for example, why some expenditure functions were not reassigned upwards, as was responsibility for Employment Insurance in 1940, and for public pensions (except in Quebec) in 1951, along with the corresponding taxation required to finance these public services?

One obvious, and often offered, explanation for post-war tax and expenditure decentralization in Canada is that it was, and remains, a response to the demand for independence by Quebec voters, for what powers are demanded and received by Quebec must be available to everyone else.²⁸ The impact of the independence movement is difficult to study because there is only one Quebec in Canada. In defense of this idea, I can only offer another, still less than conclusive, piece of evidence based on comparing Australian fiscal history with what happened in Canada.

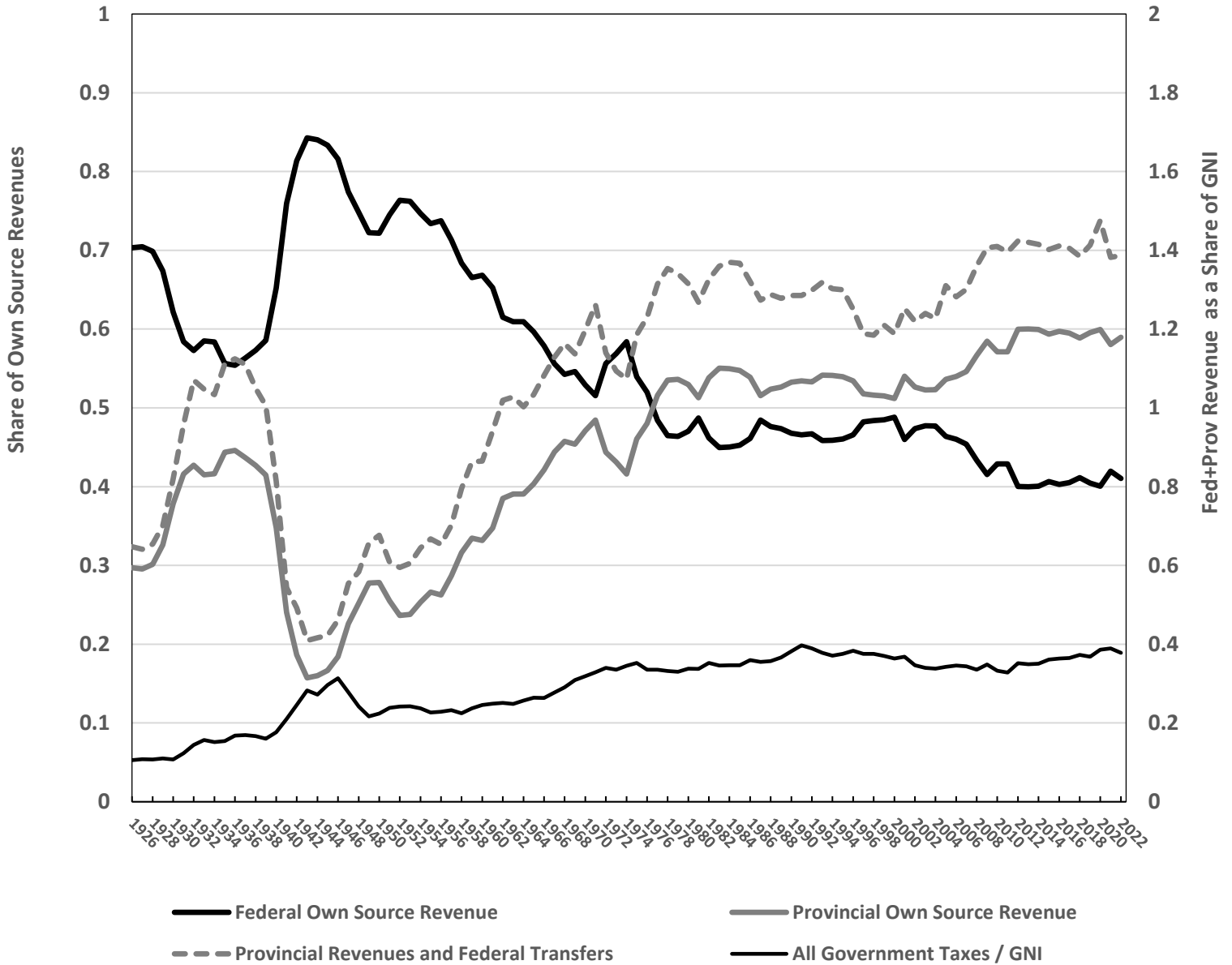
Australia experienced a reassignment of state own source taxation to the federal government during the second world war that was similar to what happened in Canada. After the war, however, the states in Australia did not regain the share of own source revenue that they had before, unlike the Canadian provinces, let alone grow their relative share to the same extent, and the Australian states still have not resumed their pre-war taxation of personal incomes. This state of affairs arose in spite of the fact that the Australian constitution of 1901 was designed to protect states' rights in opposition to what the framers saw as the undue centralization inherent in the structure of the Canadian BNA Act of 1867, in which residual power resides with the federal level.²⁹ There is no Quebec in Australia.

There are other views of the source of the fiscal decentralization illustrated in Figure 2. La Forest (1981, 26) argues that "political identification of citizens with one level of government or another is the real determinant of which government exercises the greater share of taxing power." He points to the wars as shifting power to the centre, and afterwards to the decentralizing effects of regional identifications, by which he means something broader than just Quebec separatism. Riker (1964, 118-119) provides that broader context: he argues that of greater importance than Quebec nationalism was the existence of splinter parties in the provinces that are not closely tied into the essentially two-party system at the national level, and which people viewed as legitimate and useful bargainers with the federal government on behalf of citizens in a province.

²⁸ See, for example, Riker (1964, 112-113) or Gillis (2025, 23).

²⁹ The Australian constitution does not contain a statement of residual powers. See Warden (1992) on the Australian framer's intentions.

Figure 2
Federal and Provincial Own Source Revenue Shares,
and Total Own Source Revenues as a Share of GNI.
Canada, 1926 - 2022



4. Trade in governing instruments

I think that we can go some distance in understanding the federal assignment of tax powers as well as the relative size of governments by studying two interlinked processes: the competitive pressure on every government to seek out all available tax sources and to continually adjust the structure of taxation to changing circumstances and, assuming the federal assignment is more or less fixed, the evolution of demands for public spending at different levels in the federation. This is essentially the demand side of reassignment – an explanation of what different governments in the federation would like to do – though at times I must admit that the discussion so far may, in places, appear to have the character of a longer run equilibrium analysis. To complete a model of reassignment as a market in governing instruments, it is necessary to add to demand an understanding of the conditions under which one government will supply an instrument to another.

If there is a market in governing instruments, there must be property rights in them. Therefore, let's begin the analysis by following Breton (1996, 2015) who regards the constitution as a document that establishes property rights to policy instruments of different kinds for particular governments. And with the courts as actors that can alter these rights from time to time through judicial interpretation.

I stated earlier that I would come back to the role of Section 33 in the 1982 constitution – the Notwithstanding clause – in order to explain how it relates to the analysis of reassignment. This is the appropriate place to do so. To recall, Section 33 permits provincial governments to shelter provincial legislation from aspects of the Charter of Rights for a renewable five-year period. I conjecture that embedding a Charter of Rights in the constitution increases the authority of the federal government relative to the provinces. In my view it does so by making it easier for the federal government to differentiate among citizens than for the provinces, for two reasons. First, federal differentiation that in principle applies uniformly over the whole country even while it singles out a specific activity in a particular place, is hard to detect and to prove. Secondly, the courts are likely to rule that federal legislation which nominally applies uniformly across the whole country is more acceptable than a similar action carried out within a single province. For these reasons, the Charter tends to constrain the provinces more severely than the federal government in delivering what the electorate demands. By so doing, it tends to shift the power to tax, and government authority in general, towards the federal level.³⁰ I suggest that this is the underlying reason why the provinces insisted on the Notwithstanding clause as part of the price of their assent to repatriation of the constitution.

From this point on, Breton's (1996, 2015) analysis goes like this. He argues that the effective assignment of control over various policy instruments is driven by electoral competition that forces different governments to exploit technological economies of scale in the use of governing instruments. Capturing the benefits of these economies requires that the use of policy instruments be delegated or exchanged between governments or, in other words, that instrument use be appropriately (re)centralized or decentralized as economies of scale change. Failure of intergovernmental cooperation under these conditions will yield an advantage to opposition parties

³⁰ A Notwithstanding Clause like Section 33 is unthinkable in the United States with its stronger constitutional protection for civil liberty. In light of the argument about the effect of Section 33, it is interesting to speculate on the role of the Bill of Rights as a factor that led to the rise of federal authority relative to that of the states over the last two centuries despite residual rights constitutionally residing with the states under the Tenth Amendment.

in the next election at both national and subnational levels, an argument I have already made use of in the discussion of the role of political competition in the previous section.

The giving up of a policy instrument and resulting payment to compensate for the loss of quasi-rents from its use, including intergovernmental grants of different kinds, occurs in a situation where contracts between governments are implicit and incomplete, and where post-contractual opportunism may therefore be a serious problem. In this world, the costs of negotiating and of coordinating policies across jurisdictions play key roles in determining the types of intergovernmental contracts that are finally arrived at. Tax collection technologies sometimes exhibit significant economies of scale, for example, a fact that also plays an important role in the normative theory of the optimal assignment. However, in Breton's view, even if such economies are substantial, bargaining and coordination costs may prevent exploitation of them and lead to less centralization than technological considerations alone would dictate.

This is a cogent analysis, one that I will come back to in my concluding remarks. But it is not the only approach. There is a complementary model that has been sketched by Scott (1992, 376-378). He proposed his model in a comment on an earlier paper I wrote on reassignment. I confess that at the time I did not give it the attention it deserves. In setting out his approach, I quote from some of the key paragraphs.

Scott begins by pointing out that “Politicians in a given government are constrained in their choice of tax structures [I add, by the constitution, by the structure of the economy and by electoral pressure] and turn to other governments for a removal or loosening of the constraint; politicians in the responding government are the supplier.”

He continues: “Whether a reassignment results depends on the price offered. We can set bounds on the acceptable price... From the demander’s point of view, the new tax field must come cheaper than its domestic political alternative, the dollar value of the loss in political surplus from raising rates on existing bases. From the supplier’s point of view, the base must be sold or rented at a price greater than its loss of political surplus from having less revenue with which to win votes. Between these limits, a price may be found and the transfer [of the instrument] brought about.”

“Politicians do not usually pay each other with their own cash... The demander uses the taxpayer’s money, and the supplier uses the payment to reduce his dependence on existing local taxes and so...to increase his political surplus. Thus, in Canada supplying governments [when they are provinces] have been rewarded with grants and transfers...described as ‘adjustment’, ‘equalization’, and ‘conditional’... Every government can be regarded as a net debtor or creditor of every other government. Tax reassignments go into these accounts...and lead to balancing actions in the future. It would be hard to link actual reassignments with payments for them.”³¹

If we think of the equilibrium illustrated in Figure 1 as the outcome of maximizing a political support function subject to a government budget restraint into which has been substituted the structure of the economy (see Winer and Ferris 2022 , chapters 1 – 3 for an introduction to the logic behind this

³¹ This observation suggests that empirical work on trade in governing instruments is going to be difficult.

way of representing a political equilibrium), then the maximum demand price for a new instrument in Scott's approach will be the Lagrange multiplier, or shadow price on the relaxation of the constraint. This is the politician's willingness to pay for better access to taxation in terms of their opportunity costs. The suppliers minimum supply price will be similarly calculated. Reassignments, or transfers of tax bases, take place when the governments can make a trade. "The courts play an important role...in the process, but their approval is neither necessary nor sufficient for a trade to take place. They do not set the cash or in-kind price."

So, in this way of thinking, the provinces supplied their tax bases to the federal government during the war in response to the federal government's demand. The payment was in the form of tax rentals. After the war, because economic activity grew rapidly the rental payments the feds were willing to make were not sufficient to compensate the provinces for giving up their own income taxation, and they reclaimed the power to structure their own income tax bases over the following decades. The price the provinces placed on their power to tax income was, evidently, too high for the federal government.

As another example in the Scott tradition, consider again the period surrounding the National Energy Program in the late 1970s and early 1980s. This is a time in which a trade between the oil-producing provinces and the federal government was hard to arrange. The federal government demanded more revenue so it could purchase expensive offshore oil for eastern Canada. The producing provinces were not willing to supply the revenue by reducing their royalty rates, and increased them, while the federal level increased their business taxes. A compromise was eventually reached in which, as Scott notes, the increase in oil rents was shared in a disorderly manner between levels of government. In 1982 the producing provinces were compensated for the increase in the taking of oil rents by the federal government with section 92A, giving them access to the indirect taxation of resource rents on non-crowned own land. But this 'payment' was not big enough to put an end to the conflict over resource rents, which persists into the present.

5. Concluding remarks

I have identified a set of stylized facts that characterize the history of the reassignment of tax instruments over the history of the Canadian federation, with emphasis on the provincial power to tax. In the course of doing so, I confirmed that reassignment of tax and other policy instruments among governments in the Canadian federation is a normal and recurring event. With this history in mind, I suggested in the second part of the paper how an understanding of the demand for reassignment of tax instruments may be developed by adapting a model of the formation and evolution of fiscal structure in a representative government. I used this framework to interpret some of the assembled stylized facts, including the relative size of federal and provincial public sectors. This analysis sometimes has the 'feel' of a model of a long run equilibrium as I noted earlier. But it is missing an important part of the story. To complete the analysis of reassignment, in a third part I outlined two distinct but complementary models of trade in governing instruments, and used one of them to briefly reinterpret two of the episodes recorded in Table 1.

I have not shown how the framework I assembled results in explanations or predictions that are better than that of some alternative. Still, I hope that some of the ideas I have introduced may be

helpful in constructing a more complete and generally applicable model of the reassignment of governing instruments. This will be a positive theory of how the nature and distribution of governing instruments develops over time in a liberal democratic federation. It will be free of judgements about how tax and other assignments ought to proceed and will not prescribe on economic efficiency or other normative grounds.

To conclude, I want to briefly draw attention to two issues that ought to play a role in a full analysis of reassignment, and that deserve further attention than I have accorded them here.

The first of these concerns the explanation and role of intergovernmental transfers, questions about which were raised by Anwar Shaw in his discussion at the conference. Grants are an important, quasi-independent element in the budget restraints of provincial and federal governments in the federation.³² There are several reasons why these intergovernmental transfers arise. The least studied reason for them is their role as federal payment to the provinces for the supply of an instrument. In this respect, it is important to recall that such grants may not be closely related in time to the actual trade in the governing instrument they are associated with. Grants may also arise for two other reasons which are better known in the literature: to redistribute regionally across the federation as part of insurance against aggregate risk and/or to provide greater equality in access to basic public services; and as a way of reducing the perceived tax-price of provincial public services, though federal-provincial collusion to separate spending by *each* province from its full cost, via federal taxation levied on *all* provinces.³³ The relative quantitative importance of these motives for grants is not known.

The role of transactions costs is a second issue. By transactions costs I mean the costs for citizens of acquiring information, moving between jurisdictions and signalling their preferences to governments, and the costs for provincial and federal governments of administering themselves and of coordinating their activities. Quite some time ago Weldon (1966) pointed out that in the absence such transactions costs, a model of federalism is incomplete because any assignment of governing instruments – that is, any federal structure - is feasible at the same social cost. Weldon's argument led Breton and Scott (1978) to make transactions costs the focus of their seminal study of federalism and, as I noted earlier, they play an important role in Breton's theory of trade in governing instruments. Administration and information costs are integrated into the theory of tax structure I introduced and made use of. But this is only part of the story.

Since the transactions costs I listed appear to me and others to be declining for technological reasons, it might be argued, following Weldon, Breton, and Scott, that we will observe less decentralization in the federal assignment as political competition forces governments to economize by increasing the scale at which public services are delivered. But the opposite result could also follow if we focus on the declining costs of intergovernmental cooperation to replace a central government through

³² By quasi-independent, I mean that although grants received by each province must be equal to its total expenditure less all its other sources of funds (analogously for the federal government), there are factors that determine the nature and size of grants that do not, or not in the same way, affect the other elements in the government budget restraints of donor and recipient governments.

³³ I have studied the third story concerning grants empirically in Winer (1983).

governing councils of non-central governments, an outcome that provincial governments might prefer. Or both things could happen, but in different policy areas.³⁴ In other words, it seems reasonable to expect that the declining costs of operating the public sector, if that is what is occurring, will widen the range of feasible federal assignments that we may observe in the future.

³⁴ This may be an interpretation of Boadway and Shaw's (2009, chp 17) perspective on the matter, which emphasizes the interaction of declining transactions costs with the effect of globalization.

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Table 1
Key events concerning the federal assignment of fiscal instruments in the Canadian federation
with emphasis on provincial tax structure
Canada, 1867 - 2024*

- 1867** Section 91 of the British North America Act grants the federal government the right to tax by any means as well as residual power. Section 92 sets out provincial powers: as far as taxation goes, the provinces are allowed to levy direct taxes
- 1876** British Columbia establishes a personal income tax
- 1894** Prince Edward Island establishes a personal income tax
- 1917** The federal government establishes a personal income tax
- 1920** The federal government establishes its Manufacturers' Sales Tax, a turnover tax on goods manufactured and imported into Canada. It applies at each stage of production and distribution except for the final sale to consumers. Exports are not taxed
- 1922** The (British) Judicial Committee of the Privy Council - effectively the court of last appeal before 1949 - confirms the federal government has the right to levy a personal income tax
- 1923** Manitoba establishes its own personal income tax
- 1932** Saskatchewan and Alberta establish their own personal income taxes
- 1932** British Columbia, Alberta, Saskatchewan, Manitoba, Ontario, and New Brunswick all established their own corporate income taxes during the Great Depression
- 1933-36** Newfoundland and Labrador (not yet part of Canada) defaults on its bond obligations (1933) and relinquishes self-government to Britain, regaining sovereignty (as a province) only when it joins Canada in 1949. Saskatchewan defaults on its debt obligations (1935). Alberta defaults on its debt obligations (1936). Federal support given to both provinces.
- 1936** Ontario establishes its own personal income tax, which the federal government administers. Ontario removes the rights of municipalities to levy income taxes. Alberta establishes its own sales tax only to abolish it the next year. (As of 2024, a sales tax has never been reinstated in Alberta)

***Notes to Table 1.** In addition to provincial tax structure, the table includes some events related to federal tax structure; some events concerning provincial public debt; and some changes in provincial and federal expenditure programs. A few non-fiscal policies that I think are relevant to the federal assignment are noted. Also included are some key reinterpretations of the constitutional assignment of instruments and the constitutional revision of 1982.

- 1937** Saskatchewan establishes its own retail sales tax
- 1938** Manitoba and Prince Edward Island arrange to have their personal income taxes administered and collected by the federal government
- 1939** Quebec introduces a personal income tax based on the Ontario model, which it administers
- 1940** The Rowell-Sirois (royal commission) report recommends that the provinces transfer direct taxation to the federal government. The commission also recommends increased compensatory transfers to the provinces through equalization payments and grants.
- 1940** Quebec establishes its own retail sales tax
- 1940** A constitutional amendment allows the federal government to provide unemployment insurance
- 1941** Wartime 'Tax Rental Agreements': Provinces repeal personal and corporate taxes in exchange for transfers from the federal government
- 1947** Quebec opts out of the Tax Rental Agreements and re-establishes its own corporate income tax, which the federal government collects until 1954. Other provinces re-establish their corporate tax systems which the federal government administers
- 1948** British Columbia establishes its own retail sales tax
- 1949** Nova Scotia, Prince Edward Island, and Newfoundland and Labrador establish corporate income taxes, coinciding with Newfoundland and Labrador's entry into Confederation.
- 1950** New Brunswick and Newfoundland establish their own retail sales taxes
- 1951** A constitutional amendment allows the federal government to offer old age pensions
- 1954** Quebec re-establishes its own personal income tax. It begins and continues (2024) to collect its own personal and its own corporate income tax
- 1957** Tax Rental Agreements end. Formal Tax Collection Agreements (TCAs) begin. The federal government agrees to collect personal and corporate income taxes on behalf of the provinces that opt in. Provinces retain the right to set their own tax rates subject to constraints (somewhat loosening over the years) on provincial fiscal choices: bases and rate structures have to be harmonized with the federal system; rates can be altered but have to be within mutually agreed parameters; and provinces are not allowed to impose taxes that discriminate against residents of other provinces. Most provinces (except Quebec) personal and corporate taxes are initially covered
- 1957** Tax Abatements are introduced: Provinces may reduce ("abate") their residents' federal tax

obligations by mutually agreed upon amounts. This cedes federal tax room back to the provinces, enabling them to raise their own source taxation within the same fields (primarily personal and corporate income taxes) while keeping combined federal and provincial rates stable.

- 1957** Ontario re-establishes its own corporate income tax
- 1957** A formal Equalization System to equalize the ability of every province to provide public services at comparable tax rates replaces the relatively ad hoc system of federal grants to the provinces that existed since 1867. This is a federal expenditure program. Provincial expenditure needs are not part of the calculation of a province's entitlement, which depends on a list of tax sources from a given set of provinces. (The lists of tax sources and provinces used in the calculation of Equalization entitlements evolves over time essentially according to what is manageable from the federal government's perspective)
- 1959** Nova Scotia establishes its own retail sales tax
- 1960** Prince Edward Island establishes its own retail sales tax
- 1961** Ontario establishes its own retail sales tax
- 1962** Some provinces resume a more direct role in the personal income tax field. Ontario begins to collect its own corporate income tax (until 2009).
- 1967** Manitoba establishes its own retail sales tax
- 1972** The federal government agrees to administer some tax credits for the provinces under the TCAs. Reforms stemming from the Royal Commission on Taxation (1966) come into force, including transfer of succession duties (wealth transfer taxation) to the provinces. Some taxation of capital gains introduced at the federal level as a replacement. (The latter is the main result of the Royal Commission on Taxation of 1966)
- 1973** OPEC Oil Embargo. Price of oil rises by a factor of 4. The federal government freezes oil prices (for consumers), levies export taxes to capture the difference between domestic and international prices, and uses funds to subsidize oil imported into Eastern Canada. By agreement with the producing provinces, prices are allowed to rise to about 85% of world prices by 1979
- 1977** Additional federal personal and corporate tax (percentage) points granted to provinces as part of the Established Program Financing (EPF) reforms. This transfer is part of a reform in which conditional grants for health and education are transformed into block grants delivered via a combination of tax points and cash payments. The control of the tax points remains with the federal government
- 1979** Succession duties: Ontario ends collection of its wealth transfer tax or succession duty. Succession duties have previously been abandoned by the other provinces (except Quebec)

with Alberta leading the way in 1971. Only Quebec still levies succession duties, and it also abandons this tax in 1985

- 1980** National Energy Program. Following the Iranian revolution of 1979, oil prices rise again, by a factor of about 2.5. The NEP increases federal control of the energy sector, including price controls that favor central Canada, taxes on oil revenues and exports (The Petroleum and Gas Revenue Tax) and direct investment in the energy sector. Liberal party support in western provinces collapses. The NEP is a factor in the rise of the Reform and Canadian Alliance parties in western Canada that reshape the right in Canadian politics
- 1980** First referendum in Quebec on sovereignty-association. Fails: 60% vs 40%
- 1981** Alberta establishes its own corporate income tax
- 1982** Repatriation of the Canadian constitution from Britain: the BNA Act of 1867 is subsumed into the Constitution Act. Changes of importance for the federal assignment include: i) Equalization payments to the provinces are enshrined in Section 36 without a specification of their scale and distribution; ii) Indirect taxation of non-Crown-owned natural resources is granted to the provinces in Section 92A (i.e., the provinces can count barrels of oil rather than just tax corporate profits); and iii) the 'Notwithstanding Clause', Section 33, allows provinces to shield provincial legislation from significant parts of the Charter of Rights for a renewable 5 year period
- 1987** Meech Lake constitutional amendment is proposed. It fails in 1990. Among other changes, provinces would have been able to opt out of shared cost programs with compensation if national objectives were met
- 1991** The federal government introduces a value-added tax - the Goods and Services Tax (GST) - replacing its Manufacturer's Sales Tax
- 1991** Quebec reaches agreement with the federal government to harmonize its own retail sales tax with the new federal GST, and to collect both its own and the federal GST (except for taxes on imports) with federal contributions to the province for tax administration. The base of the Quebec tax is harmonized with the federal tax by 1996
- 1991** Saskatchewan and Prince Edward Island reverse their recent decisions to harmonize with the GST, and continue to collect their own retail sales taxes
- 1993** Saskatchewan faces default on debt obligations due to low commodity prices, high debt and budget deficits leads. Urgently seeks federal assistance. The federal government provides support, and the province implements fiscal reforms to stabilize its finances without defaulting
- 1995** Second referendum in Quebec on separation with some sort of association. "Do you agree that Québec should become sovereign after having made a formal offer to Canada for a new economic and political partnership within the scope of the bill respecting the future of

Québec and of the agreement signed on June 12, 1995?" Fails 50.58 vs 49.42

- 1996** EPF is replaced by the Canada Health and Social Transfer (CHST), further consolidating federal grants. The CHST combines funding for health, post-secondary education, and social assistance into a single block transfer. This continues the trend of providing provinces with more flexibility in managing federal funds (at the expense of interregional equity?)
- 1997** The federal government and the Atlantic provinces of Newfoundland and Labrador, New Brunswick and Nova Scotia implement a harmonized value-added tax (HST) replacing provincial retail sales taxes and the GST. Administration of the HST is combined with that of the federal GST tax and provincial sales tax administration is abolished in these provinces. The "place of supply" rule applies to inter-provincial sales: Businesses must charge the tax rate of the province where the customer is located. Changes to the HST rate require the agreement of both the federal government and the participating provinces: reductions in the HST rate require unanimous approval, while increases in the rate need the approval of the federal government and the affected province
- 2000** Federal government passes the Clarity Act establishing conditions under which the government would negotiate a province's secession following a future referendum
- 2001** Ontario moves its personal income tax system from a 'tax on tax', that is, as a percent of federal tax, to a 'tax on income' basis. All other provinces soon follow, except Quebec which already has its own tax on income. Special income tax provisions administered by the federal government on behalf of the province are limited
- 2001** Alberta begins to administer and collect its own corporate income tax. Alberta also adopts a flat rate income tax. (It has never levied a sales tax)
- 2004** The CHST is split into two: the Canada Health Transfer (CHT) and the Canada Social Transfer (CST) supporting post-secondary education, social assistance, and other social services. This division provides more accountability and transparency in federal transfers, i.e., more political credit for the federal government
- 2007** Alberta becomes the first jurisdiction in North America to implement a carbon pricing policy with the Specified Gas Emitters Regulation
- 2008** British Columbia becomes the first province in North America to introduce a carbon tax, starting at \$10 per tonne of CO₂ and gradually increasing over the years
- 2009-10** Ontario reverts to having the federal government collect its corporate income tax under the TCAs. This change is part of broader tax reforms, including the introduction of the HST in Ontario in 2010
- 2010** British Columbia initially adopts the HST. But due to public opposition, a referendum is held in 2011 resulting in a decision to revert to the previous system

- 2013** British Columbia reverts to a separate, self-administered sales tax
- 2013** Prince Edward Island adopts the HST
- 2013** Quebec launches its cap-and-trade carbon pollution system, linked with California's system under the Western Climate Initiative.
- 2015** Abandoning its flat rate income tax, Alberta re-establishes a progressive income tax structure with multiple brackets
- 2018** The federal government introduces the Greenhouse Gas Pollution Pricing Act establishing a federal backstop to apply in provinces and territories that do not implement their own compliant carbon pricing systems. This includes a fuel charge and an Output-Based Pricing System for industries, with rebates of tax collected to taxpayers
- 2019** The federal carbon pricing backstop comes into effect in jurisdictions without their own systems, including Ontario, Manitoba, New Brunswick, and Saskatchewan.
- 2019** Alberta, Ontario and Saskatchewan appeal to the Supreme Court to reject the constitutionality of the federal Greenhouse Pricing Act
- 2020** Alberta introduces the Technology Innovation and Emissions Reduction (TIER) System allowing large emitters, such as oil sands operations, to meet specific emission benchmarks based on historical performance or industry standards. TIER is designed to be more lenient than the federal system, reducing costs for large emitters
- 2021** The federal government allows provincial systems like TIER in Alberta to operate if they meet or exceed the stringency of federal requirements under the Greenhouse Gas Pollution Pricing Act.
- 2021** The Supreme Court of Canada upholds the constitutionality of the federal carbon pricing framework, affirming Ottawa's authority to implement a national price on carbon emissions if provincial measures are insufficient
- 2022** Alberta amends its TIER regulations to ensure compliance with federal standards while maintaining provincial control.
- 2022** Alberta passes the Sovereignty Within a United Canada Act, allowing the provincial government to direct its entities to ignore federal laws or policies that the legislature considers to be unconstitutional or detrimental to Alberta. The act requires a resolution by the Alberta Legislature specifying the federal actions in question before provincial entities can be directed to ignore federal mandates

The frequency of events recorded in the table now increases

- 2022(Nov)** The federal government approves Saskatchewan's provincial carbon pricing plan,

effective January 1, 2023, allowing industrial carbon tax revenues to stay within the province.

2023(April) The federal carbon pricing for natural gas increases to \$65 per tonne, impacting utility bills in Saskatchewan and elsewhere.

2023(Oct) The federal government announces a three-year national pause on the carbon tax for home heating oil. The Prime Minister states that the policy will help Atlantic Canada in particular since thirty per cent of homeowners in the region use furnace oil for home heating, sparking angry demands for analogous exemptions in other provinces

2023(Dec) Saskatchewan passes The SaskEnergy (Carbon Tax Fairness for Families) Amendment Act giving the provincial government sole authority over decisions regarding the collection and remittance of the federal carbon tax on SaskEnergy bills. This legislation aims to reduce the cost of natural gas for home heating used widely in Saskatchewan

2024(July) Saskatchewan files for an injunction to prevent the CRA from garnishing the province's bank accounts over non-payment of the federal carbon tax. The federal government expresses confidence that the CRA will enforce compliance. No resolution as of December 2024