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CANADIAN TAX JOURNAL
REVUE FISCALE CANADIENNE

PEER-REVIEWED ARTICLES

Irrelevant or Even Worse? The Vicious Dilemma of the New Tax Treaty Preamble — *Andrés Báez Moreno*

POLICY FORUM

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On the Way to a Distance-Based Tax? — *Jean-Philippe Meloche, Michaël Robert-Angers, and Luc Godbout*

Comparing Canadian Output-Based Pricing Systems — *Wei Cui*

Are Carbon Contracts for Difference Well Suited for Canada? — *Wei Cui*

AWARDS

Douglas J. Sherbaniuk Distinguished Writing Award / Prix d'excellence en rédaction Douglas J. Sherbaniuk

Canadian Tax Foundation Regional Student-Paper Awards / Prix régionaux du meilleur article par un étudiant de la Fondation canadienne de fiscalité

Wayne Adams Young Practitioner Writing Award / Prix Wayne Adams du meilleur article rédigé par un jeune praticien

Canadian Tax Foundation Lifetime Contribution Award / Prix de la Fondation canadienne de fiscalité pour une contribution exceptionnelle

(Continued on inside front cover)

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FONDATION CANADIENNE DE FISCALITÉ

(Continued from outside front cover)

FEATURES

Finances of the Nation: Survey of Provincial and Territorial Budgets, 2024-25 — *David Lin*

International Tax Planning: The Fallout from Alta Energy Luxembourg—The Application of GAAR to Tax Treaties — *Brian J. Arnold*

Personal Tax Planning: Tax Considerations When Departing Canada — *Jeff Paisley and Joel Emond*

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Current Tax Reading — *David G. Duff and Alan Macnaughton*

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Vivien Morgan

1951-2025

The Canadian Tax Foundation was saddened to learn that Vivien Morgan, the Foundation's former Managing Editor, passed away on February 16, 2025. Vivien's contribution to the tax community was profound. In addition to leading the editorial department for six years, Vivien was the creator and editor of *Canadian Tax Highlights*, the Foundation's long-running monthly newsletter. Before joining the Foundation, Vivien had a distinguished career as a tax lawyer and author whose writing on statutory interpretation was quoted by the Supreme Court of Canada. Her former colleagues will sincerely miss her, and we offer our condolences to her family.

Vivien Morgan

1951-2025

La Fondation canadienne de fiscalité a appris avec tristesse le décès de Vivien Morgan, ancienne rédactrice en chef de la Fondation, survenu le 16 février 2025. Vivien a profondément marqué la communauté fiscale par sa contribution exceptionnelle. Pendant six ans, elle a dirigé le service de rédaction et a créé et a été la rédactrice du bulletin mensuel emblématique de la Fondation, *Faits saillants en fiscalité canadienne*. Vivien a brillamment exercé le métier d'avocate en fiscalité et d'auteure avant de rejoindre la Fondation. Ses travaux sur l'interprétation des lois ont été cités par la Cour suprême du Canada. Elle manquera à ses anciens collègues et nous présentons nos condoléances à sa famille.

Call for Book Proposals

The Canadian Tax Foundation, an independent, not-for-profit research and educational organization, is seeking proposals for books in the areas of taxation and public finance.

Since its inception in 1945, the Foundation has published many books and articles on a wide range of subjects within its areas of interest. The Foundation seeks proposals for research projects that will

- result in a book on a single topic of interest in the area of taxation or public finance;
- be undertaken by an experienced researcher who has expertise in an area of taxation or public finance; and
- be carried out within a time frame that is reasonable, given the nature of the project.

Projects selected by the Foundation may qualify for its full or partial financial support of the research and for its underwriting of the publication costs. The Foundation retains the absolute right at its sole discretion to choose whether to support a given proposal or to publish a project.

Interested parties should send a brief written outline of a proposal, for initial consideration by the Foundation, to:

Heather Evans
Executive Director and Chief Executive Officer
Canadian Tax Foundation / Fondation canadienne de fiscalité
145 Wellington Street West, Suite 1400
Toronto, Ontario M5J 1H8

hevans@ctf.ca

For further information, please contact the director, as indicated above, or the co-chairs of the Canadian Tax Foundation Research Committee:

Kim Brooks
c/o Canadian Tax Foundation / Fondation canadienne de fiscalité

Michael Lubetsky
c/o Canadian Tax Foundation / Fondation canadienne de fiscalité

Appel de propositions de livres

La Fondation canadienne de fiscalité (FCF) / Canadian Tax Foundation, un organisme sans but lucratif indépendant de recherche et à caractère éducatif, souhaite recevoir des propositions de livres dans les domaines de la fiscalité et des finances publiques.

Depuis sa fondation en 1945, la FCF a publié de nombreux livres et articles sur divers sujets dans ses champs d'intérêt. La FCF souhaite obtenir des propositions de projets de recherche qui :

- mèneront à la rédaction d'un livresur un sujet unique d'intérêt en fiscalité ou en finances publiques;
- seront dirigés par un chercheur chevronné ayant une expertise dans un domaine de la fiscalité ou des finances publiques;
- seront effectués dans un délai raisonnable, compte tenu de la nature du projet.

Les projets qui seront sélectionnés par la FCF pourront être partiellement ou totalement admissibles à une aide financière pour la recherche et les frais de publication. La FCF se réserve le droit absolu, et à sa seule discrétion, d'appuyer une proposition particulière ou de publier un projet.

Toute personne intéressée doit faire parvenir un bref sommaire de la proposition pour examen initial par la FCF à :

Heather Evans
Directrice exécutive et chef de la direction
Canadian Tax Foundation / Fondation canadienne de fiscalité
145 Wellington Street West, Suite 1400
Toronto, Ontario M5J 1H8

hevans@ctf.ca

Pour plus d'information, veuillez communiquer avec le directeur, tel qu'il est mentionné plus haut, ou avec les co-présidentes du comité de recherche de la Fondation canadienne de fiscalité :

Kim Brooks
a/s Canadian Tax Foundation / Fondation canadienne de fiscalité

Michael Lubetsky
a/s Canadian Tax Foundation / Fondation canadienne de fiscalité

■ Recent and Upcoming Events*
■ Activités récentes et à venir*

CANADIAN TAXATION OF TRUSTS CONFERENCE
Toronto and via webcast, May 5, 2025

JOURNÉE D'ÉTUDES FISCALES
Montreal and via webcast, May 29, 2025

PRAIRIE PROVINCES TAX CONFERENCE & LIVE WEBCAST
Calgary and via webcast, June 2-3, 2025

YOUNG PRACTITIONER FOCUS CONFERENCE
Virtual, September 3, 2025

BRITISH COLUMBIA TAX CONFERENCE & LIVE WEBCAST
Vancouver and via webcast, September 15-16, 2025

ONTARIO TAX CONFERENCE & LIVE WEBCAST
Toronto and via webcast, October 27-28, 2025

ATLANTIC PROVINCES TAX CONFERENCE
Halifax, November 7-8, 2025

77TH ANNUAL TAX CONFERENCE
Calgary, November 30-December 2, 2025

* For further details on upcoming events, please visit the Canadian Tax Foundation website at www.ctf.ca. / Pour plus de renseignements, veuillez consulter le site Web de la Fondation à www.fcf-ctf.ca.

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PEER-REVIEWED ARTICLES

1 Irrelevant or Even Worse? The Vicious Dilemma of the New Tax Treaty Preamble — ANDRÉS BÁEZ MORENO

POLICY FORUM

41 Policy Forum: Editors' Introduction—Tax Policy for the Environment — KIM BROOKS, KEVIN MILLIGAN, AND DANIEL SANDLER

43 Demand and Supply Policies for Electric Vehicle Adoption—A Comparison of Norway and Canada — NICOLAS EPELBAUM, PATRICIA JACKSON FARRELL, DHARMESH GANDHI, AND TONY PAMPENA

57 On the Way to a Distance-Based Tax? — JEAN-PHILIPPE MELOCHE, MICHAËL ROBERT-ANGERS, AND LUC GODBOUT

77 Comparing Canadian Output-Based Pricing Systems — WEI CUI

95 Are Carbon Contracts for Difference Well Suited for Canada? — WEI CUI

AWARDS

107 Douglas J. Sherbaniuk Distinguished Writing Award / Prix d'excellence en rédaction Douglas J. Sherbaniuk

109 Canadian Tax Foundation Regional Student-Paper Awards / Prix régionaux du meilleur article par un étudiant de la Fondation canadienne de fiscalité

113 Wayne Adams Young Practitioner Writing Award / Prix Wayne Adams du meilleur article rédigé par un jeune praticien

117 Canadian Tax Foundation Lifetime Contribution Award / Prix de la Fondation canadienne de fiscalité pour une contribution exceptionnelle

FEATURES

119 **Finances of the Nation:** Survey of Provincial and Territorial Budgets, 2024-25 — DAVID LIN

173 **International Tax Planning:** The Fallout from Alta Energy Luxembourg—The Application of GAAR to Tax Treaties — BRIAN J. ARNOLD

191 **Personal Tax Planning:** Tax Considerations When Departing Canada — JEFF PAISLEY AND JOEL EMOND

211 **Planification fiscale personnelle:** Considérations fiscales au départ du Canada — JEFF PAISLEY ET JOEL EMOND

235 **Corporate Tax Planning:** Navigating Intergenerational Business Transfers—Subsections 84.1(2.31) and (2.32) — SABRINA JACKSON-NAZARETH AND MATTHEW WILKINS

257 **Current Tax Reading** — DAVID G. DUFF AND ALAN MACNAUGHTON

■ Canadian Tax Journal

INVITATION TO SUBMIT

The *Canadian Tax Journal* publishes research in, and informed comment on, taxation and public finance, with particular relevance to Canada. To this end, the journal invites interested parties to submit manuscripts for possible publication as peer-reviewed articles, and it especially welcomes work that contributes to the analysis, design, and implementation of tax policies.

Articles may be written in English or French and should present an original analysis of the topic. Submitted work, or any substantial part or version thereof, must not have been previously published, either in print or online, and it must not be submitted or scheduled for publication elsewhere. The journal welcomes shorter submissions (from 4,000 to 8,000 words) focused on specific topics as well as longer submissions that analyze issues in depth.

PEER REVIEW

Submitted articles are subject to a double-blind peer review; authors' identities are not known to reviewers, and reviewers' identities are not known to authors. (Non-peer-reviewed contributions may appear elsewhere in the journal.) Final decisions on the publication of articles are made by the editors—Kim Brooks, Kevin Milligan, and Daniel Sandler—on the advice of reviewers. Reviewers are experts in the area who are chosen by the editors to provide an opinion on the publishability of the submission and to make suggestions for improvement. Submissions may be (1) accepted outright; (2) accepted if recommended revisions are made; (3) revised by the authors, as requested by the editors on the advice of reviewers, and resubmitted for further review; or (4) rejected with reasons. The time from submission to the first editorial decision is usually two months or less.

SUBMISSION DETAILS

Prospective contributors should submit a copy of the manuscript to the journal's editorial department. The preferred method of submission is by e-mail with an attached Word document. E-mail inquiries are welcome: write to CTFeditorial@ctf.ca. Contributors are responsible for providing complete and accurate citations to sources, a detailed abstract (200 to 400 words), and up to six keywords for indexing purposes.

Manuscripts accepted for publication are to be prepared in the prescribed format. For details, see the Foundation's Style and Format Guide.

Because all articles are subject to double-blind review, a separate cover page should accompany each submission. The cover page should include the author's name, e-mail and postal addresses, telephone number, and fax number. Authors should take care not to identify themselves directly or indirectly in their articles.

POLICY FORUM CONTRIBUTIONS

The Policy Forum section includes both articles commissioned by the journal editors and articles proposed by prospective authors. All articles should aim for short and rigorous analysis (3,000 to 5,000 words) and be written for an audience of policy makers, tax practitioners, and students of fiscal and tax policy. Articles may be based on original research, or they may synthesize and apply established research findings to a particular policy context.

Calls for proposals for upcoming Policy Forum sections appear on the Foundation's website and Twitter feed and are circulated by e-mail. To receive these e-mails, please contact CTFeditorial@ctf.ca and ask to have your name added to the mailing list. Proposals will be reviewed by the journal editors, and authors whose proposals are selected will be invited to prepare articles.

All Policy Forum articles are reviewed by the journal's editors prior to publication.

ACCESSING THE JOURNAL

The full text of all articles that have appeared in the *Canadian Tax Journal* since its first issue in 1953 can be found in the Canadian Tax Foundation's TaxFind database and, with a minimum one-year delay, in HeinOnline, ProQuest, and EBSCO's Business Source Ultimate database. Also, peer-reviewed articles since 1991 are publicly available on the *Canadian Tax Journal*'s Issues Index web page.

The *Canadian Tax Journal* is also indexed in Scopus, LegalTrac, EconLit, Wolters Kluwer Canada's Canadian Income Tax Research Index, Carswell's Income Tax References, Canadian Periodicals Index, and Scott's Index to Canadian Legal Periodical Literature.

■ Revue fiscale canadienne

INVITATION À SOUMETTRE

La *Revue fiscale canadienne* publie des articles de recherches et des commentaires éclairés sur la fiscalité et les finances publiques, qui sont particulièrement pertinents pour le Canada. À cette fin, la Revue invite les personnes intéressées à soumettre des articles, qui seront évalués par des pairs, pour une éventuelle publication et elle accueille plus particulièrement les écrits qui contribuent à l'analyse, à la conception et à la mise en œuvre des politiques fiscales.

Les articles peuvent être rédigés en anglais ou en français et doivent présenter une analyse inédite du sujet. L'article soumis, ou toute partie ou version substantielle de celui-ci, ne doit pas avoir été publié antérieurement, que ce soit sous forme papier ou numérique, et il ne doit pas avoir été soumis ou prévu d'être publié ailleurs. La Revue accueille les soumissions plus courtes (de 4 000 à 8 000 mots) axées sur des sujets précis et également les soumissions plus longues qui analysent des problèmes en profondeur.

RÉVISION PAR LES PAIRS

Les articles soumis font l'objet d'une révision anonyme par les pairs; l'identité des auteurs n'est pas connue des réviseurs, et l'identité des réviseurs n'est pas connue des auteurs. (Les propositions non évaluées par des pairs peuvent être publiées ailleurs dans la Revue.) Les décisions concernant la publication des articles sont prises par les rédacteurs — Kim Brooks, Kevin Milligan et Daniel Sandler — à partir des conseils des réviseurs. Ces derniers sont des experts établis en la matière, ils sont choisis par les rédacteurs pour donner leur avis en ce qui concerne le bien-fondé de publier la soumission et formuler des suggestions d'amélioration. Les soumissions peuvent être 1) acceptées sans réserve; 2) acceptées sous réserve des changements recommandés; 3) révisées par les auteurs, en fonction des exigences des rédacteurs qui suivent les conseils des réviseurs, et soumises à nouveau pour une révision supplémentaire; ou 4) rejetées avec motifs. Le délai entre la soumission et la première décision de la rédaction est généralement de deux mois ou moins.

PRÉPARATION DE LA SOUMISSION

Les contributeurs potentiels doivent soumettre une copie de leur article à la rédaction de la Revue. La méthode de transmission privilégiée est le courriel avec un document Word en pièce jointe. Toutes demandes de renseignements par courriel sont les bienvenues : vous pouvez contacter le CTFeditorial@ctf.ca. Les contributeurs ont l'entière responsabilité de fournir les références complètes et précises des documents qu'ils citent, un résumé détaillé (200 à 400 mots) et jusqu'à six mots-clés qui seront utilisés à des fins d'indexation.

Les articles acceptés pour publication doivent être préparés selon le format prescrit. Pour en savoir plus, se rapporter au Guide de rédaction et de présentation de la Fondation.

Puisque tous les articles font l'objet d'une révision anonyme par deux personnes, une page couverture séparée doit accompagner chaque article. Sur la page couverture, inclure le nom de l'auteur, l'adresse courriel et l'adresse postale, le numéro de téléphone et le numéro de télécopieur. Les auteurs doivent s'assurer qu'il est impossible de les identifier de manière directe ou indirecte dans leur article.

CONTRIBUTIONS AU FORUM DE POLITIQUES

La section Forum de politiques comprend à la fois des articles commandés par les rédacteurs en chef de la Revue et des articles proposés par des auteurs potentiels. Tous les articles doivent présenter une analyse courte et rigoureuse (3 000 à 5 000 mots) et être rédigés pour un auditoire de décideurs, de fiscalistes et d'étudiants en politique fiscale. Les articles peuvent être fondés sur des recherches originales, ou ils peuvent synthétiser et appliquer les résultats de recherche établis dans un contexte politique particulier.

Les invitations à soumettre des propositions pour les prochaines sections du Forum de politiques sont publiées sur le site Web de la Fondation, sur le fil Twitter, et elles sont également envoyées par courriel. Pour recevoir ces courriels, veuillez communiquer avec CTFeditorial@ctf.ca et demander que votre nom soit ajouté à la liste de diffusion. Les propositions seront examinées par les rédacteurs en chef de la Revue, et les auteurs des propositions retenues seront invités à rédiger des articles.

Tous les articles du Forum de politiques sont révisés par les rédacteurs en chef de la Revue avant leur publication.

ACCÈS À LA REVUE

L'intégralité de tous les articles parus dans la *Revue fiscale canadienne* depuis son premier numéro en 1953 se trouve dans la base de données TaxFind de la Fondation canadienne de fiscalité et, après un délai minimal d'un an, dans HeinOnline, ProQuest et dans la base de données Business Source Ultimate d'EBSCO. De plus, les articles révisés par les pairs depuis 1991 sont accessibles au public sur la page Web de l'Index des numéros de la *Revue fiscale canadienne*.

La *Revue fiscale canadienne* est également indexée dans Scopus, LegalTrac, EconLit, dans la section de recherche en fiscalité canadienne de Wolters Kluwer Canada, dans la section de références de Carswell, dans le Canadian Periodicals Index et dans le Scott's Index to Canadian Legal Periodical Literature.

■ Canadian Tax Foundation

The Canadian Tax Foundation is Canada's leading source of insight on tax issues. The Foundation promotes understanding of the Canadian tax system through analysis, research, and debate, and provides perspective and impartial recommendations concerning its equity, efficiency, and application.

The Canadian Tax Foundation is an independent tax research organization and a registered charity with over 12,000 individual and corporate members in Canada and abroad. For more than 70 years, it has fostered a better understanding of the Canadian tax system and assisted in the development of that system through its research projects, conferences, publications, and representations to government.

Members find the Foundation to be a valuable resource both for the scope and depth of the tax information it provides and for its services, which support their everyday work in the taxation field.

Government policy makers and administrators have long respected the Foundation for its objectivity, its focus on current tax issues, its concern for improvement of the Canadian tax system, and its significant contribution to tax and fiscal policy.

MEMBERSHIP

Membership in the Foundation is open to all who are interested in its work. Membership fees are $468.00 a year, except that special member rates apply as follows: (a) $229.00 for members of the accounting and legal professions in the first three years following date of qualification to practise; (b) $229.00 for persons on full-time teaching staff of colleges, universities, or other educational institutions; (c) complimentary for students in full-time attendance at a recognized educational institution; and (d) $197.00 for persons who have reached the age of 65 and are no longer actively working in tax. Memberships are for a period of 12 months dating from the receipt of application with the appropriate payment.

Applications for membership are available from the membership administrator for the Canadian Tax Foundation: facsimile: 416-599-9283; Internet: www.ctf.ca; e-mail: ctfmembership@ctf.ca.

■ Fondation canadienne de fiscalité

La Fondation canadienne de fiscalité est un organisme indépendant de recherche sur la fiscalité inscrit sous le régime des œuvres de charité. Elle compte environ 12 000 membres au Canada et à l'étranger. Depuis plus de 70 ans, la FCF favorise une meilleure compréhension du système fiscal canadien et aide au développement de ce système par le biais de ses projets de recherche, conférences, publications et représentations auprès des gouvernements.

Les membres considèrent l'étendue et le détail de l'information offerte par la FCF comme une importante ressource. Ils apprécient également les autres services de la FCF qui facilitent leur travail quotidien dans le domaine de la fiscalité.

Les décideurs et administrateurs gouvernementaux respectent depuis longtemps l'objectivité de la FCF, son attention aux questions fiscales de l'heure, sa préoccupation envers l'amélioration du système fiscal canadien et son importante contribution au développement des politiques fiscales.

ADHÉSION

Toute personne intéressée aux travaux de la FCF peut en devenir membre. Les droits d'adhésion sont de 468,00 $ par année, à l'exception des tarifs spéciaux suivants : a) 229,00 $ pour les personnes faisant carrière en comptabilité ou en droit pendant les trois premières années suivant leur admission à la profession; b) 229,00 $ pour le personnel enseignant à temps plein dans un collège, une université ou une autre maison d'enseignement; c) gratuite pour les étudiants fréquentant à temps plein une maison d'enseignement reconnue; et d) 197,00 $ pour les personnes qui ont 65 ans et plus et qui ne travaillent plus activement en fiscalité. La période d'adhésion est de 12 mois, à compter de la réception de la demande accompagnée du paiement approprié.

Il est possible de se procurer les demandes d'adhésion auprès de l'administratice responsible de l'adhésion à la FCF : télécopieur : 514-939-7353; Internet : www.fcf-ctf.ca; courriel : adminmtl@ctf.ca.

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Irrelevant or Even Worse? The Vicious Dilemma of the New Tax Treaty Preamble

Andrés Báez Moreno*

PRÉCIS

La thèse centrale de cet article est qu'il faut faire preuve de prudence dans l'évaluation de l'importance du nouveau préambule du modèle de convention fiscale de l'OCDE et des régimes fiscaux régis par l'instrument multilatéral dans les deux domaines où leurs partisans souhaitent voir des effets : 1) le préambule ne devrait pas avoir d'effets en soi, car il pourrait compromettre grandement l'intégrité du processus d'interprétation de la règle; 2) le préambule ne devrait pas servir de règle complémentaire au critère de l'objet principal, car cela risquerait d'amplifier la portée déjà démesurée de cette règle générale anti-évitement et, en tout état de cause, de compromettre encore davantage son interprétation.

ABSTRACT

The central thesis of this article is that the significance of the new preamble of the OECD model tax convention and the tax arrangements governed by the multilateral instrument should be evaluated with caution in the two areas where their proponents intend to see effects: (1) The preamble should not have effects on its own, since this could significantly undermine the integrity of the rule interpretation process. (2) The preamble should not serve as a complementary rule to the principal purpose test, since doing so would potentially amplify the already excessive impact of this general anti-avoidance rule and, in any case, further jeopardize its interpretation.

KEYWORDS: AVOIDANCE ■ BEPS ■ GENERAL ANTI-AVOIDANCE RULE ■ PRINCIPAL PURPOSE TEST ■ TAX TREATIES ■ TREATY SHOPPING

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CONTENTS

Introduction 2
The Alleged Autonomous Anti-Abuse Function Attributed to the New Preamble 6
An Anti-Abuse Principle with Unknown Boundaries 7
An Anti-Abuse Principle Without a Concept of Abuse 12
An Anti-Abuse Teleological Interpretation Principle Built on a Non-Existent or Contradictory Treaty Purpose 14
An Anti-Abuse Interpretation Mechanism with Unknown Objectives 18
The Alleged Complementary Function of the New Preamble in Applying the PPT 23
Linking the Teleological Prong of the PPT to the Specific Purpose of the Abused Tax Treaty Provision 24
Saving the Teleological Prong of the PPT (and the PPT Itself) by Linking It to the General Objects and Purposes of the Tax Treaty 27
The Shortcomings of Linking the Teleological Prong of the PPT to the General Objects and Purposes of Tax Treaties: Circularity, Confusion Between the Prongs of the Rule, and Excessive Reliance on Economic Substance 30
Conclusions 38

INTRODUCTION

The main focus of the base erosion and profit shifting (BEPS) action plan concerning tax treaties was on integrating a wide range of special anti-avoidance rules (SAARs) and the principal purpose test (PPT) into tax treaties. This focus might have been intended to provide alternatives to the previous practices of the Organisation for Economic Development and Co-operation (OECD)—that is, stretching the provisions of a petrified OECD model tax convention through astute and increasingly frequent interpretations in the model commentaries—or, more likely, because a multitude of new rules reaps political benefits in response to public opinion (allegedly) clamouring for changes in the structures of the so-called international tax regime. The outcomes of the BEPS plan undeniably yielded a lengthy roster of hard-law anti-avoidance measures.[1]

This is why it is so surprising that BEPS action 6, the multilateral instrument (MLI), and the new OECD model tax convention (2017)[2] devoted so much attention

1 Beyond the parts relating to definitions, scope, and final operative provisions (parts I and VII) and parts V and VI (devoted respectively to dispute resolution and arbitration) of the Organisation for Economic Co-operation and Development, Multilateral Convention To Implement Tax Treaty Related Measures To Prevent Base Erosion and Profit Shifting, released on November 24, 2016 (www.oecd.org/tax/treaties/multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beps.pdf) (herein referred to as "the MLI"), the remaining provisions of the MLI contain SAARs or general anti-avoidance rules that potentially could be integrated into covered tax treaties. Although some provisions of part II of the MLI (hybrid mismatches) may have a partially different focus, it is unequivocal that part III (treaty abuse) stands as the central core of the MLI, both in terms of quantity and significance.

2 Organisation for Economic Co-operation and Development, *Model Tax Convention on Income and on Capital: Condensed Version 2017* (Paris: OECD, November 2017) (herein referred to as "the 2017 OECD model tax convention" or "the model").

to such a seemingly ethereal change as the addition of a preamble (to the model and, above all, to the tax treaties covered by the MLI) and the modification of the model's title. Indeed, the pre-2017 versions of the OECD model tax convention[3] had the rather bland title "Convention between (State A) and (State B) with respect to taxes on income and on capital." Also, a footnote indicated that "States wishing to do so may follow the widespread practice of including in the title a reference to either the avoidance of double taxation or to both the avoidance of double taxation and the prevention of fiscal evasion." Furthermore, there was no model preamble text; a second footnote merely stated, "The Preamble of the Convention shall be drafted in accordance with the constitutional procedure of both Contracting States." Given this regulatory situation, and complying with the mandate in the 2013 BEPS action plan,[4] the BEPS action 6 final report indicated that a new title should be given to the model with the following wording: "Convention between (State A) and (State B) for the elimination of double taxation with respect to taxes on income and on capital and the prevention of tax evasion and avoidance."[5] In addition, the action 6 final report proposed a preamble for the model:

> (State A) and (State B),
>
> Desiring to further develop their economic relationship and to enhance their co-operation in tax matters,
>
> Intending to conclude a Convention for the elimination of double taxation with respect to taxes on income and on capital without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance (including through treaty-shopping arrangements aimed at obtaining reliefs provided in this Convention for the indirect benefit of residents of third States)
>
> Have agreed as follows:[6]

The conclusions of BEPS action 6 ended up reflected in (1) a change of title for the 2017 OECD model tax convention and the incorporation of the preamble above, both with the same language contained in the final report; and (2) the incorporation of the preamble above into article 6 of the MLI.

What is striking is not just the contrast between these additions of "soft" content and the BEPS project's emphasis on concrete "hard-law" SAARs and general anti-avoidance rules (GAARs). What is most intriguing is that the new preamble is the

3 At least since the publication of Organisation for Economic Co-operation and Development, Committee on Fiscal Affairs, *Draft Double Taxation Convention on Income and Capital* (Paris: OECD, 1963).

4 Which commissioned work to be carried out to clarify that tax treaties are not intended to be used to generate double non-taxation (Organisation for Economic Co-operation and Development, *Action Plan on Base Erosion and Profit Shifting* (Paris: OECD, 2013), at 19.

5 Organisation for Economic Co-operation and Development, *Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, Action 6—2015 Final Report* (Paris: OECD, 2015) (herein referred to as "BEPS action 6" or "BEPS action 6 final report"), at paragraph 72.

6 Ibid.

only content of the entire MLI that any covered tax agreement[7] must incorporate. Thanks to its design as a "reinforced" minimum standard, the last part of the preamble ("elimination of double taxation with respect to taxes on income and on capital without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance") will find its way into all covered tax agreements (CTAs).[8]

As surprising as these contrasts may be, the drive to include the new preamble (at all costs) in the post-BEPS tax treaties is not accidental. Indeed, the architects of the BEPS plan intended the new preamble to influence, in a comprehensive and transversal manner, the interpretation of all provisions within a CTA. This objective was soon explicitly articulated in the BEPS action 6 final report, whose words are worth reproducing verbatim:

> The clear statement of the intention of the signatories to a tax treaty that appears in the above preamble will be relevant to the interpretation and application of the provisions of that treaty.[9]

Not surprisingly, the interpretive effect of the new preamble has also been explicitly incorporated into both the commentaries to the 2017 OECD model tax convention[10] and the explanatory statement to the MLI.[11]

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7 Ibid. The author deliberately uses the term in article 2(1)(a) of the MLI. In other contexts of this article—less linked to the MLI—reference will be made to, simply, tax treaties.

8 Pursuant to articles 6(4) and 6(5) of the MLI, a signatory may avoid incorporating the new text of the preamble into a covered tax agreement (technically reserving it) only if the corresponding tax treaty already contains the same text. According to articles 6(3) and 6(6) of the MLI, the first part of the above-transcribed preamble (referring to the desire to further develop their economic relations and to strengthen their cooperation in tax matters) may or may not be incorporated into covered treaties depending on whether both parties to the relevant treaty so desire. In this context, the author refers to a "reinforced minimum standard" since other contents that make up the minimum standard (notably the PPT) may not be incorporated into covered tax treaties because signatories are offered other implementation options.

9 BEPS action 6, supra note 5, at paragraph 73.

10 2017 OECD model tax convention, supra note 2, introduction, at paragraph 16.2:

> Since the title and preamble form part of the context of the Convention and constitute a general statement of the object and purpose of the Convention, they should play an important role in the interpretation of the provisions of the Convention. According to the general rule of treaty interpretation contained in Article 31(1) of the Vienna Convention on the Law of Treaties, "[a] treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose."

Many other passages in the commentaries refer to the interpretive consequences of the new preamble. For example: "The Committee on Fiscal Affairs will continue to monitor the application of tax treaties in order to ensure that, as stated in the preamble of the Convention, the provisions of the Convention are not used for the purposes of tax avoidance or evasion" (ibid., introduction, at paragraph 41).

(Notes 10 and 11 are continued on the next page.)

The previous statements provide insight into the dual purpose that the proponents of the new preamble aimed to assign to it. On the one hand, it was intended to serve as a legal foundation to justify addressing alleged abuses of tax treaty provisions through a straightforward interpretation, regardless of any GAARs or SAARs ("the autonomous anti-abuse function"). On the other hand, it was meant to function as an interpretive guide to the general anti-abuse clause, known as the PPT, found in article 29(9) of the OECD model tax convention and article 7(1) of the MLI ("the complementary function of the PPT").[12] This article aims to critically examine the new preamble's role as the ultimate guarantor of tax treaty integrity (that is, the prevention of treaty abuse), questioning whether its two purported functions—

> Other States prefer to view some abuses as being abuses of the convention itself, as opposed to abuses of domestic law. These States, however, then consider that a proper construction of tax conventions allows them to disregard abusive transactions, such as those entered into with the view to obtaining unintended benefits under the provisions of these conventions. This interpretation results from the object and purpose of tax conventions as well as the obligation to interpret them in good faith (see Article 31 of the *Vienna Convention on the Law of Treaties*) [ibid., at paragraph 59 of the commentary on article 1].
>
> As explained in the footnote to the Article, Article 29 reflects the intention of the Contracting States, incorporated in the preamble of the Convention, to eliminate double taxation without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance, including through treaty shopping arrangements [ibid., at paragraph 1 of the commentary on article 29].
>
> Paragraph 9 must be read in the context of paragraphs 1 to 7 and of the rest of the Convention, including its preamble. This is particularly important for the purposes of determining the object and purpose of the relevant provisions of the Convention. . . . In that case, paragraph 9 would apply to deny that benefit because subparagraph c) of paragraph 2, when read in the context of the rest of the Convention and, in particular, its preamble, cannot be considered as having the purpose, shared by the two Contracting States, of authorising treaty-shopping transactions entered into by public companies [ibid., at paragraph 173 of the commentary on article 29].

11 Organisation for Economic Co-operation and Development, "Explanatory Statement to the Multilateral Convention to Implement Tax Treaty Related Measures To Prevent Base Erosion and Profit Shifting" (www.oecd.org/content/dam/oecd/en/topics/policy-sub-issues/beps-mli/explanatory-statement-multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beps.pdf) (herein referred to as "the explanatory statement"), at paragraph 23: "The inclusion of this statement in the preamble to the Convention is intended to clarify the intent of the Parties to ensure that Covered Tax Agreements be interpreted in line with the preamble language foreseen in Article 6(1)."

12 The dual impact of the new preamble—on the interpretation of any provision and specifically on the application of the PPT—has been generally recognized in a more or less emphatic manner by the literature: Pasquale Pistone and Nevia Čičin-Šain, "The Implementation and Lasting Effects of the Multilateral Instrument: General Report," in Michael Lang et al., eds., *The Implementation and Lasting Effects of the Multilateral Instrument* (Amsterdam: IBFD, 2021), 3-88, at 19-20 (not emphatically); and A.L. (Abigail) Kennedy, "The Effect of Article 6 MLI on Covered Tax Agreements: Fata Morgana or New Reality?" (2022) 50:4 *Intertax* 322-40, at 335-40 (https://doi.org/10.54648/taxi2022027).

namely, addressing treaty abuse without relying on SAARs or GAARs and complementing the PPT—are legally sound.

The remainder of this article is organized as follows: The next section delineates the potential autonomous anti-abuse function ascribed to the new preamble, highlighting its lack of delineated boundaries, its grounding in a non-existent natural concept of abuse, and a questionable and frequently contradictory alleged purpose of tax treaties. The third section outlines the complementary function of the PPT associated with the new preamble and criticizes the radicalization it could introduce when the PPT is applied. The final section presents the article's conclusions.

THE ALLEGED AUTONOMOUS ANTI-ABUSE FUNCTION ATTRIBUTED TO THE NEW PREAMBLE

The notion of addressing abuses of tax treaties through interpreting the relevant treaty provisions is neither novel nor a consequence of introducing the new preamble. In fact, the passage in the commentaries that most clearly reflects this approach was incorporated in 2003; it stated that some states "consider that a proper construction of tax conventions allows them to disregard abusive transactions, such as those entered into with the view to obtaining unintended benefits under the provisions of these conventions."[13]

Further, this approach aligns with a relevant school of thought in German-speaking academia called *Innentheorie*, according to which the abuse of (tax) provisions can be addressed through their proper teleological (purpose-based) interpretation,[14] rendering GAARs redundant or, at most, serving merely as a reminder for interpreters that tax treaty abuse must be tackled.[15] In essence, the new preamble adds to the

13 Paragraph 59 of the commentary on article 1 of the 2017 OECD model tax convention, supra note 2.

14 This approach, often referred to as *Innentheorie*, holds that the abuse of tax rules is resolved *from within the rules*, resorting to a teleological interpretation of the abused rules themselves. For a succinct presentation of this thesis and its contrasting approach (called the *Außentheorie*), see Klaus-Dieter Drüen, "§ 42 AO (FGO/FVG/VwZG)," in Klaus Tipke and Heinrich-Wilhelm Kruse, eds., *Tipke/Kruse AO-FGO Kommentar* (Köln: Otto-Schmidt, 2024), 1-86, at Marginal Number 9-11 (with a clear [not terminological] but conceptual inclination toward the *Außentheorie*); and Peter Fischer, "§ 42 AO," in Walter Hübschmann, Ernst Hepp, and Armin Spitaler, eds., *AO FGO Kommentar* (Köln: Otto-Schmidt, 2024), 1-200, at Marginal Number 196-202 (with a clear inclination toward the *Innentheorie*).

15 Concerning tax treaties, this viewpoint has been consistently advocated by Professor Michael Lang, who, more than any other scholar, has scrutinized and attempted to elucidate the PPT through the principles of *Innentheorie*: Michael Lang, "Die Überlegungen der OECD zur Aufnahme einer Missbrauchsvorschrift in Doppelbesteuerungsabkommen," in Elisabeth König, Eberhard Wallentin, and Werner Wiesner, eds., *Privatstiftung und Umgründungen: Gedenkschrift für Franz Helbich* (Vienna: Lexis Nexis, 2014), 3-18, at 17-18; Michael Lang, "BEPS Action 6: Introducing an Antiabuse Rule in Tax Treaties" (2014) 74:7 *Tax Notes International* 655-64, at 663-64; and particularly, Michael Lang, "The Signalling Function of Article 29(9) of the OECD Model—The 'Principal Purpose Test'" (2020) 74:4/5 *Bulletin for International Taxation* 264-68.

longstanding debate between proponents and critics of the *Innentheorie* by including within the normative framework in which the potentially abused provisions are inserted (the tax treaty) an explicit statement that this normative instrument is not intended to create opportunities for tax avoidance. As the author tries to demonstrate in this section, the new preamble has added new complications to the already abundant misconceptions surrounding the *Innentheorie*. This section analytically develops four essential criticisms of the alleged anti-abuse function of the new preamble; however, all of them boil down to one basic idea: if one starts from a solid methodological construction, particularly concerning the limits to interpretation, the new preamble should be practically irrelevant in the fight against the abuse of tax treaties. Conversely, it is necessary to assume a whole set of questionable postulates in order for interpretation to become an effective anti-abuse mechanism.

An Anti-Abuse Principle with Unknown Boundaries

The language of a provision serves as both the starting point and the boundary for its interpretation. The interpreter is constrained by the conceivable meanings attributed to those words, unable to go beyond the confines set by the actual text.[16] The attribution of a meaning to a legal text that is no longer reconcilable with that particular legal text can be no longer considered *interpretation of the law* but rather *development of tax law beyond interpretation*.[17] In legal domains like tax law, where adherence to the rule of law is notably stringent, the development of tax law beyond interpretation should be prohibited, or at least severely limited. In instances deemed potentially abusive, a correcting decision should go beyond the conceivable meanings ascribed to a legal text only if, within the framework of a GAAR, the transactions executed by the taxpayer are deemed abusive according to the particular concept of abuse expressly codified by the law.[18]

16 Arthur Meier-Hayoz, *Der Richter als Gesetzgeber: eine Besinnung auf die von den Gerichten befolgten Verfahrensgrundsätze im Beriche, der freien richterlichen Rechtsfindung gemäss Art. 1 Abs. 2 des schweizerischen Zivilgesetzbuches* (Zürich: Juris-Verlag, 1951), at 42. This insightful formulation relies on Larenz's differentiation between the literal wording of the law (*Wortlaut*) and the potential meaning(s) inherent in that wording (*Wortsinn*) (Karl Larenz and Claus-Wilhelm Canaris, *Methodenlehre der Rechtswissenschaft*, 3d ed. (Berlin: Springer, 1995), at 141-45).

17 In the author's view, this is the best translation of the German concept of *Rechtsfortbildung*. Other legal traditions use different terms to refer to this phenomenon, such as *Integración* in the Spanish-speaking legal tradition.

18 This approach can be read recently in relation to the PPT and the abuse of tax treaties in Wolfgang Schön, "The Role of 'Commercial Reasons' and 'Economic Reality' in the Principal Purpose Test Under Article 29(9) of the 2017 OECD Model," in P. Pistone, ed., *Building Global International Tax Law: Essays in Honour of Guglielmo Maisto* (Amsterdam: IBFD, 2022), 243-76, at 12.2.1. This has been the traditional position in Germany since Hensel succinctly but very illustratively formulated it: "Tax avoidance arises exactly where the art of interpretation begins to fail." (See Albert Hensel, "Zur Dogmatik des Begriffs 'Steuerumgehung,'" in *Bonner Festgabe für Ernst Zitelmann zum fünfzigjährigen Doktorjubiläum* (München-Berlin: Duncker & Humblot, 1923), 219-88, at 224.) This initial formulation was later refined, primarily by incorporating Larenz's fundamental findings, supra note 16.

The previous approach has faced significant criticism, particularly from advocates of the *Innentheorie*. However, its legal accuracy is more apparent when applied to tax treaties than it is in regard to other tax rules. Derived from article 31(1) of the VCLT,[19] general commentators have inferred that treaty rules should not be construed beyond the conceivable meaning(s) inherent in the treaty's terms. This implies that national courts and administrative authorities should refrain, when applying the treaty, from substituting these potential meaning(s) with the (purported) intentions of the contracting parties or the (stated objective) object and purpose of the treaty.[20] Tax lawyers have also endorsed this conclusion when articulating the significance of article 31(1) of the VCLT in interpreting double taxation conventions.[21] This methodological approach has significant implications. This does not mean that the object and purpose of a tax treaty (or any of its provisions), now clarified in the new

19 Vienna Convention on the Law of Treaties, signed at Vienna on May 23, 1969, 1155 UNTS 331 (herein referred to as "the VCLT") (https://treaties.un.org/doc/Publication/UNTS/Volume%201155/volume-1155-I-18232-English.pdf).

20 Frank Engelen, *Interpretation of Tax Treaties Under International Law* (Amsterdam: IBFD, 2004), at 172 (although Engelen confuses the concept and limits of purposive interpretation, in the author's opinion). See also Ulf Linderfalk, *On the Interpretation of Treaties: The Modern International Law as Expressed in the 1969 Vienna Convention on the Law of Treaties* (Dordrecht: Springer, 2007), at 203; Mark E. Villiger, *Commentary on the 1969 Vienna Convention on the Law of Treaties* (Leiden, the Netherlands: Brill, 2009), at article 31, Marginal Number 14; Mark E. Villiger, "The Rules on Interpretation: Misgivings, Misunderstandings, Miscarriage? The 'Crucible' Intended by the International Law Commission," in Enzo Cannizzaro, ed., *The Law of Treaties Beyond the Vienna Convention* (Oxford, UK: Oxford University Press, 2011), 105-22, at 110 (https://doi.org/10.1093/acprof:oso/9780199588916.003.0006); Richard K. Gardiner, *Treaty Interpretation*, 2d ed. (Oxford, UK: Oxford University Press, 2015), at 218-19; and Oliver Dörr, "Article 31: General Rule of Interpretation," in Oliver Dörr and Kirsten Schmalenbach, eds., *Vienna Convention on the Law of Treaties: A Commentary*, 2d ed. (Berlin: Springer, 2018), 557-616, at 586-87.

21 Klaus Vogel and Rainer G. Prokisch, "General Report," in International Fiscal Association, *Interpretation of Double Tax Conventions*, Cahiers de droit fiscal international, vol. 78a (The Hague: Kluwer, 1993), 55-85, at 73; Błażej Kuźniacki, "The Principal Purpose Test (PPT) in BEPS Action 6 and the MLI: Exploring Challenges Arising from Its Legal Implementation and Practical Application" (2018) 10:2 *World Tax Journal* 233-94, at 240; Werner Haslehner, "Introduction," in Eckerhart Reimer and Alexander Rust, eds., *Klaus Vogel on Double Taxation Conventions*, 5th ed. (Alphen aan den Rijn, the Netherlands: Kluwer, 2022), 1-78, at Marginal Number 99; Jan Gooijer, *Tax Treaty Residence of Entities* (Alphen aan den Rijn, the Netherlands: Kluwer Law International BV, 2019), at 75-77 (concerning the very relevant interpretation of article 4 of the 2017 OECD model tax convention, supra note 2); Stef van Weeghel, "A Deconstruction of the Principal Purposes Test" (2019) 11:1 *World Tax Journal* 3-45, at 16; Robert Danon, "The PPT in Post-BEPS Tax Treaty Law: It Is a GAAR but Just a GAAR!" (2020) 74:4/5 *Bulletin for International Taxation* 242-63, at 252-53 (regarding precisely the limits to the purposive interpretation arising from the application of the new preamble); and Kasper Dziurdź, "The Concept of the 'Object and Purpose' in Tax Treaty Law Based on the Vienna Convention (1969) and the Principal Purposes Test Rule" (2024) 78:3 *Bulletin for International Taxation* 110-26, at 115-16.

preamble, should be entirely irrelevant when addressing taxpayer strategies that involve treaty abuse. The provisions of tax treaties are occasionally articulated in significantly expansive terms or with limited connections to established concepts in (private) law, thereby leading to many possible interpretations. In such cases, some meanings may prove more suitable than others in effectively addressing the taxpayer's endeavours to engage in abuse. An interpretation of such a term that prevents abuse aligns with the intended purpose of the tax treaty or the specific provision in question. This interpretation remains within the boundaries established by article 31(1) of the VCLT by not going beyond the possible meanings of the term.[22] However, if none of the conceivable interpretations effectively addresses the abuse, the recourse lies in applying a GAAR. The GAAR functions to (exceptionally) lift the prohibition on expanding tax law beyond interpretation, as mandated by the principles of the rule of law and the specific demands of legal certainty within tax law.[23]

These theoretical discussions can be illustrated through two straightforward instances. Take the term "beneficial owner" found in articles 10, 11, and 12 of the OECD model tax convention. Its complete absence of definition and the absence of connections with concepts in the domestic laws of most jurisdictions (whether private or tax-related)[24] initially suggest the potential to select an interpretation of the term that effectively restrains specific treaty-shopping strategies devised by taxpayers.[25] Of course, the correct interpretation of this term will depend on many other variables

22 This stance was articulated a century ago in Hensel's scholarship, which differentiated between attempted avoidance (*bloßer Umgehungsversuch*) addressable through the accurate interpretation of the abused rule, and genuine avoidance (*echter Umgehungsfall*), necessitating the application of GAARs. See Hensel, supra note 18, at 245-47; and Albert Hensel, *Steuerrecht*, 3d ed. (Berlin: Julius Springer, 1933), at 99.

23 Christine Osterloh-Konrad, *Die Steuerumgehung: Eine Rechtsvergleichende und Rechtstheoretische Analyse* (Tübingen, Germany: Mohr Siebeck, 2019), at 649-55; and Schön, supra note 18, at 12.2.2 (recently applying this fundamental starting point to the role of the PPT and its relation to tax treaty interpretation).

24 According to the 2017 OECD model tax convention, supra note 2, commentaries on article 10, at paragraph 12.1; article 11, at paragraph 9.1; and article 12, at paragraph 4. Only a few common-law countries provide a specific definition—often referred to as a "narrow technical sense"—for the term "beneficial owner" in their domestic private law, particularly within the context of trust law.

25 In the same vein: Danon, supra note 21, at 253; Robert Danon, "The Beneficial Ownership Limitation in Articles 10, 11 and 12 OECD Model and Conduit Companies in Pre- and Post-BEPS Tax Treaty Policy: Do We (Still) Need It?" in Guglielmo Maisto, ed., *Current Tax Treaty Issues: 50th Anniversary of the International Tax Group* (Amsterdam: IBFD, 2020), 585-661, at 15.3.1.2 (admitting such a possible interpretation in hypothetical terms); Luc De Broe, "Role of the Preamble for the Interpretation of Old and New Tax Treaties and on the Policy of the Prevention of Treaty Abuse" (2020) 74:4/5 *Bulletin for International Taxation* 163-73, at 171, footnote 73 (more hesitant); and Dziurdź, supra note 21, at 3.4 (in similar terms to those set out here about the possible meanings of the term "beneficial owner" yet diverging in the context of the correlation between a purposive interpretation and the application of the PPT).

that may eventually lead to the rejection of its use as a broad-spectrum GAAR.[26] The specific wording of the beneficial ownership clause does not permit one to categorically dismiss an interpretation of the term that, in alignment with the preamble, effectively dismantles specific abusive treaty-shopping structures.

An opposing illustration may arise when considering the interpretation of the residence concept within the framework of tax treaties. According to the prevailing view,[27] resident status under a convention is primarily contingent on satisfying the legal criteria outlined in the domestic laws of the contracting states, under the condition that the taxpayer seeking treaty benefits is liable to tax in the respective state. This conclusion would follow, without further ado, from the wording of article 4(1) of the OECD model tax convention and OECD-patterned bilateral conventions.[28] Weak domestic residence criteria allow companies with very little substance and few material links to a given jurisdiction to gain residence for tax treaty purposes. Despite the ambiguity surrounding the notion of treaty shopping, deriving treaty benefits in such a scenario may contradict the intended purpose of tax treaties, as outlined in the new preamble. Nonetheless, attempting to limit the concept of residence to

26 The latest comprehensive examination of the concept of beneficial ownership concludes that its scope is significantly more confined than that of the PPT. It is specifically limited to particular instances of treaty shopping, such as those functionally equivalent to using agents or nominees. The study further notes that the drafters of the commentary on article 29(9) perceive beneficial ownership as playing a considerably more restricted role than the PPT (or anti-conduit regulations), rendering it almost irrelevant. See Adolfo Martín Jiménez, "Beneficial Ownership," in *Global Tax Treaty Commentaries* (Amsterdam: IBFD, 2022), at 3.3.

27 Robert Couzin, *Corporate Residence and International Taxation* (Amsterdam: IBFD, 2002), at 143; Danon, supra note 21, at 247; and Raphael Assef Lavez, "The Implications of the Supreme Court of Canada's Decision in Alta Energy Luxembourg (2021) for the OECD Principal Purpose Test" (2022) 76:6 *Bulletin for International Taxation* 308-15, at 312. This stance is likewise clearly articulated in paragraph 4 of the commentary on article 4 of the 2017 OECD model tax convention, supra note 2.

28 The author is not unaware that a small (albeit relevant) group of academic authors propose a possible different meaning for article 4(1) of the 2017 OECD model tax convention, supra note 2, according to which the reference to residence "by reason of his domicile, residence, place of management *or any other criterion of a similar nature* [emphasis added]" requires the taxpayer to have a material link to the jurisdiction in which it claims to be resident. This proposed interpretation would, in turn, exclude companies from the subjective scope of tax treaties if their residency is determined solely by the formal criteria in the domestic laws of the contracting states. Advocating this position recently as an (interpretive) way of dealing with treaty shopping: Eva Escribano, "Alternative Approaches To Address the (Yet To Be Defined) Treaty Shopping Phenomenon" (2019) 47:11 *Intertax* 938-49, at 946-47 (quoting the classic works that require domestic residence tests to ensure a material connection between the taxpayer and its residence jurisdiction in order to fulfill the "similar nature" requirement as formulated in article 4(1) of the OECD model tax convention). The author holds a dissenting view on this interpretation, the thorough exploration of which exceeds the scope of this article. Nevertheless, the primary objective here is to explain the limits of interpretation when one assumes a concept of (treaty) residence that necessarily corresponds (without any additional substantive requirements) to domestic law.

disallow the application of treaty benefits to these companies using simple interpretation seems unfeasible, given that article 4(1) does not appear to mandate a substantial connection between the taxpayer and its state of residence.[29] If deemed necessary, any such restriction must be implemented through the application of the PPT.

From this perspective, it becomes apparent that the anti-abuse interpretation advocated by the new preamble should encounter its boundary precisely where interpretive efforts reach their limit—namely, in the potential meanings of the normative expressions within the purportedly abused provisions. The commentaries to the OECD model tax convention do not explicitly address the constraints of the anti-abuse interpretation; they simply refer to article 31(1) of the VCLT.[30] This reference might be construed as an implicit acknowledgement of the limits mentioned earlier, which align with deductions drawn by internationalist and tax doctrine from that provision.

However, both the new preamble and its commentary are inserted into the pre-existing commentaries on the model, which, as explained below, appear to take a different position on the limits of interpretation. Indeed, at least two passages in the commentaries indicate that the benefits of a tax treaty could be withheld on the basis of an interpretation of the abused treaty rules, thereby overlooking the limits deriving from the possible meanings of those rules.

Paragraph 56 of the commentary on article 1 of the OECD model tax convention identifies, without further investigation and in conjunction with the new preamble text,[31] two scenarios as abusive:

1. situations in which a "person (whether or not a resident of a Contracting State), acts through a legal entity created in a State essentially to obtain treaty benefits that would not be available directly"; and
2. situations in which "an individual who has in a Contracting State both his permanent home and all his economic interests, including a substantial shareholding in a company of that State, and who, essentially in order to sell the shares and escape taxation in that State on the capital gains from the alienation (by virtue of paragraph 5 of Article 13), transfers his permanent home to the other Contracting State, where such gains are subject to little or no tax."[32]

In both cases, the commentaries point to the need to deny the application of treaty benefits because their concession would run counter to the treaty's object and purpose—specifically, the prevention of tax avoidance. Notably, these considerations

29 Gooijer, supra note 21, at 77; and Danon, supra note 21, at 253.

30 2017 OECD model tax convention, supra note 2, introduction, at paragraph 16.2.

31 This connection is made very clear in paragraph 54 of the commentary on article 1 *in fine* by stating, "As confirmed in the preamble of the Convention, it is also a part of the purposes of tax conventions to prevent tax avoidance and evasion."

32 Paragraph 56 of the commentary on article 1 of the 2017 OECD model tax convention, supra note 2.

are made without delving into an interpretation of the purportedly abused rules, which are not even mentioned,[33] and without resorting to the PPT.[34]

Paragraph 59 of the commentary on article 1 of the 2017 OECD model tax convention indicates that some states consider that a proper construction of tax conventions allows them to disregard abusive transactions; subsequently, paragraph 61 of the same commentary institutes, since 2003, the so-called guiding principle, according to which the benefits of a double taxation convention should not be available where a main purpose for entering into certain transactions or arrangements was to secure a more favourable tax position and where obtaining that more favourable treatment in these circumstances would be contrary to the object and purpose of the relevant provisions. Hence, it appears that the model commentaries acknowledge interpretation as a mechanism that enables states to address abusive transactions, irrespective of the possible meaning of the normative expressions contained in the allegedly abused provisions, and again without resorting to the PPT. This guiding principle pretends to work as a sort of unwritten GAAR,[35] in clear contradiction with all the logical and methodological principles referred to above.

In summary, while the anti-abuse interpretation stemming from the new preamble should—for methodological and, mainly, legal reasons—remain within the confines of interpretation, it is true that the commentaries, in some passages, allow for a very expansive understanding of interpretation, which the new preamble seeks to reinforce.

An Anti-Abuse Principle Without a Concept of Abuse

The new preamble fails to provide even a brief definition of the concepts it addresses, including, notably, tax avoidance and treaty shopping.[36] Therefore, the

33 As discussed in other contexts, when it comes to companies allegedly engaging in treaty shopping, the provision most susceptible to have been abused is likely article 4(1), possibly in conjunction with article 1 of the model (see Andrés Báez Moreno, "GAARs and Treaties: From the Guiding Principle to the Principal Purpose Test: What Have We Gained from BEPS Action 6?" (2017) 45:6/7 *Intertax* 432-46, at 437-38). When individuals relocate to low-tax jurisdictions, the taxpayer often relies on the tiebreaker rules outlined in article 4(2) of the model as a fundamental element of their tax planning strategy (Andrés Báez Moreno, "Cross-Border Mobility of Individuals and Anti-Avoidance Tax Rules," in Svetislav V. Kostić, Andrés Báez Moreno, Vikram Chand, and Mario Tenore, eds., *Mobility of Individuals and Workforces: Tax Challenges Raised by Digitalization* (Amsterdam: IBFD, 2024), 191-222, at 215-18).

34 In fact, these examples appear in the commentaries to the OECD model tax convention as early as 1977, 40 years before the PPT was introduced in the model.

35 Schön, supra note 18, at 12.2.2. A description of different concepts of abuse (thresholds for determining abuse) can be found in Osterloh-Konrad, supra note 23, at 651-55.

36 Claire (Xue) Peng and Joseph Schuch, "The Relevance of the Preamble for Treaty Entitlement," in Michael Lang et al., eds., *Tax Treaty Entitlement* (Amsterdam: IBFD, 2019), 1-22, at 1.3.2.3 and 1.3.2.4; Danon, supra note 25, at 15.3.1.1; and Tomás Álvarez Palacios, "The Relevance of the Preamble for Treaty Entitlement," in C. Dimitropoulou and D. Auer, eds., *Access to Treaty Benefits* (Vienna: Linde, 2021), 3-26, at 10-11.

utilization of the preamble as an interpretive tool for preventing abuse needs to rest on the notion that an inherent, overarching concept of tax treaty abuse exists. Indeed, if everything boils down to the possibility of dealing with abusive transactions in the absence of or outside SAARs or GAARs—which can indicate what is meant by abuse—there will be no choice but to understand that there is an inherent concept of abuse that transcends specific legal provisions. Nonetheless, it is evident that there is no universally accepted or inherent concept of tax treaty abuse.[37]

Although all GAARs may initially appear to adhere to a shared philosophy, significant disparities become apparent on closer examination. A clear illustration of this can be found in the varying abuse thresholds of diverse GAARs established at the global and European levels, which the BEPS initiative has directly or indirectly influenced.[38] Similarly, the approaches to abuse employed by local GAARs also yield significant disparities.[39] Therefore, constructing an anti-abuse principle of interpretation without a shared understanding of abuse by the parties to the MLI is bound to be prone to complete arbitrariness. In any case, it is bound to generate an endless series of unilateral, asymmetric, and uncoordinated responses which, it is worth remembering, were precisely what the BEPS project and the MLI were intended to eliminate.

However, again, there is an apparent disconnect between well-constructed theoretical foundations and the stances articulated in the commentaries to the OECD model tax convention. Indeed, the commentaries on article 1 not only cite instances of abusive transactions in the absence of any specific abuse test,[40] but also, as previously

37 Schön, supra note 18, at 12.2.1.

38 To illustrate this point, see the straightforward comparison of the abuse thresholds outlined in article 29(9) of the OECD model tax convention, articles 6(1) and (2) of the ATAD Directive (European Union, Council Directive 2016/1164/EU of 12 July 2016, Laying Down Rules Against Tax Avoidance Practices That Directly Affect the Functioning of the Internal Market, OJ L 193/1, July 19, 2016, Setting Out Rules Against Tax-Avoidance Practices that Directly Affect the Functioning of the Internal Market) or articles 1(2) and (3) of the Parent Subsidiary Directive (European Union, Council Directive 2011/96/EU of 30 November 2011 on the Common System of Taxation Applicable in the Case of Parent Companies and Subsidiaries of Different Member States, OJ L 345, December 29, 2011). For a more detailed comparison of, for example, the PPT and the ATAD GAAR, see Guglielmo Maisto, "Counteracting Tax Treaty Abuses from a European Perspective: Frictions and Interactions Between the OECD PPT and the ATAD GAAR," in Georg Kofler, Ruth Mason, and Alexander Rust, eds., *Thinker, Teacher, Traveler: Reimagining International Tax—Essays in Honor of H. David Rosenbloom* (Amsterdam: IBFD, 2021), 343-54.

39 While some comparative law studies have attempted to identify certain shared elements among various domestic GAARs, the prevailing reality is heterogeneity, particularly regarding the presence of tests with markedly disparate tolerances toward the abuse phenomenon. See Paulo Rosenblatt and Manuel Tron, "General Report," in International Fiscal Association, *Anti-Avoidance Measures of General Nature and Scope—GAAR and Other Rules SdU*, Cahiers de droit fiscal international, vol. 103 (The Hague: Kluwer 2018), 11-51, at 11-21.

40 Paragraph 56 of the commentary on article 1 of the 2017 OECD model tax convention, supra note 2.

mentioned, take a daring step by introducing a notion of abuse seemingly out of thin air. In essence, the purported guiding principle is a test of abuse invented by the commentaries.[41] Neither the guiding principle nor an anti-abuse interpretation attempting to maintain internal coherence by drawing on the concept of abuse inferred from the former can adequately justify why the abuse test they rely on focuses on one of the main purposes of the transaction—rather than, for instance, the main, essential, or sole purpose of the transaction or entirely non-intentional concepts such as artificiality or lack of genuineness. The commentaries also fail to acknowledge that the reference to the object and purpose of the pertinent (abused) provisions is inherent to any GAAR; GAARs based on purely non-intentional tests, particularly the artificiality of the transactions under scrutiny, do not necessitate a teleological examination of the avoided rules, let alone conceptual thresholds of abuse built on the intention of the taxpayers or the purpose of the transactions they might implement. In essence, the introduction by the commentaries of a standard of abuse[42] is the necessary tradeoff for implementing a functional anti-abuse interpretation.

An Anti-Abuse Teleological Interpretation Principle Built on a Non-Existent or Contradictory Treaty Purpose

The commentaries to the OECD model tax convention[43] and the explanatory statement to the MLI[44] support an object and purpose of tax treaties being to prevent tax avoidance in the pure text of the new preamble. This is perfectly acceptable, especially considering that international lawyers universally acknowledge treaty preambles as the natural starting point for any inquiry into the object and purpose of a treaty.[45] However, this starting point may become problematic if, taken to the extreme, it is understood that the parties to the convention may attribute to it whatever purposes they see fit, whether or not the provisions of the convention confirm

41 Paragraph 61 of the commentary on article 1 of the 2017 OECD model tax convention, ibid.

42 We use the term "paralegal standard" to imply a lack of democratic process, since the Commentaries are drafted by a select group of officials. Specifically, the guiding principle is particularly ill-considered, and the abuse test it encompasses has faced significant criticism (see Juan José Zornoza and Andrés Báez, "The 2003 Revisions to the Commentary to the OECD Model on Tax Treaties and GAARs: A Mistaken Starting Point," in Michael Lang et al., eds., *Tax Treaties: Building Bridges Between Law and Economics* (Amsterdam: IBFD, 2010), 129-60, at 153-58).

43 2017 OECD model tax convention, supra note 2, introduction, at paragraph 16.2: "Since the title and preamble form part of the context of the Convention and *constitute a general statement of the object and purpose of the Convention*, they *should play an important role in the interpretation* of the provisions of the Convention [emphasis added]."

44 Explanatory statement, supra note 11, at paragraph 23: "The inclusion of this statement in the preamble to the Convention *is intended to clarify the intent of the Parties to ensure* that Covered Tax Agreements be interpreted in line with the preamble language foreseen in Article 6(1) [emphasis added]."

45 Kennedy, supra note 12, at 323 (with an exhaustive list of references in footnote 7).

that purpose. In this context, if a tax treaty lacks robust anti-avoidance provisions, or if such provisions are of limited significance, it becomes challenging to assert that one of the treaty's purposes is to prevent abuse, even if the parties intend such a purpose. Along with certain internationalists,[46] tax lawyers have reached the same conclusion regarding the interpretive significance of the new preamble to the CTAs.[47] The implications of the preceding statement are clear: when the preamble is incorporated alongside the PPT within a CTA, it can, at most, affect the interpretation of the PPT as deemed suitable.[48] However, if the new preamble is introduced independently[49] or is meant to be retroactively applied as an interpretive guideline,[50] its impact will be minimal or non-existent without an anti-abuse provision in place. In brief, the object and purpose of a tax treaty are not simply bestowed upon it by the parties through a superficial label. Instead, they emerge as an abstract articulation of the treaty's objectives, shaped by the collective impact of its specific provisions. As argued on previous occasions,[51] while the parties are "the owners of the treaty"[52] and can accordingly determine the meaning of its terms in a binding manner, the parties can never be the owners of the underlying rationale for the treaty. No matter how unrestricted the parties may be regarding the purposes of a treaty, it is beyond their reach to declare that a provision or set of provisions pursues a purpose (that is, a general anti-abuse purpose) that it does not and cannot pursue.

46 Isabelle Buffard and Karl Zameneck, "The 'Object and Purpose' of a Treaty: An Enigma?" (1998) 3:1 *Austrian Review of International & European Law* 311-43, at 333: "A prima facie assumption of the object and purpose of a treaty must be formed by having recourse to the title, preamble and, if available, programmatic articles of the treaty. This assumption must then be tested in a second stage against the text of the treaty and all other available material and, if necessary, adjusted in the light of that test."

47 Dziurdź, supra note 21, at 2.3 (with many references in footnote 55). Professor Arnold had already expressed this view when, in 2003, the commentaries to the model incorporated the statement that the prevention of abuse is a purpose of tax treaties: Brian J. Arnold, "Tax Treaties and Tax Avoidance: The 2003 Revisions to the Commentary to the OECD Model" (2004) 58:6 *Bulletin for International Fiscal Documentation* 244-60, at 249.

48 This potential influence will be dealt with in detail under the heading "The Alleged Complementary Function of the New Preamble in Applying the PPT."

49 This scenario is improbable within the framework of the MLI, since both the preamble and the PPT constitute minimum standards. Similarly, it is implausible that it will occur during bilateral negotiations or renegotiations of tax treaties.

50 See in this regard the discussion under the heading "An Anti-Abuse Interpretation Mechanism with Unknown Objectives."

51 Andrés Báez Moreno, "Los principios y reglas de prevención del abuso: interpretación antiabuso y regla del propósito principal," in José Manuel Almudí Cid, Jorge Alberto Ferreras Gutiérrez, and Pablo Andrés Hernández González-Barreda, eds., *El tratado multilateral para aplicar las medidas relacionadas con los tratados fiscales para prevenir la erosión de las bases imponibles y el traslado de beneficios* (Pamplona: Thomson Reuters Aranzadi, 2022), 163-211, at 172.

52 This expression is commonly used in treaty jargon: see Dörr, supra note 20, at 594.

However, even if one were to recognize an abstract object and purpose of tax treaties aimed at preventing abuse, it is essential to remember that these treaties serve other objects and purposes, often mirrored in their specific provisions, which may at times conflict with one another. These include promoting the exchange of goods and services and the free movement of capital and persons by eliminating international double taxation. Faced with this problem, some scholars argue that the main objective of a tax treaty is to correct double taxation, thus suggesting that in cases where there is a conflict between this objective and others (namely, preventing tax avoidance) prioritizing relief from double taxation is paramount.[53] In simpler words, they contend that an interpretation of a tax treaty provision that stops treaty abuse but leads to double taxation cannot be considered accurate. This approach could pose challenges to the practical functioning of the new preamble, since there is a considerable possibility that an anti-abuse interpretation may lead to instances of unresolved double taxation. If GAARs (particularly the PPT) already involve a significant risk of discrepancies between the tax authorities of the contracting states stemming from the open-ended nature of their abuse test, this risk becomes even greater under a purported anti-abuse mechanism where the points of divergence may be even more pronounced. Indeed, the parties may disagree on whether the autonomous anti-abuse function of the new preamble actually constitutes an anti-abuse mechanism. And even if they do agree on this point, they may still diverge—as discussed above—on what the appropriate threshold for abuse should be. As often happens, these discrepancies will lead to instances of unrelieved double taxation. However, the logical and legal problem that the new preamble may pose in the face of contradictory objects and purposes in tax treaties is much more complex.

The commentaries to the 2017 OECD model tax convention continue to state that "[t]he *principal purpose of double taxation conventions* is to promote, *by eliminating international double taxation*, exchanges of goods and services, and the movement of capital and persons [emphasis added]."[54] However, neither the commentaries nor the

53 Luc De Broe, *International Tax Planning and Prevention of Abuse* (Amsterdam: IBFD, 2008), at 3.3.1.2.1; Joris Luts, "BEPS Action 6: Tax Treaty Abuse" (2015) 43:2 *Intertax* 122-46, at 144; Robert J. Danon, "Treaty Abuse in the Post-BEPS World: Analysis of the Policy Shift and Impact of the Principal Purpose Test for MNE Groups" (2018) 72:1 *Bulletin for International Taxation* 31-55, at 40; Vikram Chand, *The Interaction of Domestic Anti-Avoidance Rules with Tax Treaties (with Special References to the BEPS Project)* (Geneva-Zürich-Basel: Schulthess, 2018), at 195; and De Broe, supra note 25, at 172.

54 Paragraph 54 of the commentary on article 1 of the 2017 OECD model tax convention, supra note 2. The varying significance attributed to different objects and purposes of tax treaties is apparent throughout the commentaries, albeit to a somewhat lesser degree in certain sections. One such instance can be found in the introduction to the model, where the main objective of tax treaties is underscored as the avoidance of double taxation (2017 OECD model tax convention, ibid., introduction, at paragraph 15.2), while merely stressing the importance of preventing tax avoidance and evasion (at paragraph 15.6). Van Weeghel argues that the overarching purpose of tax treaties is fully captured in the first paragraph of the introduction to the 2017 OECD model tax convention (van Weeghel, supra note 21, at 16-17).

numerous authors who persist in characterizing the correction of double taxation as the *main*, *primary*, *prominent*, or *prevailing* objective of tax treaties provide any rationale to support this stance. The secondary role assigned to the prevention of tax avoidance may have been reasonable in tax treaties patterned according to the pre-2017 versions of the OECD model tax convention, where anti-avoidance provisions were largely peripheral.[55] However, persisting in relegating this purpose to a secondary position concerning tax treaties affected by the changes introduced by the MLI—which incorporate, at minimum, the PPT and often a diverse array of SAARs—simply disregards the current state of affairs. Assigning similar importance to the various objects and purposes of a tax treaty, particularly those related to correcting double taxation and preventing tax avoidance, does not resolve the issue; instead, it exacerbates it. What is the appropriate course of action when interpreting a treaty provision that encompasses two potential interpretations, one of which resolves double taxation but allows for treaty abuse, while the other prevents treaty abuse but leads to double taxation? Neither specialists in treaty law[56] nor international tax lawyers[57] have successfully resolved this issue; rather, they have simply brought attention to it.

In the author's view, this issue is inherently unsolvable within this context. When a tax treaty includes provisions that permit various conflicting general objectives and purposes to be associated with it, determining whether the correct interpretation of a provision should prioritize one of those purposes becomes a subjective and arbitrary endeavour. The fundamental mistake lies in failing to recognize that purposive interpretation must begin with *the provision's* specific purpose rather than with a generic and overarching objective, which typically results in purely arbitrary outcomes. Many experts on treaties,[58] and in particular on double taxation conventions,[59] have argued that article 31(1) of the VCLT does not require consideration of the specific purpose of the provision being interpreted, but rather of the object and purpose of the entire treaty. However, focusing on the specific purpose of the interpreted provision notably diminishes the contradictions stemming from a broader interpretation of the concept of object and purpose. Although this argument cannot be entirely discounted, it is far less probable that inherently contradictory purposes drive a specific provision of a tax treaty. It is evident that this approach to purposive interpretation significantly limits the scope for an alleged anti-abuse interpretation principle.

55 Convincingly, Arnold, supra note 47, at 248; and De Broe, supra note 53, at 3.3.1.2.1.

56 Ian Sinclair, *The Vienna Convention on the Law of Treaties*, 2d ed. (Manchester, UK: Manchester University Press, 1984), at 130; and Kennedy, supra note 12, at 329. Gardiner references a ruling by the Appellate Body at the World Trade Organization that highlights the problem but ultimately provides an unsatisfactory solution (Gardiner, supra note 20, at 216).

57 De Broe, supra note 53, at 3.3.1.2.1 (regarding alleged ancillary purposes of a treaty); and Dziurdź, supra note 21, at 2.4 (advocating for the reconciliation or prioritization of conflicting objectives and, if that is not feasible, abandoning purposive interpretation and turning to alternative methods of interpretation).

58 Dörr, supra note 20, at 585.

59 Vogel and Prokisch, supra note 21, at 72-73; and Haslehner, supra note 21, at 3.4.10.

An Anti-Abuse Interpretation Mechanism with Unknown Objectives

In the 2017 OECD model tax convention and the MLI, the new content (new title and new preamble) were incorporated contemporaneously with the PPT. The design of both the new title and preamble as a minimum standard will lead to their systematic joint incorporation into tax treaties, at least for treaties covered by the MLI.[60] In these circumstances, the question arises as to what the purpose of this new interpretive principle might be, precisely in a context where tax treaties incorporate a GAAR with as broad a spectrum as that of the PPT. There are various ways to coordinate the two measures, and since none of the documents addressing their contents have expressed a stance on their interaction, an exploration of all possible alternatives is needed:

1. *The new preamble and the PPT are identical and therefore interchangeable.* Although this idea might have some potential for addressing the problem, it is fundamentally flawed because it contains several errors. It is not clear that the two norms have the same boundaries. Although the new preamble may affect the interpretation of the PPT's objective prong, it is not necessarily the case that the concept of treaty abuse underlying the new preamble, whatever it might be, is identical to the one triggering the application of the PPT. Conversely, the consequences of an anti-abuse interpretation will not necessarily be the same as those corresponding to the PPT.[61] Two rules with different premises and legal consequences cannot be interchangeable. Besides, the complete identification of the anti-abuse interpretation with the PPT could be contrary to the rule of effectiveness, according to which any interpretation that leaves a treaty term meaningless and devoid of any effect must be rejected.[62] The requirements of this principle are particularly relevant in a case such as this, where the MLI has invested significant effort in integrating the new preamble and the PPT into all CTAs.

60 This simultaneous and extensive integration of the new preamble and the PPT is also evident in tax treaties negotiated or renegotiated outside the MLI. Among the nine tax treaties that entered into force between January 1 and May 9, 2024, eight included the preamble and the PPT with wording identical to articles 6 and 7 of the MLI (author's analysis of new tax treaties in English in the International Bureau of Fiscal Documentation database). It is presumed that a similar pattern persists for tax treaties renegotiated through the addition of a protocol.

61 As mentioned in previous work, on the basis of the wording of the PPT, it appears that in cases of rule shopping, the legal outcome would be the rejection of not only the distributive rule claimed by the taxpayer, but also any other distributive rule that could have been applicable in the absence of an abusive transaction (Báez Moreno, "GAARs and Treaties," supra note 33, at 443). This could never happen in the context of an anti-abuse interpretation, since the interpreter would typically apply the legal consequences of the circumvented rule.

62 On this interpretive principle and its particular relevance to international treaty law, see Dörr, supra note 20, at 578ff.

2. *The anti-abuse interpretation would apply only in cases where a treaty does not include the PPT.*[63] This perspective could provide a more equitable understanding of the role of the anti-abuse interpretation, which would serve as a fallback option for situations in which a treaty does not include the PPT. This legal scenario cannot be ruled out, since the BEPS action 6 final report[64] and the MLI allow parties to meet the BEPS minimum standard without using the PPT. Indeed, article 7(15)(a) of the MLI permits a party not to apply the PPT to its CTAs if it intends to use a combination of a detailed limitation-on-benefits provision (LOB) and rules to address conduit financing structures.[65] However, it is improbable for a CTA to remain unaffected by the PPT. The MLI presents the PPT as the default option,[66] and, additionally, the signatories of the MLI appear hesitant to implement the minimum standard using a combination of an LOB and anti-conduit rules.[67] The widespread rejection of this way of implementing the minimum standard of action 6 seems easy to justify. In short, this option amounted to an attempt to lure the United States into the MLI, since the United States had based its fight against treaty shopping on a combination of an LOB and domestic anti-conduit rules.[68] After the United States

63 The 2017 commentaries seem to suggest this approach by stating that when "a tax convention does not include such rules [that is, the PPT and other specific treaty anti-abuse rules] the question may arise whether the benefits of the tax convention should be granted when transactions that constitute an abuse of the provisions of that convention are entered into" and connecting this idea to the following assertion: "[Some] States . . . consider that a proper construction of tax conventions allows them to disregard abusive transactions." See paragraphs 57 and 59 of the commentary on article 1 of the 2017 OECD model tax convention, supra note 2.

64 Supra note 5, at paragraph 22.

65 Article 7(17)(a) of the MLI seems to imply that some jurisdictions could meet the minimum standard when, in the future, they adopt through bilateral negotiation an LOB provision that replaces the PPT. However, this interpretation would contradict the contents of article 7(15)(a) of the MLI. This is precisely the interpretation that the explanatory statement seems to embrace when it states that a party making a notification under article 7(17)(a) may also express its intent to adopt a simplified or detailed LOB provision to supplement paragraph 1, or to replace paragraph 1 with a detailed LOB provision supplemented by rules to address conduit financing structures (explanatory statement, supra note 11, at paragraph 115).

66 Explanatory statement, supra note 11, at paragraph 90.

67 According to the OECD database on Reservations and Choices of Optional Provisions under the MLI, no signatory to the MLI has reserved the right under article 7(15) to not apply the PPT to its CTAs on the basis that it intends to adopt a combination of a detailed LOB provision and either rules to address conduit financing structures or a PPT. See Organisation for Economic Co-operation and Development, "BEPS MLI Matching Database," under "Reservations and Choices of Optional Provisions" (www.oecd.org/tax/treaties/mli-matching-database.htm#reservations-options).

68 Robert Stack, Daniel Shah, and David Lenter, "United States," in International Fiscal Association, *Reconstructing the Treaty Network*, Cahiers de droit fiscal international, vol. 105A (The Hague: Kluwer, 2020), 873-90, at 877-79.

declined to sign the MLI,[69] it appears evident that MLI signatories are inclined to adopt the minimum standard of action 6 by integrating the PPT into their CTAs. However, a (very small) number of jurisdictions that signed the MLI have indicated an intention, in time, to adopt a detailed LOB in addition to or instead of the PPT.[70] It seems unlikely that the final report on action 6, along with MLI's extensive endeavours to integrate the new preamble into all CTAs, was premised on a highly improbable scenario—namely, MLI signatories completely opting out of the PPT.

3. *The new preamble is merely instrumental with respect to the other anti-abuse rules in the MLI, and particularly with respect to the PPT.* This idea appeared to be implied in the BEPS action 6 final report[71] and has been supported by several authors.[72] The commentaries on the 2017 OECD model tax convention have displayed a degree of ambiguity on this matter. At times, they appear to strongly advocate for the instrumental nature of the preamble in relation to conventional anti-abuse clauses.[73] However, in other instances, they

69 One of the grounds for rejecting the agreement was the consideration that, by signing, the United States would not have been able to use the MLI as a mechanism to include its preferred detailed LOB provision in treaties that currently do not have such a provision (ibid., at 885).

70 Although this is a way to meet the minimum standard that is not explicitly contemplated by the MLI, some jurisdictions (notably Canada, Chile, Colombia, Kuwait, Mauritius, Norway, Poland, Senegal, and Seychelles), perhaps following the option provided by the explanatory statement (supra note 11, at paragraph 115), have expressed this choice.

71 The BEPS action 6 final report states: "[Countries] *should also implement that common intention* [to eliminate double taxation without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance, including through treaty-shopping arrangements] *through either* the combined approach described in paragraph 19 (subject to the necessary adaptations referred to in paragraph 6 above), the inclusion of the PPT rule or the inclusion of the LOB rule supplemented by a mechanism (such as a treaty rule that might take the form of a PPT rule restricted to conduit arrangements or domestic anti-abuse rules or judicial doctrines that would achieve a similar result) that would deal with conduit arrangements not already dealt with in tax treaties." BEPS action 6, supra note 5, at paragraph 22 (emphasis added).

72 Luts, supra note 53, at 144; Luc De Broe, "Fighting Treaty Shopping After the Multilateral Instrument," in Brian J. Arnold, ed., *Tax Treaties After the BEPS Project: A Tribute to Jacques Sasseville* (Toronto: Canadian Tax Foundation, 2018), 91-107, at 95; Danon, supra note 53, at 40 (attributing this approach to the OECD); De Broe, supra note 25, at 171; Jonathan Schwarz, "The Impact of the New Preamble on the Interpretation of Old and New Treaties and on Policy of Abuse Prevention" (2020) 74:4/5 *Bulletin for International Taxation* 174-78, at 177; and Danon, supra note 21, at 251-54.

73 Paragraphs 57 and 59 of the commentary on article 1 of the 2017 OECD model tax convention, supra note 2, state:

> Where, however, a tax convention does not include such rules, the question may arise whether the benefits of the tax convention should be granted when transactions that constitute an abuse of the provisions of that convention are entered into.
>
> Other States prefer to view some abuses as being abuses of the convention itself, as opposed to abuses of domestic law. These States, however, then consider that a proper

seem to acknowledge the potential autonomous application of an anti-abuse interpretation.[74] Be that as it may, adopting the former stance notably curtails the real-world significance of the updated preamble, nullifying the envisaged dual impact mentioned earlier. The tangible fruits of establishing it as a minimum standard, along with the subsequent endeavours of the MLI to integrate it into all CTAs, would materialize only if its importance in interpreting the PPT were pivotal. Although this issue will be discussed later, numerous advocates for the strictly supplementary character of the preamble have forecasted that its importance in interpreting the PPT will be limited.[75]

4. *The new preamble seeks to retroactively apply the anti-abuse interpretation to CTAs and perhaps even beyond.* All the scenarios outlined above essentially negate the practical impact of the new preamble. This undermines its effective application and appears inconsistent with the substantial efforts invested in its successful integration into CTAs. This fourth interpretation would address the issue that affected pre-MLI versions of CTAs lacking conventional anti-abuse clauses. Simultaneously, it would confer significant effects on the new preamble. Several authors have employed diverse arguments to support this alleged retroactive effect. For instance, they contend that article 6(1) of the MLI clarifies an idea already articulated in the commentaries to article 1 of the OECD model tax convention.[76] Alternatively, in somewhat more intricate terms, it has also been argued that the new preamble might be construed as a binding agreement concerning the interpretation of a treaty, as outlined in

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construction of tax conventions allows them to disregard abusive transactions, such as those entered into with the view to obtaining unintended benefits under the provisions of these conventions. This interpretation results from the object and purpose of tax conventions as well as the obligation to interpret them in good faith.

This approach may be consistent with the one stated in point 2. It is plausible to argue that the preamble may serve as an autonomous anti-abuse measure only when anti-abuse rules are absent in a tax treaty. However, in the presence of such rules, the preamble can still play a valuable role in facilitating their interpretation.

74 In particular, the commentaries state: "That principle [the so-called guiding principle] applies independently from the provisions of paragraph 9 of Article 29, which merely confirm it" (see paragraph 60 of the commentary on article 1 of the 2017 OECD model tax convention, supra note 2, *in fine*). According to certain authors, the guiding principle can be viewed as an implied GAAR that arises from the inherent anti-abuse objective of tax treaties.

75 Schwarz, supra note 72, at 177-78; De Broe, supra note 25, at 171; Arthur Brunner and Moritz Seiler, "Implementing the Multilateral Instrument in Switzerland," in *The Implementation and Lasting Effects of the Multilateral Instrument*, supra note 12, 871-92, at 875-77.

76 Heinz Jirousek, Christiane Zöhrer, and Karol Dziwinski, "Die Auswirkungen des MLI auf das österreichische DBA-Netzwerk" (2017) 70:15-16 *Österreichische Steuerzeitung* 393-97, at 395; Heinz Jirousek, "Austria," in Cahiers de droit fiscal international, vol. 105A, supra note 68, 149-66, at 163-64. Jirousek refers to paragraph 9.4 of the commentary on article 1 of the 2017 OECD model tax convention, supra note 2.

article 31(3)(b) of the VCLT.[77] Going further, one could even argue that article 6(1) of the MLI is an interpretive rule with inherent retroactive effects.[78] If one adopted this argument, and surmounted potential challenges posed by article 28 of the VCLT,[79] the anti-abuse interpretation outlined in article 6(1) would extend its effects to the application of CTAs even before the MLI entered into force. The proponents of BEPS action 6 or those interpreting the rules derived from that action might even contemplate a more extensive expansion of the anti-abuse interpretation stemming from the new preamble. The mere inclusion of the prevention of abuse in the title of a double taxation convention (other than a CTA) could prompt the application of an independent anti-abuse interpretation.[80] A more audacious approach might be to advocate for applying these interpretive consequences to double taxation conventions that lack a preamble. This would include those whose titles, akin to all versions of the OECD model tax convention published between 1992 and 2017, contain no reference whatsoever to the purposes of the convention. Indeed, the 2017 commentaries[81] suggest that the removal of the reference to the elimination of double taxation from the title of the model in 1992 was driven by the implicit acknowledgment that these agreements could serve purposes beyond the elimination of double taxation, including, among others, the prevention of tax avoidance. In a more decisive twist, it could even be argued that all the interpretive consequences of the new preamble could also be projected onto a treaty that does not even mention the purposes of the convention in its title.

77 David W. Blum, "The Relationship Between the OECD Multilateral Instrument and Covered Tax Agreements: Multilateralism and the Interpretation of the MLI" (2018) 72:3 *Bulletin for International Taxation* 131-40, at 134.

78 With all necessary nuances, the retroactive nature of interpretive provisions has traditionally been acknowledged. On this problem, see Victor Thuronyi, Kim Brooks, and Borbala Kolozs, *Comparative Tax Law* (Alphen aan den Rijn, The Netherlands: Kluwer Law International, 2016), at 64.

79 According to von der Decken, the provision in article 28 of the VCLT stating that treaties shall not be retroactive unless a different intention appears from the treaty *or is otherwise established* pertains to situations where retroactivity arises from the inherent nature of the treaty. This includes treaties designed to interpret a preceding treaty (Kerstin von der Decken, "Article 28: Non-Retroactivity of Treaties," in *Vienna Convention on the Law of Treaties: A Commentary*, supra note 20, 505-19, at 511-12). Some authors have raised objections to this interpretation, contending that alterations to a CTA that result from the MLI could potentially affect the pre-MLI version of that treaty, invoking the prohibition of retroactivity outlined in article 28 of the VCLT (see David Duff and Daniel Gutmann, "General Report," in Cahiers de droit fiscal international, vol. 105A, supra note 68, 17-52, at 44).

80 Although only a few pre-MLI tax treaties explicitly state this purpose in their title or preamble (see Duff and Gutmann, ibid., at 22), it is crucial to note that, at least since 2003, the commentaries to article 1 have maintained that preventing tax avoidance is also an objective of tax treaties. (On these 2002 changes in the commentaries, see Arnold, supra note 47, at 247-49.)

81 2017 OECD model tax convention, supra note 2, introduction, at paragraph 16.

> This omission would somehow work as an implicit recognition that the prevention of abuse (and not only the correction of double taxation) is among the purposes of the treaty. As unconventional as it may seem, certain tax authorities have begun to propose these and similar approaches.[82] As expected, these arguments are also beginning to surface in case law.[83]

The purpose of this diversion was to underscore the challenging integration of the new preamble into tax treaties containing explicit anti-abuse provisions and the extraordinary extension of its impacts to rationalize the substantial efforts dedicated to its inclusion in all CTAs.

Taken together, the points outlined throughout this section might lead to a preliminary conclusion: the new preamble, when considered independently, should (and the author expects will) result in minimal change to the interpretation of tax treaties. Only a significant departure from the logical and legal principles of interpretation and certain basic consensuses on the appropriate way to deal with tax avoidance would enable the preamble to achieve the effects envisioned by BEPS proponents and the implementers of the MLI. Now, the question arises whether the new preamble alters anything when it is linked with the PPT. This different problem will be addressed in the following section.

THE ALLEGED COMPLEMENTARY FUNCTION OF THE NEW PREAMBLE IN APPLYING THE PPT

The PPT stipulates that even if it is demonstrated that obtaining a benefit under the convention was one of the principal purposes of the transaction under analysis, the transaction can still be deemed non-abusive and eligible for the benefits of the convention if it is shown that "granting the benefit . . . would be *in accordance with the object and purpose of the relevant provisions of this Convention* [emphasis added]." Building on this "teleological prong"[84] of the PPT, the commentaries to the OECD

82 Duff and Gutmann, supra note 79, at 47.

83 Despite its verbose argumentation and the difficulty of fully endorsing its postulates, the ruling of the Argentine Supreme Court on September 2, 2021, *Molinos Río de la Plata S.A. c/ Dirección General Impositiva* (September 2, 2021, AR: CSJN; CAF 1351/2014/CA1–CS1; CAF 1351/2014/1/RH1) seems to raise this argument precisely in relation to a tax treaty that does not even adhere to the structure or basic tenets of the OECD model tax convention. Although the defects of the ruling make it challenging to discern its precise meaning, some authors have interpreted specific passages—correctly, in the opinion of the author—as containing traces of this retroactive effect of the preamble and, in general, of the anti-abuse mechanisms whose inclusion in modern tax treaties has been promoted through the BEPS project. See in particular Adolfo Martín Jiménez, "Is There an International Minimum Standard on Tax Treaty Shopping After BEPS Action 6? Some Recent Divergent Trends" (2022) 14:3 *World Tax Journal* 451-88, at 468.

84 Essentially, Professor Schön diverges from the predominant approach of delineating two tests (subjective and objective) within the PPT. Instead, he advocates for a distinction between a teleological/normative prong and a PPT (Schön, supra note 18, at 12.2.1). This article adopts the same terminology.

model tax convention[85] and numerous scholars[86] have established a connection between the PPT and the new preamble of the CTAs: put in straightforward terms, if (1) a transaction is abusive where the benefits deriving from it are not in accordance with the object and purpose of the corresponding provisions, and (2) the preamble states that a CTA should not create opportunities for non-taxation or reduced taxation through tax evasion or avoidance (including through treaty-shopping arrangements aimed at obtaining reliefs provided in the CTA for the indirect benefit of residents of third jurisdictions), then (3) the preamble (defining a purpose of the treaty) must necessarily influence how the PPT (referring to the purpose of the abused provision) is applied.

In the author's opinion, this connection between the general purposes of the tax treaty and the application of the PPT is incorrect or should, at least, be extensively nuanced.

Linking the Teleological Prong of the PPT to the Specific Purpose of the Abused Tax Treaty Provision

A thorough examination of the teleological prong of the PPT reveals that it pertains to the specific object and purpose behind the provision of the convention that has been abused, rather than the overarching purpose of the tax treaty.[87] This approach of asking about conformity with the object and purpose of the particular treaty provision that may have been abused holds significant implications. As the author has

85 Paragraph 173 of the commentary on article 29 of the 2017 OECD model tax convention, supra note 2. Although the commentaries extensively mention the effects of the new preamble on interpretation, this is the only explicit reference the author is aware of regarding the preamble's impact on the interpretation of the PPT.

86 Kuźniacki, supra note 21, at 261-72; David G. Duff, "Tax Treaty Abuse and the Principal Purpose Test—Part 2," International Tax Planning feature (2018) 66:4 *Canadian Tax Journal* 947-1011, at 986-88; Vikram Chand, "The Principal Purpose Test in the Multilateral Convention: An In-Depth Analysis" (2018) 46:1 *Intertax* 18-44, at 25-26; Marcus Livio Gomes, "The DNA of the Principal Purpose Test in the Multilateral Instrument" (2019) 47:1 *Intertax* 66-90, at 88; Ian Zahra, "The Principal Purpose Test: A Critical Analysis of Its Substantive and Procedural Aspects—Part 1" (2019) 73:11 *Bulletin for International Taxation* 609-22, at 3.3.1; Kennedy, supra note 12, at 339-40; Schön, supra note 18, at 12.4.1; Khrystyna Franchuk, "The Assistance of Examples of the Application of the Principal Purpose Test Listed in the Commentary on Article 29(9) of the OECD Model in Establishing the Legal Certainty of the Test" (2022) 5:11 *International Tax Studies* (https://doi.org/10.59403/1rfx0ry), at 2.2.2.5; and Jinyan Li, "Finding the Purpose of Tax Treaty Provisions Under GAAR: Lessons from Alta Energy" (2022) 105:2 *Tax Notes International* 147-61, at 161.

87 Andrés Báez Moreno, "La Cláusula del Propósito Principal (Principal Purpose Test): Un Análisis Crítico de la Acción 6 del Proyecto BEPS" (November 2016) 404 *Estudios Financieros, Revista de Contabilidad y Tributación* 5-52, at 24-36; Báez Moreno, "GAARs and Treaties," supra note 33, at 436-40; Danon, supra note 53, at 45; Danon, supra note 21, at 258; De Broe, supra note 25, at 171; Ameya Mithe, "Critical Analysis of the Principal Purpose Test and the Limitation on Benefits Rule: A World Divided but It Takes Two To Tango" (2020) 12:1 *World Tax Journal* 129-65, at 150; Kennedy, supra note 12, at 339.

contended in previous work,[88] a rigorous application of the PPT to cases of treaty shopping would ensure that any transaction aligns with the intended object and purpose of the provision potentially being abused. In these instances, such provision typically pertains to the residency rule outlined in article 4 of the OECD model tax convention.[89] If we consider the objectives outlined in the commentaries regarding the concept of residence, which include establishing the personal scope of the convention and resolving cases of double taxation arising from dual residency or taxation in both the resident and source state,[90] then granting tax treaty benefits to the most insubstantial conduit would, at least at first glance, seem to align with the stated object and purpose of article 4. Furthermore, applying the objective prong of the PPT is not any simpler in instances of rule shopping. The absence of a purposive rationale behind the distribution rules in articles 6 to 22 of model-based tax treaties, beyond the essential sharing of taxation rights between two states, often makes it challenging to definitively determine whether a transaction aiming to avoid one distribution rule in favour of a more advantageous one aligns with or contradicts the object and purpose of the rule being circumvented or applied.[91]

This interpretation renders the PPT a rule with an impractical application. If strictly adhered to, it implies that no instance of treaty shopping would be deemed abusive, since even companies without any substance would fulfill the declared purposes of article 4, while cases of rule shopping could be resolved only through judgments as arbitrary as the purported purposes of the rules for the allocation of taxing rights.[92] When it comes to cases of treaty shopping, the conclusion mentioned above

88 Báez Moreno, "GAARs and Treaties," supra note 33, at 437.

89 Numerous authors contend that in treaty-shopping cases, the provision that is exploited is article 4 of the OECD model tax convention: van Weeghel, supra note 21, at 23 (adding the distributive rule of the tax treaty—in the specific case, article 10 on dividends—to which the treaty shopper has acceded); Danon, supra note 21, at 258 (in combination with the applicable distributive rule and, as the case may be, the relief provisions); Schwarz, supra note 72, at 177; and Schön, supra note 18, at 12.4.2.4.

90 Paragraph 1 of the commentary on article 4 of the 2017 OECD model tax convention, supra note 2.

91 Báez Moreno, "GAARs and Treaties," supra note 33, at 438-39. According to the author, some notable exceptions exist to this absence of logic within the distribution rules, such as specific transactions to avoid the emergence of a permanent establishment. A case in point is example J in the commentaries, which, unlike the other examples, makes at least a rudimentary reference to the object and purpose of article 5(3) of the model. Example E in the commentaries similarly draws on the object and purpose of the provision being circumvented, although the author believes that the teleological analysis in that example is simplistic and technically flawed.

92 Many authors have pointed out the considerable difficulties and unsatisfactory outcomes that stem from a strict interpretation of the objective prong of the PPT: Chand, supra note 53, at 193-94; van Weeghel, supra note 21, at 14 (while rightly pointing out that the difficulties of the teleological prong of the PPT and the guiding principle may affect tax authorities or taxpayers, depending on who bears the burden of proof); Craig Elliffe, "The Meaning of the Principal Purpose Test: One Ring To Bind Them All?" (2019) 11:1 *World Tax Journal* 47-76,

is no longer just theoretical. The ruling by the Supreme Court of Canada in the *Alta Energy* case[93] did not explicitly address the application of the PPT but rather the analogous Canadian GAAR. Nevertheless, it significantly complicates the application of GAARs that rely heavily on the purpose of the allegedly abused provisions. This intricacy is especially noticeable in tax treaties, because the court adopts a unified textual, contextual, and purposive interpretation of the specific provisions at issue to determine the abusive nature of transactions, without delving into the pursuit of overarching policies of the tax treaty.[94] Furthermore, the judgment delineates the intent of articles 1 and 4 of the OECD model tax convention by focusing on establishing the subjective scope of application of tax treaties and streamlining their straightforward and secure implementation.[95] Notably, it refrains from mandating that residency implies the presence of substantial economic ties with the intended state of residence.[96] Several authors, both within and outside Canada, have suggested that the outcome of the case would likely have remained unchanged had it pertained to a tax treaty incorporating the new preamble.[97] In essence, if Canada's GAAR, or its equivalent, the PPT, considers the object and purpose of the provisions being abused, the inclusion of a preamble referring to the general purposes of tax treaties would not significantly alter the analysis. The same opinion is held by those who, beyond the *Alta Energy* case, have argued that the preamble should exert minimal or negligible influence on interpretation of the PPT.[98]

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at 74; Danon, supra note 53, at 45; Chand, supra note 86, at 24; David G. Duff, "Canada: Tax Treaty Abuse—Alta Energy Luxembourg S.A.R.L. v. The Queen," in E. Kemmeren et al., eds., *Tax Treaty Case Law Around the Globe 2022* (Amsterdam: IBFD, 2023), 435-64, at 464 (referring to the Canadian GAAR, but in terms that can be perfectly extrapolated to the PPT).

93 *Canada v. Alta Energy Luxembourg SARL*, 2021 SCC 49.

94 Ibid., at paragraph 49.

95 Ibid., at paragraphs 42-56.

96 Ibid., at paragraphs 57-67.

97 De Broe, supra note 25, at 171; Catherine Anne Brown and Joseph Bogle, "Treaty Shopping and the New Multilateral Tax Agreement—Is It Business as Usual in Canada?" (2020) 43:1 *Dalhousie Law Journal* 1-32, at 15-18 (published before the judgment of the Supreme Court of Canada was handed down); Jiménez, supra note 83, at 464 (not emphatically though); Michael N. Kandev and John J. Lennard, "Treaty Shopping in Canada after Alta Energy Luxembourg (2021): A Closed Door Without a Lock?" (2022) 76:3 *Bulletin for International Taxation* 110-22, at 122; and Robert J. Danon, "Canada v. Alta Energy Luxembourg SARL—An Analysis Based on the Vienna Convention on the Law of Treaties," International Tax Planning feature (2023) 71:2 *Canadian Tax Journal* 543-79, at 576-78. Against this view, although with significant nuances, see Duff, supra note 92, at 464. Li, however, believes that the new preamble may mitigate the impact of the decision in other cases: Jinyan Li, "Finding the Purpose of Tax Treaty Provisions Under GAAR: Lessons from Alta Energy" (2022) 105:2 *Tax Notes International* 147-61, at 161.

98 Schwarz, supra note 72, at 177-78; and De Broe, supra note 25, at 171.

Saving the Teleological Prong of the PPT (and the PPT Itself) by Linking It to the General Objects and Purposes of the Tax Treaty

Although the interpretation described above is sound, the author foresaw, in previous work, that the practical application of the PPT would diverge significantly from that interpretation. The application of the PPT was anticipated to place significant emphasis on the overall objectives of the tax treaty. The object and purpose of the particular provision subject to abuse would be relativized, marginalized, or disregarded entirely; instead, it would be supplanted by examining the broader aims of the tax treaty—particularly, disallowing the creation of opportunities for non-taxation or reduced taxation through tax evasion or avoidance.[99] An influential minority of scholars appear to be leaning toward this approach, endeavouring to blur somewhat the distinction between the object and purpose of a specific provision and that of the tax treaty in general. They argue that virtually all provisions in a tax treaty are geared toward serving its overarching objectives. Consequently, a provision's specific object and purpose cannot be comprehended independently of the broader aims of the treaty.[100] Those in favour of not giving too much weight to the exact wording of the PPT and qualifying its scope by resorting to the general objects and purposes of tax treaties have even gone so far as to establish rules of relationship between specific and general purposes. They state, for example, that (1) taxpayers (in order to escape the application of the PPT) must show that the tax benefit is both in line with the general goals of the treaty and with the specific purpose underlying the allocation rule in issue;[101] or (2) where the text of a treaty provision does not suggest a specific rationale, its object and purpose can generally be construed in light of the object and purpose of the treaty as a whole.[102] In the author's opinion, these and other intricate interpretive suggestions[103] aim to circumvent (albeit unsuccessfully) the likelihood that a reinterpretation of the teleological prong of the PPT heavily reliant on the general objectives of tax treaties consistently results in categorizing any transaction that aims to attain treaty benefits as one of its primary purposes as abusive. This sort of mechanical connection between treaty benefits and treaty abuse becomes evident in an analysis of the teleological prong of the PPT as interpreted by the commentaries to the OECD model tax convention. This issue is briefly discussed below.

99 Báez Moreno, supra note 87, at 33-36; and Báez Moreno, "GAARs and Treaties," supra note 33, at 439-40.

100 Reinout Kok, "The Principal Purpose Test in Tax Treaties Under BEPS 6" (2016) 44:5 *Intertax* 406-12, at 409; Kuźniacki, supra note 21, at 262-72; Duff, supra note 86, at 986-92; Gomes, supra note 86, at 87-88; Schön, supra note 18, at 12.4.1; and Kennedy, supra note 12, at 340.

101 Elliffe, supra note 92, at 74; and Schön, supra note 18, at 12.4.1.

102 Duff, supra note 86, at 990; and Kennedy, supra note 12, at 340.

103 For instance, the two-stage analysis proposed by Chand, according to which the taxpayer has to first determine the object and purpose of the relevant provisions in light of the objectives pursued by a tax treaty and then prove that the transaction respects the object and purpose of the relevant provisions at stake (Chand, supra note 86, at 26).

The commentaries on the teleological prong of the PPT within the OECD model tax convention are fragmented and somewhat disjointed. Indeed, in contrast to the other normative elements in the clause, such as the concepts of "benefit," "arrangement or transaction," and "one of the principal purposes," the attention devoted in the commentary to the concept of "benefit . . . *in accordance with the object and purpose of the relevant provisions of this Convention* [emphasis added]" is considerably more limited. However, the detailed analysis of the different examples in the commentaries that interpret the PPT gives an accurate picture of the approach the OECD intends to take to the teleological prong of the PPT, in line with the way the author has been asserting as incorrect so far:

1. Paragraph 173 of the commentary on article 29(9) stands out as the sole passage that appears, at first glance, to allude in the abstract to the concept of "object and purpose of the provisions of the Convention." However, despite clarifying that article 29(9) should be interpreted within the context of paragraphs 1 to 7 and the remainder of the convention, including its preamble, its commentary is predominantly based on a strange example. The example revolves around a public company whose shares are regularly traded on a recognized stock exchange in the contracting state of which the company is a resident. The public company derives income from the other contracting state. The public company in the example is a bank that enters into a conduit financing arrangement intended to indirectly provide a resident of a third state with the benefit of lower source taxation under a tax treaty.

   The example proves oversimplified and captious.[104] Beyond this, the commentaries contain a disputable statement according to which—even where the object and purpose of article 29(2)(c) is to establish a threshold for the treaty entitlement of public companies whose shares are held by residents of different states—the provision, when read in the context of the preamble, cannot be considered as having the purpose of authorizing treaty-shopping transactions entered into by public companies. According to the author, it should be clear that the tax treaty provision acknowledging the listed bank's qualified resident status is not the one being abused.[105] In essence, no taxpayer would undergo the process of being listed on a recognized stock exchange solely to abuse the benefits of a tax treaty. However, what is crucial in this example is that the commentaries overlook the object and purpose of the provision allegedly being abused, opting instead to apply the PPT in line with the broader objects and purposes of the tax treaty.

104 Certainly, the mention in the example of a conduit financing arrangement intended to indirectly provide tax treaty benefits to a resident of a third state completely predetermines the case's result.

105 Certainly, the example attempts to navigate around the challenging issue highlighted by the author, which is that in cases of treaty shopping, the abused provisions of the tax treaty are articles 1 and 4, specifically the concept of residence they encompass.

2. Most of the examples in the commentaries that illustrate the practical application of the PPT are resolved on the basis of the general objects and purposes of the tax treaties, whether they conclude that transactions are abusive[106] or not abusive.[107] Where the commentaries conclude that obtaining tax treaty benefits is abusive, they state that it would be contrary to the object and purpose of the tax treaty to grant the benefit of that exemption or limitation under a treaty-shopping arrangement. These examples do not refer to the general object and purpose of the tax treaty (outlined in the preamble), which could potentially oppose the granting of the treaty benefit under consideration. In cases where it is determined that the PPT does not apply because the transaction is not abusive, the examples draw on the overarching goal of tax treaties of encouraging cross-border investment.[108] Finally, the commentaries provide examples where the teleological prong of the PPT is entirely omitted[109] or it is unclear whether the rule applies under the teleological prong.[110]
3. It should be acknowledged that in at least two examples in the commentaries, the potential application of the PPT hinges on the object and purpose of the provision purportedly abused.[111] Although the commentaries generally proceed in the correct direction in these cases, the analysis of the object and purpose behind the abused provisions appears to be lacking. In fact, the resolution of the cited examples appears to conflate the *purpose* of the provisions in issue with their *object* by indicating, for example, "[t]hat subparagraph [(2)(a) of article 10] uses an arbitrary threshold of 25 per cent for the purposes of determining which shareholders are entitled to the benefit of the lower rate of tax on dividends."[112] In this instance, the commentaries border on

106 Examples A and B in paragraph 182 of the commentary on article 29 of the OECD model tax convention, supra note 2.

107 Examples C, D, K, and L, ibid.

108 This approach relies on two distinct models. On the one hand, example C appears to merge the overall objects and purposes of tax treaties with those specific to its provisions by stating that, given that a general objective of tax conventions is to encourage cross-border investment, obtaining the benefits of the convention is in accordance with the object and purpose of the provisions of that convention (ibid., example C *in fine*). On the other hand, examples D, K, and L advocate an even more complex solution. The utilization of the teleological aspect of the PPT—under the general purpose of tax treaties to provide benefits to encourage cross-border investment—hinges on whether the investment made is part of an arrangement undertaken for the principal purpose of obtaining the benefit of the tax treaty (examples D, K, and L, ibid.).

109 Examples F, H, and I, ibid.

110 Examples G and M, ibid.

111 Example E, ibid., referring to the object and purpose of article 10(2)(a) of the 2017 OECD model tax convention, and example J, referring to the object and purpose of article 5(3) of the OECD model tax convention. Example I, ibid., also makes reference to the object and purpose of the relevant provisions, yet it does not specify the particular provisions involved in the given case.

112 Example E, ibid.

tautology by suggesting that a rule diminishing the maximum tax rate on dividends at source for significant holdings serves the purpose of diminishing the maximum tax rate on dividends at source for significant holdings![113] This limited line of argumentation shows, as previously noted, that the absence of a purposive rationale behind the distributive rules in articles 6 to 22 of tax treaties makes it very difficult to apply the PPT canonically to alleged rule-shopping cases without incurring serious arbitrariness.[114]

The Shortcomings of Linking the Teleological Prong of the PPT to the General Objects and Purposes of Tax Treaties: Circularity, Confusion Between the Prongs of the Rule, and Excessive Reliance on Economic Substance

There have been commendable efforts through academic works aiming to address the significant deficiencies of the PPT by linking its teleological prong with the overarching objects and purposes of tax treaties, and in particular with the newly introduced contents of the preamble. Nonetheless, the author believes that the examples provided in the commentaries and their corresponding solutions highlight the considerable challenges that such an interconnected interpretation might pose in practice:

1. Some scholars raised concerns about the circular nature of the guiding principle, which was introduced in the commentaries to the 2003 OECD model tax convention. This principle stipulates that, for a transaction to be deemed abusive, the acquisition of tax benefits associated with the transaction must

113 Although not to the extent seen in example E, example J also presents a form of tautological reasoning by stating that "granting the benefit of that rule" (article 5(3) of the model, which requires that a construction site permanent establishment must last more than 12 months) "in these circumstances" (a fragmentation of an expected 22-month-long project into different contracts each lasting 11 months) "would be contrary to the object and purpose of that paragraph, as the time limitation of that paragraph would otherwise be meaningless."

114 In the author's opinion, example E in paragraph 182 of the commentary on article 29 of the 2017 OECD model tax convention, supra note 2, implicitly acknowledges this notion by affirming that "subparagraph [(2)(a) of article 10] uses an *arbitrary threshold of 25 per cent* for the purposes of determining which shareholders are entitled to the benefit of the lower rate of tax on dividends [emphasis added]." However, in the author's opinion, this arbitrary nature of article 10(2)(a) of the model extends to nearly all rules governing the allocation of taxing rights outlined in articles 6 to 22. This generally accounts for the challenging application of teleological criteria (and, consequently, the PPT) to instances of abuse concerning allocation rules. The author contends that strategies involving the exploitation of the permanent establishment concept may constitute an exception, since this concept permits a teleological approach in a more traditional sense. On this issue, which goes far beyond the scope of this article, see Andrés Báez Moreno, "Tomando en Serio las Palabras y las Finalidades de la Ley: A Propósito del Teletrabajo y los Establecimientos Permanentes," in *Direito Tributário: Estudos em Homenagem ao Professor Luís Eduardo Schoueri* (São Paulo: NSM, 2023), 469-86, at 481-85.

contradict the objects and purposes of the relevant treaty provisions. This circularity became apparent when the teleological aspect was connected with the overarching aims of tax treaties.[115] Given its almost identical wording, similar circularity has been criticized regarding the teleological prong of the PPT.[116] Indeed, this circularity becomes apparent in the examples provided in the commentaries. In resolving some of these examples, the commentaries determine that the PPT is applicable because the allegedly abused provision cannot be considered as having the purpose of authorizing treaty-shopping transactions entered into by public companies,[117] or because it would be contrary to the object and purpose of the tax convention to grant the benefit of that exemption under that treaty-shopping arrangement.[118] Nowhere in the commentaries is there justification provided for why cases of treaty shopping are being addressed;[119] essentially, once it is established that one of the principal purposes of the arrangement was to gain treaty benefits, the deduction is made that these benefits ought to be withheld, because the arrangement is deemed abusive as a form of treaty shopping. It appears as though the commentaries regard the existence of treaty shopping as a premise rather than a conclusion. Simplified to its core, the commentaries assert something astonishingly tautologic like *we are dealing with abusive treaty shopping, and therefore the transaction is not permissible, because treaty shopping goes against the object and purpose of the tax treaty of preventing tax avoidance through treaty shopping*. In addition, as rightly pointed out,[120] examples A and B in the commentaries do not challenge the taxpayer's nexus, which would typically result in the purported treaty-shopping scenario. Instead, they address abusive transactions

115 Arnold, supra note 47, at 247 (indicating explicitly that it should be necessary for the tax authorities to establish a more specific treaty scheme or purpose that is frustrated or abused by the transaction); De Broe, supra note 53, at 3.3.1.2.3; and Brian J. Arnold and Stef van Weeghel, "The Relationship Between Tax Treaties and Domestic Anti-Abuse Measures," in Guglielmo Maisto, ed., *Tax Treaties and Domestic Law* (Amsterdam: IBFD, 2006), 81-122, at 5.4.3.

116 Luc De Broe, "Tax Treaty and the EU Law Aspects of the LOB and PPT Provision Proposed by BEPS Action 6," in Robert J. Danon, ed., *Base Erosion and Profit Shifting (BEPS)—Impact for European and International Tax Policy* (Geneva: Schulthess, 2016), 197-254, at 213; Báez Moreno, "GAARs and Treaties," supra note 33, at 440; Kuźniacki, supra note 21, at 266 (with nuances); and Schön, supra note 18, at 12.4.2.1 (referring to a particular interpretation of the teleological prong of the PPT).

117 Paragraph 173 (*in fine*) of the commentary on article 29 of the 2017 OECD model tax convention, supra note 2.

118 Examples A and B in paragraph 182 of the commentary on article 29, ibid.

119 The example in paragraph 173 of the commentary on article 29, ibid., seems deliberately constructed to create the impression of abuse by indicating that "a bank that enters into a *conduit financing* arrangement intended to provide *indirectly* to a resident of a third state the benefit of lower source taxation under a tax treaty [emphasis added]."

120 Van Weeghel, supra note 21, at 32.

falling under the realm of rule shopping. The circularity in the examples continues, with other sections in the commentaries exacerbating it. Examples D, K, and L,[121] beginning with the premise that the aim of tax treaties is to offer incentives for cross-border investment, conclude that the PPT should not be applied because the arrangement under scrutiny was not undertaken for the principal purpose of obtaining the benefits of the tax treaty. Thus, the commentaries condition the application of the teleological prong of the PPT on obtaining treaty benefits being one of the main purposes of the transaction. However, conventional logic and the typical interpretation of the rule suggest that once it has been verified that one of the main purposes of the transaction is to capture the benefits of the tax treaty, the transaction might still be deemed non-abusive if the pursuit of those benefits aligns with the teleological prong of the commentary's rationale. The argument regresses to the initial point. In theory, moreover, in these cases, the commentaries generate circular reasoning without any need for it: if it could be concluded that obtaining the benefits of the convention was not one of the main purposes of the transaction, there was no need to consider the application of the teleological prong of the PPT.[122]

2. Several authors have voiced concerns regarding certain sections of the commentary on article 29, particularly paragraph 174,[123] which suggests that any arrangement with a main objective of securing a more favourable tax treatment does not promote bona fide exchanges of goods and services and movements of capital and persons and should ultimately trigger the application of the PPT.[124] The author squarely agrees with the criticism but argues that the passage in paragraph 174 does not stem from a misinterpretation of the PPT but rather from its flawed design. It precisely reflects the problematic approach to the objective prong of the PPT based on the general objects and

121 Examples D, K, and L in paragraph 182 of the commentary on article 29 of the 2017 OECD model tax convention, supra note 2.

122 As concluded by Zahra in relation to example D: Zahra, supra note 86, at 3.3.2.3.

123 According to which,

> [t]he provisions of paragraph 9 establish that a Contracting State may deny the benefits of a tax convention where it is reasonable to conclude, having considered all the relevant facts and circumstances, that one of the principal purposes of an arrangement or transaction was for a benefit under a tax treaty to be obtained. The provision is intended to ensure that tax conventions apply in accordance with the purpose for which they were entered into, i.e. *to provide benefits in respect of bona fide exchanges of goods and services, and movements of capital and persons as opposed to arrangements whose principal objective is to secure a more favourable tax treatment* [emphasis added].

See paragraph 174 of the commentary on article 29 of the 2017 OECD model tax convention, supra note 2.

124 Peter H. Blessing, "Limitations on Treaty Access By or Through Commercial Entities," in *Current Tax Treaty Issues*, supra note 25, 237-318, at 268; and Schön, supra note 18, at 12.4.2.2.

purposes of tax treaties. Indeed, following this (perverse) logic, if the objective prong of the PPT is equated with the general objects and purposes of the tax treaty, and the preamble of the treaty explicitly rejects tax avoidance through treaty-shopping arrangements, it is plausible that a tax authority keen on eliminating any room for tax planning (and also courts lacking expertise in international tax matters) may overapply the PPT. This will mainly occur when determining whether a transaction with a treaty-shopping structure—or, more neutrally, whether an entity with residence in a contracting state that was created by a resident of a third state (without a tax treaty or with a less advantageous one)—can avail itself of the benefits in the treaty with the state where the investment is made.[125] In essence, the technical flaws of the PPT are unlikely to hinder its application. Instead, its simplistic logic favours its systematic use, creating a self-fulfilling prophecy. According to this view, any arrangement aiming to access the benefits of a tax treaty, especially where multiple states are involved, is automatically a suspected treaty-shopping arrangement. Consequently, it is deemed appropriate to invoke the PPT, since the very purpose of a tax treaty is to prevent such instances of treaty shopping from succeeding.

3. Some authors[126] have defended the rationale behind the PPT, especially its objective prong, by suggesting that an arrangement or transaction backed by a valid commercial purpose should be respected under that prong. Their argument revolves around the notion that double taxation conventions primarily aim to facilitate exchanges of goods and services and the movement of capital and individuals by eliminating international double taxation.[127] This reinterpreted understanding of the PPT language can serve as a rational framework for assessing instances of rule shopping, especially when they involve self-cancelling or mutually offsetting arrangements[128] or assessing unique cases of treaty shopping marked by so-called round-tripping strategies.[129]

125 This same pessimistic prediction can also be seen in Báez Moreno, "GAARs and Treaties," supra note 33, at 439-40.

126 Duff, supra note 86, at 992 (proposing a "genuine cross-border economic activity" regarding instances of treaty shopping); Kuźniacki, supra note 21, at 266-72, at 267 (referring to "genuine economic transactions or arrangements"); and Schön, supra note 18, at 12.4.2.4 (referring to "*bona fide* commercial reasons or economic reality").

127 This aim is reflected in the commentaries (paragraph 54 of the commentary on article 1 of the 2017 OECD model tax convention, supra note 2) and can, to some extent, be traced in the new preamble where it refers to the development of economic relationship and the "elimination of double taxation."

128 Schön, supra note 18, at 12.4.2.4 (not referring explicitly to rule-shopping cases).

129 Danon, supra note 21, at 259. Danon describes round-tripping as "structures in which income arising in one Contracting State is artificially shifted to an entity interposed in the other Contracting State and then transferred back to resident investors of the first Contracting State." Ibid., at 244.

Ultimately, this approach to the PPT's objective prong indirectly aligns with the longstanding concept of artificiality often employed by GAARs.[130] However, the complexity escalates when this approach is applied to purported instances of traditional treaty shopping involving more than two states.[131] For the PPT to effectively serve as a GAAR while safeguarding the purported function of tax treaties in fostering cross-border investment, it is crucial to acknowledge that not all cross-border investment flows merit tax treaty benefits. Given the inherently bilateral nature of the tax treaty network and its foundation on a principle of pure reciprocity, it is prudent for the PPT to discern between "good" and "bad" cross-border investments.[132] However, within the framework of the expansive interpretation of the objective prong of the PPT in the commentaries, this notion introduces a new dilemma rather than resolving the problem: What criterion should be employed to determine that a cross-border investment is "good" and thus aligns with the primary purpose of tax treaties? Asserting that "abusive" investments or those that "result in treaty shopping" are undeserving of treaty protection creates the circularity criticized above.

In this context, the sole viable option is identifying cross-border investments worthy of protection: those made by taxpayers who demonstrate sufficient substance and activity in the jurisdiction where they claim residency.[133] Yet again, the challenge lies in determining both the presence and, more importantly, the level of activity and substance required by the primary objective of a tax treaty and, consequently, when to apply the PPT. This task is far from straightforward. To address this difficulty, the most discerning commentators advocate for a legal definition of "substance." They look to other provisions of the model and the MLI, such as those attributing qualified resident status for the purposes of applying the LOB rules,[134] or to other normative materials stemming from the BEPS initiative. These approaches may include

130 At times, this concept has been suggested as a potential alternative to address the numerous challenges associated with the PPT's objective prong: Báez Moreno, "GAARs and Treaties," supra note 33, at 440.

131 These potential abuses of tax treaties are the most worrying, as evidenced by the preamble's explicit mention of "treaty-shopping arrangements aimed at obtaining reliefs provided in this Convention for the indirect benefit of residents of third States" (in this vein, see Porus F. Kaka, "From the Avoidance of Double Taxation to the Avoidance of Double Non-Taxation: The Changing Objectives of Tax Treaties" (2021) 75:11/12 *Bulletin for International Taxation* 613-17, at 613).

132 Brian J. Arnold, "An Introduction to Tax Treaties," at paragraph 46 (www.un.org/esa/ffd/wp-content/uploads/2015/10/TT_Introduction_Eng.pdf), referring in general to tax avoidance as an "inappropriate incentive to [international] commerce"; Kuźniacki, supra note 21, at 267 (following Arnold); and Schön, supra note 18, at 12.4.2.2 and 12.4.2.4.

133 Schön, supra note 18, at 12.4.2.2 and 12.4.2.4.

134 Van Weeghel, supra note 21, at 38-39; and Schön, supra note 18, at 12.4.2.2.

the modified nexus approach of BEPS action 5[135] or the new developments in transfer pricing outlined in BEPS actions 8-10.[136] Each of these comprehensive proposals encounters substantial legal challenges, the discussion of which exceeds the scope of this article.[137] However, what is most pertinent for our current focus is that the commentaries have not displayed a tendency toward this model of "systematic normativization" of the substance concept, even though there is a noticeable inclination, particularly in the PPT examples, to rely on substance to determine whether the PPT applies.[138] Certainly, the resolution of numerous examples in the commentaries demonstrates a less stringent approach that aligns with the inconsistent application of the PPT, especially its objective prong, as previously discussed. This assertion warrants further elaboration.

The analysis in the commentaries' examples of the activity and substance of taxpayers that might eventually be engaged in (unacceptable) treaty-shopping strategies is poor and very inconclusive. Primarily, the examples fail to thoroughly examine the activity and substance of the intermediate entities in the arrangements, despite some academic suggestions that imply otherwise.[139] Upon closer examination, it becomes evident that a thorough analysis of economic substance is found only in examples G,[140]

135 Danon, supra note 53, at 48-49.

136 Adolfo Martín Jiménez, "Tax Avoidance and Aggressive Tax Planning as an International Standard—BEPS and the 'New' Standards of (Legal and Illegal) Tax Avoidance," in Ana Paula Dourado, ed., *Tax Avoidance Revisited in the EU BEPS Context, 2016 EATLP Congress Munich 2-4 June 2016* (Amsterdam: IBFD, 2017), 25-62, at 55; and Danon, supra note 53, at 48, although less emphatically.

137 Van Weeghel is particularly critical of these proposals, for reasons the author shares: supra note 21, at 38-40.

138 On this heavy reliance on substance by the examples in the commentaries, see Danon, supra note 53, at 48; and Kuźniacki, supra note 21, at 267.

139 Kuźniacki, supra note 21, at 267, suggesting that examples A, B, C, D, F, G, H, I, K, L, and M in paragraph 182 of the commentary on article 29(9) analyze, positively or negatively, the economic substance and valid business reasons for the transactions described in connection with the purpose of the tax treaties to encourage cross-border business activities.

140 According to the example:

> This decision is mainly driven by the skilled labour force, reliable legal system, business friendly environment, political stability, membership of a regional grouping, sophisticated banking industry and the comprehensive double taxation treaty network of State R, including its tax treaties with the five States in which TCO owns subsidiaries, which all provide low withholding tax rates. . . . Assuming that the intra-group services to be provided by RCO, including the making of decisions necessary for the conduct of its business, constitute a real business through which RCO exercises substantive economic functions, using real assets and assuming real risks.

See example G in paragraph 182 of the commentary on article 29 of the 2017 OECD model tax convention, supra note 2.

H,[141] and K,[142] and to a lesser extent in examples L[143] and M[144] of the commentaries.[145] However, even among the limited examples that examine the activity and/or sub-

141 According to the example:

> TCO therefore establishes RCO, a subsidiary resident of State R (a country where there are developed international trade and financial markets as well as an abundance of highly-qualified human resources), as a base for developing its foreign business activities. RCO carries on diverse business activities such as wholesaling, retailing, manufacturing, financing and domestic and international investment. RCO possesses the human and financial resources (in various areas such as legal, financial, accounting, taxation, risk management, auditing and internal control) that are necessary to perform these activities. It is clear that RCO's activities constitute the active conduct of a business in State R.

See example H, ibid.

142 According to the example:

> The decision to establish the regional investment platform in State R was mainly driven by the availability of directors with knowledge of regional business practices and regulations, the existence of a skilled multilingual workforce, State R's membership of a regional grouping and the extensive tax convention network of State R, including its tax convention with State S, which provides for low withholding tax rates. RCO employs an experienced local management team to review investment recommendations from Fund and performs various other functions which, depending on the case, may include approving and monitoring investments, carrying on treasury functions, maintaining RCO's books and records, and ensuring compliance with regulatory requirements in States where it invests. The board of directors of RCO is appointed by Fund and is composed of a majority of State R resident directors with expertise in investment management, as well as members of Fund's global management team. RCO pays tax and files tax returns in State R.

See example K, ibid.

143 According to the example:

> In establishing RCO, the bank took into account a large number of issues, including State R's robust securitisation framework, its securitisation and other relevant legislation, the availability of skilled and experienced personnel and support services in State R and the existence of tax benefits provided under State R's extensive tax convention network.

See example L, ibid.

144 According to the example:

> After a review of possible locations, Real Estate Fund decided to establish RCO in State R. This decision was mainly driven by the political stability of State R, its regulatory and legal systems, lender and investor familiarity, access to appropriately qualified personnel and the extensive tax convention network of State R, including its treaties with other States within the specific geographic area targeted for investment.

See example M, ibid.

145 Example C could be included in this list, in that establishing a manufacturing plant for electronic device production assumes the presence of both activity and substance.

stance of the entities involved, such analysis is minimally beneficial in the application of the PPT to different factual scenarios.[146]

Indeed, the examples that delve deeper into substance appear tailored to support a predetermined conclusion, which consistently leans toward the non-application of the PPT. These examples are constructed using stereotypical formulas that strongly suggest the presence of significant activity and corresponding substance. Indeed, the frequent mentions of a "skilled labour force," "experienced local management," or "reliable regulatory and legal systems," just to name a few, and the cumulative convergence of all these elements of activity and substance in the examples, imply a notion of stylized substance, which inevitably leads to a predetermined conclusion. The examples provided do not explore specific aspects of the required substance, nor do they adequately address the proportion this substance should maintain in relation to the type and scale of the company's activities. Ultimately, the conclusions drawn in these examples simply state that having a skilled labour force, experienced local management, or dependable regulatory and legal systems indicates sufficient substance. This reasoning is tautological; just as it would be incorrect to claim that the absence of skilled labour, a lack of experienced local management, or the establishment of a company in jurisdictions with unstable or unreliable legal systems indicates a deficiency in economic substance.

It is also surprising (and disappointing) that none of the examples that find it necessary to apply the PPT do so by determining that the company denied treaty benefits lacks the necessary activity or substance.[147] Furthermore, and of even more concern in the context of this article, in numerous examples where the commentaries scrutinize the activity and substance of intermediate entities and determine it to be adequate, it remains unclear whether the tax benefits are granted solely as a result of applying the objective prong of the PPT or as a result of other factors. The link between the overarching objective of tax treaties to promote cross-border investment (objective prong) and the non-application of the PPT seems evident in examples C and K.[148]

146 Navarro is moderately critical of the substance-related examples in the commentaries, although he approaches them from the perspective of the (physical or digital) presence of relevant employees in the corresponding jurisdiction: Aitor Navarro, "The Incidence of Cross-Border Mobility of Individuals on Post-BEPS Substance Requirements," in Svetislav V. Kostić et al., eds., *Mobility of Individuals and Workforces: Tax Challenges Raised by Digitalization* (Amsterdam: International Bureau of Fiscal Documentation, 2024), 367-400, at 385-90.

147 As accurately pointed out by van Weeghel, example A and example B (both of which deny treaty benefits in treaty-shopping scenarios) do not question the nexus of the taxpayer with the state of residence, but rather address abusive transactions (van Weeghel, supra note 21, at 32).

148 In any event, van Weeghel's insights into the specific manner in which the overarching objectives and purposes of tax treaties should function concerning collective investment vehicles are highly relevant and may challenge the conclusion drawn in the text concerning example K (van Weeghel, supra note 21, at 35).

However, it is less apparent in examples G,[149] H,[150] L,[151] and M.[152] In this context, it becomes exceedingly challenging to derive practical conclusions regarding how the overarching objective of tax treaties to promote cross-border investment functions in regard to the PPT.

In summary, resorting to the new preamble to overcome an overly strict reading of the teleological prong of the PPT comes with its own problems. Indeed, in some cases, referring to the general purposes of the tax treaty does not facilitate the application of the PPT, and in others, it clearly leads to a circular and confusing application of the rule.

CONCLUSIONS

One of the tax treaty consequences of the BEPS project announced with the most fanfare was the incorporation of a preamble into the 2017 OECD model tax convention and all tax agreements covered by the MLI. There was a lot of hype around the rather simplistic idea that tax treaties should not facilitate their very abuse. The ideologues of BEPS and the technicians who designed the MLI invested enormous effort to ensure that the new preamble and its essential contents were incorporated into the CTAs without exception.

Despite the high expectations that some wanted to place on it, the new preamble is a smokescreen that, at best, will prove harmless. As the title of this article suggests, the new preamble may be irrelevant. However, in worse scenarios it might lead to untenable interpretations that may jeopardize the very survival of tax treaties as instruments that provide some stability and legal certainty to cross-border taxpayers.

149 Regarding example G, several authors have questioned whether the PPT's non-application results from the influence of the objective prong, either because they understand that the purposive prong of the rule is not even verified (Chand, supra note 86, at 33) or because it is unclear under which of the two tests of the rule the final decision has been taken (van Weeghel, supra note 21, at 34).

150 The commentaries resolve example H by employing the purposive prong of the PPT, although it might have been more logical to use the object and purpose of the treaty instead (van Weeghel, supra note 21, at 34-35).

151 Although initially the resolution of example L suggests that the described facts satisfy the purposive prong of the PPT, the concluding remarks of the example are somewhat enigmatic. They indicate that

> in the absence of other facts or circumstances showing that RCO's investment is part of an arrangement or relates to another transaction undertaken for a principal purpose of obtaining the benefit of the Convention, it would not be reasonable to deny the benefit of the State R-State S tax convention to RCO.

See example L in paragraph 182 of the commentary on article 29 of the 2017 OECD model tax convention, supra note 2.

152 The resolution of example M is mainly irrelevant to the objective prong of the PPT if one considers that, as indicated by the example, the taxpayer would not obtain treaty benefits that are better than the benefits to which its investors would have been entitled had they made the same investment directly (van Weeghel, supra note 21, at 37).

Indeed, the dilemma between irrelevance and irrationality faced by the new preamble is evident in the two main interpretive consequences frequently attributed to it.

Except in particular cases, resorting to the preamble as an autonomous anti-abuse mechanism implies that authorities will disregard the limits of tax treaty interpretation,[153] apply a non-existent—and therefore arbitrary—concept of treaty abuse,[154] and baselessly privilege the general purposes of tax treaties over other purposes.[155] In addition to the problems above, it is difficult to ascertain how this anti-abuse interpretation copes with the other GAARs and SAARs incorporated into CTAs, especially the PPT.[156]

The PPT is a poorly designed GAAR. Its objective prong, when interpreted strictly, can make its application impossible, particularly in cases of treaty shopping.[157] However, a more flexible application of this rule in line with the general purposes of tax treaties contained in the preamble[158] may have dire consequences. Indeed, resorting to these purposes may induce a circular, confusing, and arbitrary application of the PPT.[159]

Any legal scholar knows that an interpretation of a legal term rendering it void of content is, in principle, unacceptable. From this point of view, the central idea of this article—that the new preamble should not have any effect on the interpretation of tax treaties—should be rejected. However, this interpretive maxim cannot be taken to the extreme by forcing the relevance of the preamble, even at the expense of compromising the methodological and legal postulates that govern the interpretation of tax treaties. In tax, as in any other field of law, the application of rules implies frequently more of a weighing of evils than goods.

153 See the discussion under the heading "An Anti-Abuse Principle with Unknown Boundaries."

154 See the discussion under the heading "An Anti-Abuse Principle Without a Concept of Abuse."

155 See the discussion under the heading "An Anti-Abuse Teleological Interpretation Principle Built on a Non-Existent or Contradictory Treaty Purpose."

156 See the discussion under the heading "An Anti-Abuse Interpretation Mechanism with Unknown Objectives."

157 See the discussion under the heading "Linking the Teleological Prong of the PPT to the Specific Purpose of the Abused Tax Treaty Provision."

158 As suggested by the commentaries to the OECD model tax convention and some scholars: See the discussion under the heading "Saving the Teleological Prong of the PPT (and the PPT Itself) by Linking It to the General Objects and Purposes of the Tax Treaty."

159 See the discussion under the heading "The Shortcomings of Linking the Teleological Prong of the PPT to the General Objects and Purposes of Tax Treaties: Circularity, Confusion Between the Prongs of the Rule, and Excessive Reliance on Economic Substance."

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Policy Forum: Editors' Introduction—Tax Policy for the Environment

Public support for direct pricing of consumer carbon emissions is on the wane. Governments across Canada have acted to lower the burden on consumers of taxes on motor fuels and home heating. In the United States, the Biden administration's approach did not push carbon pricing, and the Trump administration is even less likely to do so. Perhaps the support for consumer carbon pricing will return, but in the meantime policy makers must pursue alternative ways to lower emissions. This Policy Forum addresses alternative policy measures in tax and related areas to reduce our reliance on greenhouse gas emissions.

The first article, by Nicolas Epelbaum, Patricia Jackson Farrell, Dharmesh Gandhi, and Tony Pampena, compares policies favouring electric vehicles in Canada and Norway. Policies like subsidies for low- and zero-emission vehicles are a prime feature of Canada's approach, along with regulations aiming to phase out internal combustion engines and reduce the carbon content of fuel. This article looks at demand and supply measures taken in Norway, which leads the world with 29 percent of its in-use vehicles being zero-emission. It discusses demand factors like purchasing incentives, high-occupancy vehicle lanes, subsidized charging stations, and changes to building codes to make electric vehicle ownership easier. On the supply side, it examines sales mandates, vehicle emission standards, and low-carbon fuel standards. The main conclusion is that the upfront financial incentives in Norway are pivotal, but the other measures play a supporting role.

The second article, by Jean-Philippe Meloche, Michaël Robert-Angers, and Luc Godbout, examines the potential of distance-based taxation for automobiles. The article begins with a detailed provincial-level breakdown of existing government revenue sources: fuel charges, registration fees, and road tolls. As electrification continues, generating revenue through these sources may become more difficult. Distance-based taxation presents a possible solution. Charging drivers for the kilometres they drive can potentially align better with the wear and tear vehicles cause to infrastructure. Technology (including use of global positioning systems) has advanced to a point where several jurisdictions (the Netherlands, Brussels, Oregon, and other US states) have implemented pilot projects or even permanent distance-based levies. Grappling with the technological, administrative, and privacy concerns that are raised by distance-based pricing, the article concludes that it will take time to implement—and that further reliance on fuel charges is the best path forward in the short term.

The third and fourth articles in this Policy Forum, both by Wei Cui, consider aspects of industrial carbon pricing. Pricing industrial carbon emissions seems to be less politically contentious, but the design of industrial carbon pricing requires good policy choices.

The third article considers the output-based pricing system (OBPS). In a typical OBPS, carbon pricing on emissions in an industrial facility begins when production reaches a specific benchmark. In this way, pricing at the margin still affects incentives but producers are relieved of the burden on some of their inframarginal emissions. Producers can further benefit from reducing emissions where a marketable credit is provided for reducing emissions below the benchmark. The article summarizes the rules governing each province's OBPS regime, as well as the federal OBPS regime (which applies where there is no "equivalent" provincial regime). The aim of an OBPS is typically to maintain competitiveness in export-intensive and trade-exposed industries, although the author is critical of this international competitiveness motivation. For example, electricity producers are typically subject to OBPS regimes on the basis of the size of their facilities, but electricity markets are not particularly competitive, so it is unclear how price-sensitive exports are. The article highlights important differences in the stringency of the benchmark under the various OBPS regimes, and in how the stringency tightens over time. The article ends with a discussion of how best to assess the impact of Canada's carbon-pricing strategy overall in the face of provincial OBPS regimes that vary significantly in stringency and impact.

The final article in this Policy Forum discusses a relatively new instrument, which appears to be gaining popularity as a way to combat greenhouse gas emissions: the carbon contract for difference (CCfD). CCfDs are a form of contract between a government and a private firm that essentially allows the firm to monetize its emission reductions and hedge against the risk of the government making future industrial carbon-price policy changes. For example, a CCfD could be signed under which the government agrees to purchase carbon credits (that is, credits that the government grants under an OBPS regime) with a strike price of $90 per tonne. This CCfD would pay off to the firm if the industrial carbon credit price fell below $90 per tonne. In principle, CCfDs could induce firms to make carbon-abating investments in new technologies. This article critically assesses the case for CCfDs. One argument against CCfDs is that, in the context of a complex OBPS market, price signals are noisy, and clear price signals are required for a successful CCfD market. But even if CCfDs were successful in de-risking some carbon-reduction investments, the article argues that it is odd for the government to insure private firms against future policy changes in general, and especially against one particular type of future policy change.

In summary, policy makers are responding to voters' apparent dislike of consumer carbon pricing by seeking alternatives. This Policy Forum points out some of the opportunities and challenges of alternatives to consumer carbon prices. There is no costless solution to abating carbon use, but clear thinking about alternatives can help to provide policy makers with feasible and effective options that could be more palatable to voters.

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Policy Forum: Demand and Supply Policies for Electric Vehicle Adoption—A Comparison of Norway and Canada

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PRÉCIS

Le budget fédéral canadien 2022 proposait plusieurs politiques visant à encourager à la fois la demande de véhicules électriques chez les consommateurs et l'offre de véhicules électriques de la part de l'industrie des transports afin d'atteindre ses cibles de zéro émission. Cependant, l'adoption des véhicules électriques (VE) au Canada a été lente; en 2023, seulement 2,3 pour cent des voitures en circulation étaient des VE. En revanche, la Norvège est le leader mondial en matière d'adoption des VE, avec 29 pour cent de ses véhicules en circulation qui sont des VE en 2023. Cet article examine les politiques relatives aux VE en matière d'offre et de demande dans les propositions du budget fédéral canadien 2022 et les compare aux politiques déjà en place en Norvège. Les auteurs constatent qu'au Canada, certaines politiques sont mises en œuvre au niveau provincial, mais que la modernisation du réseau et les incitations non financières doivent être coordonnées au niveau national pour accroître l'adoption des VE.

ABSTRACT

The 2022 Canadian federal budget proposed several policies to incentivize both the demand for electric vehicles among consumers and the supply of electric vehicles from the transport industry in order to reach zero-emission targets. However, Canada's electric vehicle (EV) adoption has been slow; as of 2023, only 2.3 percent of its cars in use are EVs. On the other hand, Norway is the world leader in EV adoption, with 29 percent of its vehicles in use being EVs as of 2023. This article reviews the demand-side and supply-side EV policies in the 2022 Canadian federal budget

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proposal and compares them to policies already in place in Norway. The authors find that, in Canada, certain policies are enacted at the provincial level, but further grid modernization and non-financial incentives must be coordinated at the national level to increase EV adoption.

KEYWORDS: BUDGETS ■ INCENTIVES ■ CANADA ■ NORWAY ■ AUTOMOBILES

CONTENTS

Introduction 44
Demand Factors 47
Financial Incentives 47
High-Occupancy Vehicle Lane Access 48
Public (Non-Home) Chargers and Fuelling Stations 49
EV-Ready Building Codes 49
Carbon Pricing 50
Summary of Demand Factors 50
Supply Factors 50
ZEV Sales Mandate 50
Vehicle Emissions Standards 52
Low-Carbon Fuel Standards 52
Summary of Supply Factors 53
Assessment of Policies 53
Conclusion 56

INTRODUCTION

The 2022 Canadian federal budget proposed a series of measures to help Canada on its path to achieving zero emissions and building a clean economy. Canada is already experiencing the impact of climate change with an increase in heatwaves, wildfires, and heavy storms, which will continue to accelerate if remedial actions are not taken. Some of the measures revolve around reducing carbon emissions to 40-45 percent below 2005 levels by 2030 and reaching net-zero emissions by 2050. Given that on-road transportation accounts for 20 percent of Canada's greenhouse gas (GHG) emissions, numerous measures and incentives have been proposed by the federal government to accelerate the adoption of cleaner vehicles. The federal government put in place a sales mandate to ensure that zero-emission vehicles (ZEVs)[1] will make up at least 20 percent of new light-duty vehicle sales by 2026, at least 60 percent by 2030, and 100 percent by 2035. In addition, the federal government aims to achieve

1 While the terms electric vehicle (EV) and zero-emission vehicle (ZEV) are often used interchangeably, for the purposes of this article we distinguish them based on their technical definitions and remain consistent to the underlying reference source. EVs specifically refer to vehicles that use electric energy for propulsion, while ZEVs refers to vehicles that produce no emissions from the tailpipe, regardless of how they are powered. As a result, all EVs can be ZEVs, but not all ZEVs are EVs; for example, hydrogen fuel cell vehicles are ZEVs but are not considered to be electric vehicles.

ZEV sales of 35 percent of total medium- and heavy-duty vehicle sales by 2030 and 100 percent by 2040.

To make the switch from internal combustion engine (ICE) vehicles to ZEVs more affordable, the government provided a variety of incentives to both individual and corporate consumers in its 2022 federal budget. The government will provide $1.7 billion over five years to extend the incentives for the ZEV program until March 2025, to help more Canadians purchase ZEVs. This program, which was introduced in May 2019, has helped Canadians purchase or lease over 136,000 new ZEVs by offering purchase incentives of up to $5,000 for eligible vehicles. In addition, the government announced that the Canada Infrastructure Bank will invest $500 million in large-scale urban and commercial ZEV charging and refuelling infrastructure with the aim of building a national network of electric vehicle charging stations. Finally, the federal government will provide $547.5 million to Transport Canada over four years to launch a new purchase incentive program for medium- and heavy-duty ZEVs to help businesses upgrade their fleets.

Broadly, and consistent with Melton et al.,[2] the ZEV policies in the 2022 federal budget can be categorized into two groups: demand-focused policies and supply-focused policies. Demand-focused policies are primarily aimed at consumers and include policies such as purchase subsidies and the deployment of public charging infrastructure. Supply-focused policies are aimed primarily at the automotive industry and include ZEV sales mandates and vehicle emissions standards. Not surprisingly, governments across the world have developed different policy schemes to encourage the adoption of ZEVs. Norway has been so successful in their policies that, as of 2023, 29 percent of its vehicles are electric vehicles (EVs).[3] Norway's success is remarkable, considering that it leads other nations such as Sweden (11 percent) and the Netherlands (8.3 percent) by ample margins in the proportion of vehicles that are EVs. Norway's success has been largely propelled by its high level of EV sales. Since 2020, EV sales as a percentage of total vehicles sold has consistently been greater than 75 percent, reaching 93 percent in 2023.[4] On the other hand, Canada's EV adoption has been slow, with EV sales representing just 13 percent of total vehicles sold in 2023.[5] As of 2023, only 2.3 percent of Canada's cars in use are ZEVs.[6] Figure 1

2 Noel Melton, Jonn Axsen, and Barbar Moawad, "Which Plug-in Electric Vehicle Policies Are Best? A Multi-Criteria Evaluation Framework Applied to Canada" (June 2020) 64 *Energy Research & Social Science* (https://doi.org/10.1016/j.erss.2019.101411).

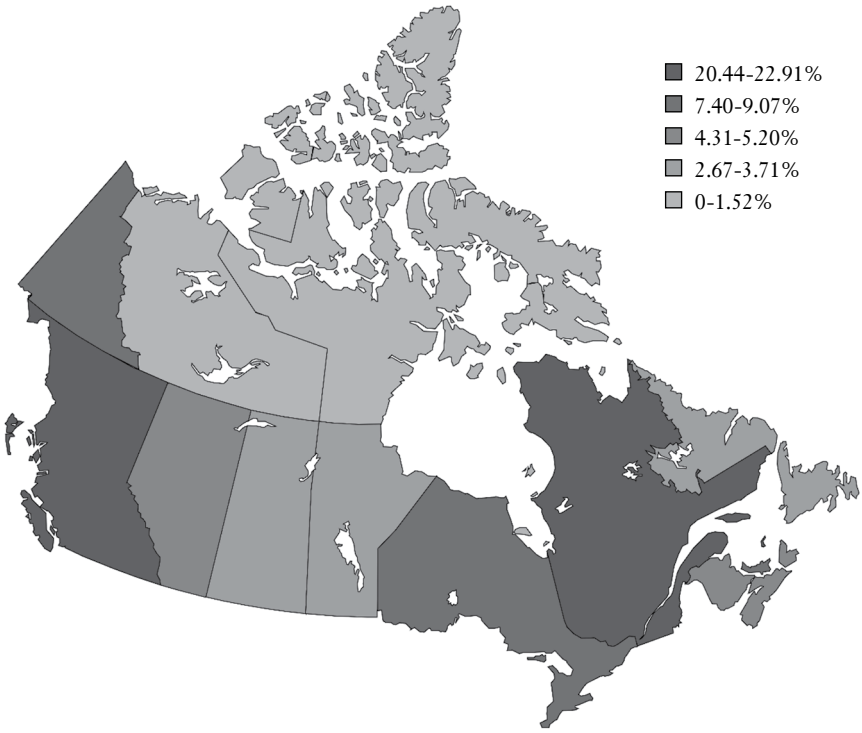
3 International Energy Agency: Norway (www.iea.org/data-and-statistics/data-tools/global-ev-data-explorer).

4 International Energy Agency, "Global EV Data Explorer," under Historical tab: EV sales share, cars, Norway 2011-2023 (www.iea.org/data-and-statistics/data-tools/global-ev-data-explorer).

5 International Energy Agency, "Global EV Data Explorer," under Historical tab: EV sales share, cars, Canada 2011-2023 (www.iea.org/data-and-statistics/data-tools/global-ev-data-explorer).

6 International Energy Agency, "Global EV Data Explorer," for Canada (www.iea.org/data-and-statistics/data-tools/global-ev-data-explorer).

FIGURE 1 Market Share of Zero-Emission New Vehicle Registrations by Canadian Province in 2023 (Q4)



shows a map with the market share of ZEV new vehicle registrations by Canadian province in 2023.[7] The map highlights that (with the exception of British Columbia and Quebec) less than 10 percent of new vehicle registrations in each of the Canadian provinces are ZEVs.

In this article, we compare how the five demand-focused policies and the three supply-focused policies proposed by Melton et al. are being applied in Norway and Canada. Given that Norway is a worldwide leader in ZEV adoption, our aim is to provide Canada with useful lessons from Norway. In the first section, we discuss how the five demand-focused policies are applied in Norway and Canada. In the second section, we assess how the three supply-focused policies are applied in Norway and Canada. In the third section, we provide an assessment of the policies reviewed, with

7 Transport Canada, "Canada's Zero-Emission Vehicle Sales Targets" (https://tc.canada.ca/en/road-transportation/innovative-technologies/zero-emission-vehicles/canada-s-zero-emission-vehicle-sales-targets) analysis of data acquired from S & P Global Mobility, "Automotive Insights—Q4 2023 Canadian EV Information and Analysis," February 28, 2024 (www.spglobal.com/mobility/en/research-analysis/automotive-insights-q4-2023-canadian-ev-information-and-analys.html).

the objective of providing policy makers with actionable suggestions to increase the adoption of EVs among individual consumers in Canada.

DEMAND FACTORS

Consistent with Melton et al., demand ZEV policies are primarily aimed at consumers, with the goal of increasing adoption. These demand-focused policies can be broadly categorized into the following five categories:

1. financial incentives,
2. high-occupancy vehicle (HOV) lane access,
3. public (non-home) chargers/fuelling stations,
4. electric-vehicle-ready building codes, and
5. carbon pricing.

Financial Incentives

Depending on the jurisdiction, financial incentives include point-of-sale incentives, rebate programs, tax exemptions, and tax credits. This type of policy is popular and has been implemented in many US states, several European countries, and Canada.[8]

Norway has introduced a variety of consumer incentives to stimulate uptake of ZEVs. ZEVs are exempt from the registration tax (a tax based on emissions, engine power, and weight), value-added tax (VAT) (a 25 percent tax on the sale price minus the registration tax), and motor fuel taxes. Furthermore, ZEVs receive at least a 50 percent reduction in road taxes, as well as ferry and parking fees.[9] In addition, tax incentives include a progressive tax on vehicles, on the basis of their weight and emissions, which makes ZEVs more economical for consumers compared with ICE vehicles.[10] Together, these incentives have made Norway's ZEV financial incentive policy the strongest in the world. The net value of Norway's incentives (including disincentives on ICE vehicles) exceed Cdn$30,000 per ZEV.[11]

Canada established the Incentives for Zero-Emission Vehicles (iZEV) program, which is a federal financial incentive program for the purchase of qualifying new battery electric, fuel cell electric, and plug-in hybrid electric automobiles.[12] The incentive provides eligible consumers with an incentive of up to $5,000, depending on the model of the vehicle and the size or capacity of its battery.[13] In addition to the

8 Melton et al., supra note 2.

9 Organisation for Economic Co-operation and Development, "Norway's Evolving Incentives for Zero-Emission Vehicles" (www.oecd.org/en/publications/2021/09/ipac-policies-in-practice_1a65968e/norway-s-evolving-incentives-for-zero-emission-vehicles_c74c1e9d.html).

10 Internation Energy Agency (www.iea.org/policies/17809-norways-electric-vehicle-incentives).

11 Melton et al., supra note 2.

12 Transport Canada, Incentives for Zero-Emission Vehicles (iZEV) Program, Questions and Answers (https://tc.canada.ca/en/road-transportation/innovative-technologies/zero-emission-vehicles/incentives-zero-emission-vehicles/questions-answers).

13 Ibid.

federal program, there are financial incentives at the provincial level. As of 2024, these incentives range from up to $3,000 in the province of Nova Scotia (EVAssist Nova Scotia) to up to $7,000 in the province of Quebec (Roulez vert) and up to $7,500 in the Northwest Territories (Arctic Energy Alliance).[14] Access to these programs requires only an application form, with no taxable income threshold or preapproval required. This makes the incentives low risk and accessible to all residents of the applicable province.

Somewhat offsetting these financial incentives, the government of Canada recently implemented a 100 percent surtax on all Chinese-made EVs, effective October 1, 2024, following similar actions by the United States and the European Union.[15] Canada's tariffs will have an immediate impact on EV manufacturers such as Tesla and Polestar, which currently sell Chinese-made EVs in Canada. It is anticipated that the new tariffs will result in fewer affordable EVs for Canadians, less competition, and more climate pollution.[16] On the other hand, the Norwegian government has decided that it will not follow the European Union, and thus will not establish tariffs for Chinese-made EVs.[17]

High-Occupancy Vehicle Lane Access

During periods of higher traffic congestion, high-occupancy vehicle (HOV) lanes enable drivers to travel faster. However, these lanes are available only to vehicles occupied by at least one passenger in addition to the driver. Providing access to HOV lanes to drivers of ZEVs, regardless of occupancy, creates an incentive for consumers to purchase and drive ZEVs. HOV lane access is a popular policy used in several regions of North America and Europe.[18] In Norway, drivers not only have access to HOV

14 Government of Nova Scotia, "Electric Vehicle Rebate Program Applications Open," *News Release*, March 12, 2021 (https://news.novascotia.ca/en/2021/03/12/electric-vehicle-rebate-program-applications-open); Gouvernement du Québec, "Financial Assistance for a New Electric Vehicle" (www.quebec.ca/en/transports/electric-transportation/financial-assistance-electric-vehicle/new-vehicle).

15 Canada, Department of Finance, "Backgrounder: Surtax on Chinese-Made Electric Vehicles" (www.canada.ca/en/department-finance/news/2024/08/surtax-on-chinese-made-electric-vehicles.html).

16 Clean Energy Canada, "Canada's Approach to EV Tariffs Undermines Affordability and Our Climate," *Media Release*, August 26, 2024 (https://cleanenergycanada.org/canadas-approach-to-ev-tariffs-undermines-affordability-and-our-climate).

17 Bloomberg, "EV Leader Norway Won't Follow EU on Chinese Electric Car Tariffs" (www.bloomberg.com/news/articles/2024-06-12/ev-leader-norway-won-t-follow-eu-on-chinese-electric-car-tariffs).

18 Lingzhi Jin, Stephanie Searle, and Nic Lutsey, *Evaluation of State-Level U.S. Electric Vehicle Incentives* (Washington, DC: International Council on Clean Transportation, 2014); Uwe Tietge, Peter Mock, Nic Lutsey, and Alex Campestrini, *Comparison of Leading Electric Vehicle Policy and Deployment in Europe* (Washington, DC: International Council on Clean Transportation, 2016).

lanes but also are exempt from toll road charges. They also get free public parking[19] and access to bus lanes.[20] On the other hand, in Canada, HOV lane access is available to ZEVs in only three provinces: British Columbia,[21] Quebec,[22] and Ontario.[23]

Public (Non-Home) Chargers and Fuelling Stations

A broad network of charging infrastructure encourages consumers' adoption of EVs.[24] Recently, Norway's EV charging infrastructure has grown exponentially to match the elevated levels of EV adoption. As of 2022, more than 22,000 public chargers had been installed in Norway.[25] Conversely, Canada had just under 12,500 public charging stations as of August 2024.[26] Canada is approximately 24 times larger than Norway, with an area of 8,788,700 km^2 versus Norway's 364,270 km^2.[27] This results in 60.4 public chargers per 1,000 km^2 in Norway versus 1.4 public chargers per 1,000 km^2 in Canada. Clearly, Norway's public charging network is substantially more dense and extensive than Canada's.

EV-Ready Building Codes

Governments can improve consumer access to home charging by requiring that residential buildings install chargers. Building code improvements have already been enacted in three Canadian provinces (Ontario, Quebec, and British Columbia), the European Union, and Norway (through its membership in the European Economic

19 Lorenc Malka et al., "Energy System Analysis with a Focus on Future Energy Demand Projections: The Case of Norway" (June 2023) 272 *Energy* (https://doi.org/10.1016/j.energy.2023.127107).

20 Erik Figenbaum, "Perspectives on Norway's Supercharged Electric Vehicle Policy" (December 2017) 25 *Environmental Innovation and Societal Transitions* 14-34.

21 Government of British Columbia, "Apply for Electric Vehicles in HOV Lanes on B.C. Highways" (www2.gov.bc.ca/gov/content/transportation/driving-and-cycling/traveller-information/routes-and-driving-conditions/hov-lanes/electric).

22 Société de l'assurance automobile du Québec, "Registering a Vehicle" (https://saaq.gouv.qc.ca/en/vehicle-registration/registering-vehicle/electric-plug-in-hybrid-hydrogen-vehicle).

23 Government of Ontario, "Get a Green Licence Plate" (www.ontario.ca/page/get-green-licence-plate).

24 Melton et al., supra note 2.

25 Márton Békés et al., "What Norway's Experience Reveals About the EV Charging Market," *McKinsey and Company*, May 8, 2023 (www.mckinsey.com/industries/automotive-and-assembly/our-insights/what-norways-experience-reveals-about-the-ev-charging-market).

26 Canada, Natural Resources Canada, "Electric Charging and Alternative Fuelling Stations Locator" (https://natural-resources.canada.ca/energy-efficiency/transportation-alternative-fuels/electric-charging-alternative-fuelling-stationslocator-map/20487#/find/nearest?country=CA).

27 Our World in Data, "Land Area in Square Kilometres" (https://ourworldindata.org/grapher/land-area-km?tab=table).

Area).[28] Given that most charging done by EV owners happens at home and at work, this is a crucial policy to accelerate EV adoption.[29]

Carbon Pricing

Carbon-pricing schemes put a price on carbon, which increases the cost of fossil fuels relative to low-carbon electricity. This increases the cost savings on fuel associated with owning and driving a ZEV.[30] Assessing carbon-pricing schemes is beyond the scope of this article, but we note that both Norway and Canada have prominent carbon-pricing schemes.[31]

Summary of Demand Factors

Among the demand-focused ZEV policies that we have assessed, the 2022 Canadian federal budget includes two main components: an extension of the iZEV program until March 2025, which provides eligible consumers with an incentive of up to $5,000, and an extension to the national network of EV charging stations.

In table 1, we summarize how the demand policies compare between Norway and Canada, noting that in all categories Norway leads by ample margins.

SUPPLY FACTORS

Consistent with Melton et al.,[32] supply ZEV policies are primarily aimed at the automotive industry, with the goal of increasing EV production. These supply-focused policies can be broadly categorized into the following three categories:

1. ZEV sales mandate,
2. vehicle emissions standards, and
3. low-carbon fuel standards (LCFS).

ZEV Sales Mandate

A ZEV sales mandate requires that ZEVs account for a minimum percentage of an automaker's overall sales in a given region.[33] In Norway, the government plans to sell only ZEVs by 2025, according to its transportation plan.[34] The state of California

28 Melton et al., supra note 2.

29 Sikandar Abdul Qadir et al., "Navigating the Complex Realities of Electric Vehicle Adoption: A Comprehensive Study of Government Strategies, Policies, and Incentives" (May 2024) 53 *Energy Strategy Reviews* (https://doi.org/10.1016/j.esr.2024.101379).

30 Melton et al., supra note 2.

31 World Bank Group, "State and Trends of Carbon Pricing Dashboard" (https://carbonpricingdashboard.worldbank.org).

32 Melton et al., supra note 2.

33 Ibid.

34 Norsk elbilforening, "Norwegian EV Market" (https://elbil.no/english/norwegian-ev-market).

TABLE 1 Summary of Demand Policies for Norway and Canada

Demand policy	Norway	Canada	Country offering higher benefit
Financial incentives	Cdn$30,000	Up to Cdn$5,000 federally, plus some provincial incentives	Norway
High-occupancy vehicle lane access	Nationally	Only in British Columbia, Ontario, and Quebec	Norway
Public (non-home) chargers/fuelling stations	60.4 per 1,000 km^2	1.4 per 1,000 km^2	Norway
Electric-vehicle ready building codes	Nationally	Only in British Columbia, Ontario, and Quebec	Norway
Carbon pricing	Both countries have a carbon-pricing scheme.		

is also a world leader in the adoption of ZEVs; it has had ZEV rules in place since 1990. California significantly strengthened its ZEV sales requirements in 2022, aiming for 100 percent of new car sales to be ZEVs by 2035. Nine other US states have adopted the California ZEV regulations.[35] Both Norway and California are making significant advances in reducing emissions; Norway's targets are more aggressive in the short term, while California has a broader long-term strategy.

Within Canada, ZEV sales regulations are already in place in Quebec and British Columbia, which represent roughly 35 percent of the nation's new light-duty vehicle market. Canada's 2022 federal budget proposed a national sales mandate applicable to all companies that manufacture in Canada or import into Canada, ensuring that at least 20 percent of new light-duty vehicle sales are ZEVs by 2026, at least 60 percent by 2030, and 100 percent by 2035. Canada's regulations are similar to those of California, the other nine US states, and China in their scope, their definition of ZEVs, and their partial credits available for plug-in hybrid electric vehicles, depending on their electric-only range.[36]

35 Environment and Climate Change Canada, "Proposed Regulated Sales Targets for Zero-Emission Vehicles" (www.canada.ca/en/environment-climate-change/news/2022/12/proposed-regulated-sales-targets-for-zero-emission-vehicles.html). Ten American states have adopted the California ZEV regulations: California, Connecticut, Maine, Maryland, Massachusetts, New Jersey, New York, Oregon, Rhode Island, and Vermont. By 2026, Colorado, Minnesota, Nevada, New Mexico, Virginia, and Washington will also adopt these regulations.

36 Melton et al., supra note 2.

Vehicle Emissions Standards

Vehicle emissions standards require that a manufacturer's fleet of vehicles not exceed a certain level of average emissions, based on the rated fuel economy of vehicles sold.[37] On December 12, 2015, Canada and 194 other countries reached the Paris Agreement to address climate change. As part of this agreement, Canada committed to reducing net GHG emissions to 30 percent below 2005 levels by 2030. The combined emissions standard required for cars and light trucks in 2025 is 119 g CO_2/km, strengthening to 71 g CO_2/km by 2040. However, despite improvements in fuel efficiency, emissions from road transportation in Canada have increased by 18 percent from 2005 to 2019 because of an increase in passenger and freight activity and a shift towards larger vehicles like SUVs and light trucks.[38] In 2020, the top 10 GHG emitters worldwide were China, the United States, India, the European Union, Russia, Indonesia, Brazil, Japan, Iran, and Canada. Together, these countries represent approximately 67 percent of total global GHG emissions in 2020.[39]

By contrast, in Norway, the vehicle emissions goal was 85 g CO_2/km by 2020, a more ambitious target than the EU threshold of 95 g CO_2/km.[40] Carbon emissions from road traffic in Norway had dropped by about 15 percent in 2021 from their peak in 2015 as biofuel use increased and the proportion of ZEVs rose.[41]

Low-Carbon Fuel Standards

Low-carbon fuel standards (LCFS) require fuel suppliers to reduce their lifecycle GHG intensity, which is the amount of pollution from their fuels, thereby decreasing GHG emissions. Such standards have been implemented in California and British Columbia.[42] California was the first to implement LCFS in 2007, with the aim of reducing the carbon intensity of its transportation fuels by at least 20 percent by 2030. Canada's 2021 federal budget invested $1.5 billion over five years to establish a Clean Fuels Fund, including clean fuel regulations that require liquid fossil fuel

37 Ibid.

38 Transport Canada, *Transportation in Canada 2021: Comprehensive Report* (Ottawa: Transport Canada, 2021), at 41, under the heading "Greenhouse Gas Emissions."

39 United States Environmental Protection Agency, "Global Greenhouse Gas Overview" (www.epa.gov/ghgemissions/global-greenhouse-gas-overview). Data includes CO_2, CH_4, N_2O, and fluorinated gas emissions from energy, agriculture, forestry and land use change, industry, and waste.

40 Guillaume Simonet, *Norway Transport: The Progressive Electrification of Land and Maritime Transport* (Paris: Climate Chance, 2019) (www.climate-chance.org/wp-content/uploads/2019/11/cp4-2019_transport-norway-vf-en_20191126_complet.pdf).

41 Environment Norway, "Norwegian Greenhouse Gas Emissions" (www.environment.no/topics/climate/norwegian-green-house-gas-emissions).

42 Melton et al., supra note 2.

providers to reduce the carbon intensity of their fuels to 15 percent below 2016 levels by the year 2030.[43]

In Norway, a blending obligation for biofuels in road transportation fuels was implemented in 2007. The share of biofuels has steadily increased, and in 2019 the obligation was to have 12 percent of traded fuels being biofuels (advanced biofuels are double counted). In 2020, the blending obligation further increased to 20 volume percentage.[44]

Since the Clean Fuels Fund investment was not part of the 2022 federal budget, assessing the LCFS schemes is beyond the scope of this article. However, both Canada and Norway have implemented standards to reduce GHG emissions.

Summary of Supply Factors

Among the supply-focused ZEV policies that we have assessed, the 2022 Canadian federal budget includes one main component—namely, a national sales mandate applicable to all automotive companies that manufacture in Canada or import into Canada, ensuring that at least 20 percent of new light-duty vehicle sales are ZEVs by 2026, at least 60 percent by 2030, and 100 percent by 2035.

In table 2, we summarize how the supply-focused ZEV policies compare between Norway and Canada, noting that in all categories Norway leads by ample margins.

ASSESSMENT OF POLICIES

Why is Norway so far ahead in terms of EV adoption relative to Canada? Norway's national incentive policies for ZEVs target demand more than supply to boost sales. Norway has adopted a "polluter pays principle" in the car tax system, making it economically beneficial to choose zero- and low-emission cars over high-emission vehicles.[45] By waving vehicle import duties and car registration and sales taxes, Norway's legislation is effectively subsidizing ZEV purchases. Furthermore, Norway supplemented the tax relief with non-financial incentives such as a broad public charging network, access to HOV and bus lanes, exemptions from toll road charges, and free public parking.

A recent study by Cincotta and Thomassen found that EV exemptions from VAT and from CO_2- and weight-based registration tax—which together make up about 70 percent of the pre-tax price of ICE vehicles—are the most effective policies in driving EV adoption in Norway.[46] In fact, the authors estimated that the removal of

43 Canada, Environment and Natural Resources, "Clean Fuel Regulations" (www.canada.ca/en/environment-climate-change/services/managing-pollution/energy-production/fuel-regulations/clean-fuel-regulations.html).

44 IEA Bioenergy, "Country Reports: Implementation of Bioenergy in Norway—2021 Update" (www.ieabioenergy.com/wp-content/uploads/2021/11/CountryReport2021_Norway_final.pdf).

45 Norsk elbilforening, "Norwegian EV Policy" (https://elbil.no/english/norwegian-ev-policy).

46 Costanza Cincotta and Øyvind Thomassen, *Evaluating Norway's Electric Vehicle Incentives* (Bergen, Norway: NHH Norwegian School of Economics, Department of Business and Management Science, Institutt for foretaksøkonomi, 2023).

TABLE 2 Summary of Supply Policies for Norway and Canada

Supply policy	Norway	Canada	Country offering higher benefit
Regulated ZEV sales targets	100% ZEV by 2025	100% ZEV by 2035	Norway in the short term
Vehicle emissions standards	85 g CO_2/km by 2020	119 g CO_2/km by 2025; 71 g CO_2/km by 2040	Norway in the short term
Low-carbon fuel standards	Both countries have a low-carbon fuel scheme.		

ZEV = zero-emission vehicle.

these financial incentives would reduce the EV market share to 25 percent from the 66 percent observed in 2021, and increase CO_2 emissions from new vehicles sold by 170 percent. The findings from this study suggest that Norway's success can be largely attributed to the financial incentives offered to consumers, especially when one considers that Norway imposes hefty vehicle import duties and car registration taxes, making cars significantly more expensive there than in most other countries. By providing these financial incentives for EVs, Norway is effectively subsidizing EV purchases at levels that other countries cannot afford.[47]

In contrast, Canada began its push for ZEVs far later than other jurisdictions. Canada has adopted a mix of both supply and demand legislation, harnessing advantages from both the Norwegian and Californian systems. However, Canada's policies substantially lag behind Norway's. Canada's financial incentives are substantially lower than Norway's, even after the extension of the iZEV financial program in the 2022 Canadian federal budget. Having said this, economists have expressed concerns that EV subsidies alone may be a costly and ineffective way to reduce GHG emissions, considering that the amount of carbon abated per dollar of subsidy may be economically unjustifiable. Irvine notes that the financial subsidy granted to EV consumers in Canada—which ultimately decreases CO_2 emissions via EV adoption—can have a substantially higher cost than the corrective carbon tax collected by the government.[48] Exacerbating this issue is the fact that a portion of EV purchasers who receive the financial incentive would still purchase an EV in the absence of a subsidy, ultimately diluting the power of the subsidy. Since the iZEV financial program extension in the 2022 Canadian federal budget provides substantially less financial incentive

47 Felix Richter, "This Chart Shows How Norway Is Racing Ahead on EVs," *World Economic Forum*, June 6, 2023 (www.weforum.org/stories/2023/01/norway-electric-vehicle-energy-transport).

48 Ian Irvine, "Electric Vehicle Subsidies in the Era of Attribute-Based Regulations" (2017) 43:1 *Canadian Public Policy* 50-60.

than Norway's policies, additional measures, such as more substantial GHG-reduction policies, may be necessary to reach Canada's Paris Agreement goals.

In addition, Canada should consider non-financial incentives that have aided Norway's EV adoption success. Canada's non-financial incentives are limited to access to HOV lanes and EV-ready building codes in selected provinces. Furthermore, Canada's national infrastructure of charging stations is far less extensive than Norway's. This is perhaps the biggest challenge, given that Canada is approximately 24 times the size of Norway in terms of land mass but has 43 times fewer charging stations per 1,000 km^2 than Norway. A broad network of charging infrastructure has been reported as a major factor that encourages consumers' adoption of EVs,[49] so this non-financial incentive could further support Canada in accomplishing its ZEV adoption objectives. The government of Canada has begun to take action on this front. In the 2022 Canadian federal budget, it announced that the Canada Infrastructure Bank will invest $500 million in large-scale urban and commercial ZEV charging and refuelling infrastructure. However, it remains to be seen whether this major investment can bridge the gap between Canada and Norway's charging infrastructure. Finally, Canada will need to consider developing a national charging strategy, like Norway did.[50] Norway's rapid EV adoption initially resulted in an ad hoc approach to the resulting increase in charging demand, which led to multiple public charging vendors using multiple mobile apps, limited options for direct payment, poorly designed parking spots, short charging cables, and malfunctioning hardware.[51] As a consequence of this, the Norwegian Ministry of Transport has developed a national charging strategy to ensure that charging services are simple to use. Canada will need to plan for this type of strategy when expanding its EV charging infrastructure.

In addition to Norway's stronger supply and demand policies to encourage the adoption of ZEVs, the country has other intrinsic factors that can further explain its success. Most notably, as a jurisdiction, Norway's concern for the environment is significantly greater than Canada's, considering that Norway is a leader on climate change performance and Canada is a laggard.[52] In the 2024 Climate Change Performance Index (CCPI)—which evaluates 63 countries and the European Union on their progress in reducing GHG emissions and energy consumption, increasing renewable energies, and enacting climate policy—Norway was ranked 12th overall, while Canada was near the bottom in 62nd place.[53]

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49 Melton et al., supra note 2.

50 Norwegian Ministry of Transport, National Charging Strategy (Oslo: Norwegian Ministry of Transport, n.d.) (www.regjeringen.no/contentassets/26d4c472862342b69e8d49803b45c36a/en-gb/pdfs/national-charging-strategy.pdf).

51 Békés et al., supra note 25.

52 York University, Faculty of Environmental and Urban Change, "5 Ways Norway Leads and Canada Lags on Climate Action," February 10, 2021 (https://euc.yorku.ca/news-story/5-ways-norway-leads-and-canada-lags-on-climate-action/).

53 Climate Change Performance Index (https://ccpi.org).

CONCLUSION

The 2022 Canadian federal budget proposed several policies to incentivize both the demand for EVs among consumers and the supply of EVs by the automotive industry in order to reach Canada's zero-emission targets. However, Canada's EV adoption has been slow; as of 2023, only 2.3 percent of its cars in use were EVs. On the other hand, Norway is the world leader in ZEV adoption, with 29 percent of its vehicles in use being ZEVs as of 2023.

After reviewing the demand and supply policies in Canada and Norway, we conclude that Canada lags substantially behind Norway in both areas. Canada could enhance its ZEV adoption by incorporating certain policies that have proved successful in Norway, such as a more extensive EV charging and refuelling infrastructure and the implementation of non-financial incentives such as HOV lanes and EV-ready building codes at the national level. Other intrinsic factors, such as a greater concern for climate change performance, can aid Canada in its pursuit of zero-emission targets. Like Canada, Norway has a cold northern climate with large rural areas, so Norway's success in EV adoption provides reassurance to those who question whether EVs can handle Canada's freezing weather.

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Policy Forum: On the Way to a Distance-Based Tax?

Jean-Philippe Meloche, Michaël Robert-Angers, and Luc Godbout*

PRÉCIS

Cet article s'intéresse aux outils de financement du réseau routier canadien qui mettent à contribution les usagers des routes. Quatre sources de revenu sont présentées : les taxes sur les carburants, les frais d'immatriculation, les taxes sur le carbone et la tarification routière. Une analyse sommaire des recettes tirées de ces sources de revenu pour le Québec et l'Ontario montre qu'elles ne permettent pas de combler les coûts des réseaux routiers dans ces deux provinces. Dans un contexte de changement technologique, les recettes des taxes sur les carburants reculent et les frais d'immatriculation prennent une place de plus en plus prépondérante dans le financement des routes. Pour redresser la situation, la mise en place d'une tarification kilométrique apparaît comme une solution appropriée. Cette solution est toutefois complexe à mettre en place et sa réalisation pourrait prendre plusieurs années. D'ici là, une hausse des taxes sur les carburants est le meilleur moyen de financer le maintien des réseaux routiers en bon état et pour faciliter la migration vers un nouveau mode de financement.

ABSTRACT

This article looks at the instruments through which motorists contribute to financing the Canadian road network. Four sources of revenue are presented: fuel taxes, vehicle registration fees, carbon taxes, and tolls. A summary analysis of the revenues from these sources in Quebec and Ontario shows that they do not cover the costs of the road networks in these two provinces. In these times of technological change, revenues from fuel taxes are shrinking and those from vehicle registration fees are growing steadily and fast becoming the chief source of road financing. To redress the situation, a distance-based pricing system seems like the best solution. However, such a solution is complex to implement and could take several years to become operational. Until then, raising fuel taxes is the best way to ensure financing for road network maintenance and to facilitate the transition to a new mode of financing.

KEYWORDS: ROADS ■ PRICING ■ DISTANCE-BASED TAX ■ GASOLINE TAX ■ GREEN TAX

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CONTENTS

Introduction 58
How Motorists Contribute to Road Financing 59
Fuel Taxes 59
Driver's Licence and Vehicle Registration Fees 60
Carbon Tax and Emission-Control Mechanisms 63
Tolls 63
Challenges of Road Financing 65
Not Enough Revenues To Sustain the Road Network 65
Accounting for Externalities 68
Crumbling of the Fuel Tax Base 68
Possible Solution: A Distance-Based Tax 70
Distance-Based Tax 72
Costs and Benefits of a Distance-Based Tax 73
In the Meantime: Raise Fuel Taxes 75
Conclusion 75

INTRODUCTION

Canada is a vast country where road transportation is the primary mode of moving freight and passengers across the land. Public authorities (federal, provincial, and municipal governments) make available more than 1.1 million kilometres of public roads, nearly 40 percent of which are paved.[1] Public expenditure for the construction and maintenance of these roads amounts to tens of billions of dollars annually.[2] Figuring out how to get the different network users to contribute in a fair and equitable manner and determining a suitable pricing system in order to offer optimal public services is no easy task. Furthermore, there is no consensus on the notion of user charges for public infrastructure use. In fact, many people perceive user fees as nothing more than an additional, unfair, and regressive form of taxation.[3]

Since the end of the 1990s,[4] three factors have shifted our traditional thinking about appropriate policy levers designed to address the pricing of road use. First, increased knowledge about the consequences of climate change means that the

1 Canada, Transport Canada, "Transportation in Canada 2021: Road System" (https://tc.canada.ca/en/corporate-services/transparency/corporate-management-reporting/transportation-canada-annual-reports/2021/road-system).

2 These expenditures amount to nearly $18 billion for roads in Quebec and Ontario alone, excluding forest roads (see table 3).

3 Richard M. Bird and Thomas Tsiopoulos, "User Charges for Public Services: Potentials and Problems" (1997) 45:1 *Canadian Tax Journal* 25-86.

4 The first Conference of the Parties (COP) bringing together on an annual basis the countries committed to reducing GHGs took place in Berlin in 1995. In 1997, the Kyoto Protocol setting binding targets for GHG reduction was signed. See: Compte CO_2, "Les COP : Une brève histoire de la COP1 à la COP27" (www.compteco2.com/article/historique-cop-conference-des-parties).

relationship between internal combustion engine vehicle use and the generation of greenhouse gases (GHGs) must be taken into account. Second, because of the efforts being made to electrify the stock of road vehicles, fuel consumption is on the decline, which points to an inevitable decline in fuel tax revenues and the need to identify new pricing mechanisms.[5] Third, expenditures for developing and maintaining the road and public transit infrastructures are expected to rise because wages and the cost of materials are subject to inflation.[6] Consequently, it seems inevitable that the sources of road financing need to be changed.

This article looks at the financing prospects for the Canadian road network. It revisits the conclusions drawn by Robert-Angers, Meloche, and Godbout regarding road financing in Quebec.[7] The first part of the article presents the financing instruments tied to road use and describes how these instruments are used in Canada. The second part presents the issues and challenges of financing the network in the context of how motorists contribute to it and what developments in engine technology mean for this financing. The last part presents potential options over the short and long term for covering the growing shortfall in road financing.

HOW MOTORISTS CONTRIBUTE TO ROAD FINANCING

Motorists contribute to public finances for roads through four sources of user-based financing that rest on the principles of user pays, polluter pays, and beneficiary pays. These sources of revenue are fuel taxes, vehicle registration fees, carbon pollution taxes, and tolls.

Fuel Taxes

Fuel taxes in Canada are excise taxes that are proportional to the amount of fuel consumed. Historically, fuel consumption has been proportional to distances travelled on roads. This is why fuel taxes have long been viewed as a form of user charge that in large part respects the principle of "user pays." However, as engines have become more fuel efficient, this relationship has softened. Moreover, fuel taxes do not take account of the impact of the disproportionate wear on roads caused by heavier vehicles, nor do they ensure that owners of electric vehicles contribute to the cost of maintaining

5 Joel Wood, "The Past, Present, and Future of Fuel Taxation in Canada," Finances of the Nation feature (2024) 72:2 *Canadian Tax Journal* 375-400.

6 This is observed in the provincial budget forecasts. For an example, see Québec, Finances Québec, 2023-2024 Budget, Plan Budgétaire, March 21, 2024, at H.23.

7 Michaël Robert-Angers, Jean-Philippe Meloche, and Luc Godbout, *Remplacer (éventuellement) la taxe sur les carburants par une taxe kilométrique?* Cahier de recherche no. 2024-06 (Sherbrooke, QC: Université de Sherbrooke, Chaire de recherche en fiscalité et en finances publiques, 2024) (https://cffp.recherche.usherbrooke.ca/remplacer-eventuellement-la-taxe-sur-les-carburants-par-une-taxe-kilometrique).

and improving the network.[8] On the other hand, fuel taxes are proportional to the level of GHG emissions released by vehicles on the roads and thus contribute to reducing emissions.[9] In this sense, they respect the principle of "polluter pays."

Figure 1 shows the total of the applicable rates of fuel excise taxes on gasoline and diesel in the Canadian provinces as of March 1, 2025. This total includes 10 cents per litre (¢/L) on gasoline and 4 ¢/L on diesel levied by the federal government in all the provinces. All the provinces apply fuel excise taxes. Newfoundland and Labrador and Ontario have lowered their rates temporarily. In Quebec and in British Columbia, rates are higher in certain regions. For example, the rate is 3 ¢/L higher in the Greater Montreal area than elsewhere in Quebec. In Metro Vancouver, the rate is 12.5 ¢/L higher than in the rest of the province. The higher taxes are justified by the need to finance public transportation. It is not unreasonable to believe that, in these urban areas, traffic problems are such that individuals who choose to travel by public transit contribute to easing congestion. Even if it is not possible to draw a direct proportional connection between this benefit and the amount of tax paid, we know that public transportation use contributes to improved motor vehicle travel.[10] Given that public transit constitutes a benefit for the road network, the surtaxes in Montreal and Vancouver are in keeping, at least in part, with the principle of "beneficiary pays."

Driver's Licence and Vehicle Registration Fees

Fixed costs represent a large part of the cost of the transportation network. Road infrastructures serve the purpose of facilitating access to and travel across the land. For this reason, how the network is deployed is not entirely a function of traffic volume (especially in remote regions). Consequently, the road network affords an inherent benefit beyond the use that motorists make of it. To finance these costs, fixed annual fees, such as for driver's licences and vehicle registration fees, are appropriate.

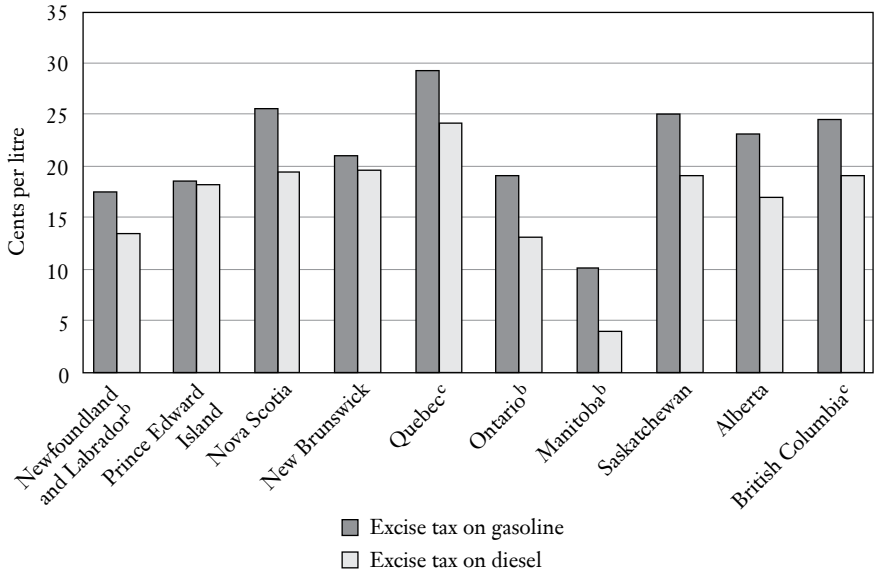
Table 1 shows the vehicle registration renewal fees across Canada. They range from $61 to $189 depending on the province and on vehicle-type parameters. They have been reduced to nil in Ontario since 2022. Amounts are difficult to compare across provinces because they sometimes include service charges. Moreover, additional fees are included in some provinces or regions, notably for public transit financing.

8 Justin Leroux, Mariane Arsenault, and Jérémy Laurent-Lucchetti, *Réflexion sur la tarification du réseau routier québécois*, rapport de projet no. 2010RP-02 (Montreal: Centre for Interuniversity Research and Analysis on Organizations (CIRANO), 2010) (https://cirano.qc.ca/files/publications/2010RP-02.pdf), at 10.

9 Canada, Ressources naturelles, *Guide de consommation de carburant 2023* (Ottawa: Ressources naturelles, 2023) (https://ressources-naturelles.canada.ca/sites/nrcan/files/oee/pdf/transportation/fuel-efficient-technologies/Guide%20de%20consommation%20de%20carburant%202023.pdf).

10 Michael L. Anderson, "Subways, Strikes, and Slowdowns: The Impacts of Public Transit on Traffic Congestion" (2014) 104:9 *American Economic Review* 2763-96.

FIGURE 1 Cumulative Rate of Fuel Excise Taxes by Province[a] and Fuel Type, as of March 1, 2025



a Total of provincial and federal taxes. The federal portion is the same in all the provinces, namely, 10 ¢/L for gasoline and 4 ¢/L for diesel.

b The provinces of Newfoundland and Labrador and Ontario declared a temporary partial tax holiday. Respectively, this represents a discount of 7 ¢/L and 5.7 ¢/L (5.3 for diesel).

c In Quebec and in British Columbia, rates vary by region. For example, they are higher in Montreal (3 ¢/L more than in the rest of Quebec) and in Vancouver (12.5 ¢/L more than in the rest of British Columbia).

Sources: Kalibrate, "Full Monty" (https://charting.kalibrate.com/Charting/FullMonty) and authors' calculations.

In Quebec, additional fees for luxury vehicles[11] and large cylinder-capacity vehicles are added to the registration fee.[12] Also, a $30 contribution is added in municipalities served by public transit services. An additional contribution is added on top of this

11 Vehicles worth more than $40,000 with a net mass of 3,000 kg or less and less than seven years old. The contribution amounts to 1 percent of the value exceeding $40,000. However, if it is a fully electric, plug-in hybrid, or hydrogen fuel cell vehicle, the owner benefits from a reduction or exemption based on the value of the vehicle. See Société de l'assurance automobile du Québec, "Payer les droits d'immatriculation additionnels pour un véhicule de luxe" (https://saaq.gouv.qc.ca/immatriculation/droits-immatriculation-additionnels-vehicules-luxe). It should be noted that the federal luxury tax applies to new vehicles, never registered, manufactured after 2018, and whose value is more than $100,000.

12 Engine of 3.95 litres or more, manufactured after 1994. The additional cost is $40.75 for a displacement of 4 litres and increases gradually depending on the displacement. It is capped at $432 for a displacement of 7 litres and more (2024). See Société de l'assurance automobile du

TABLE 1 Annual Vehicle Registration Renewal Fees for Passenger Vehicles by Province, 2024

Province	Fee[a]	Note
Newfoundland and Labrador	$90.00	Rates are reduced for online transactions, seniors, and veterans.
Prince Edward Island[b]	$100.00	
Nova Scotia	$71.65 to $166.95	Fee varies proportionally to vehicle weight. Annual fee invoiced every two years for twice the amount indicated here.
New Brunswick	$61.00 to $189.00	Fee varies proportionally to vehicle weight.
Quebec[b]	$133.00	Registration fee only. Rates are reduced for designated and peripheral regions. In some regions, a public transit contribution is added. There are additional fees for large cylinder-capacity vehicles and luxury vehicles.
Ontario	$0	Initial fees to obtain plate and certificate apply, but renewal fees have been reduced to $0 since March 13, 2022.
Manitoba	$119.00	
Saskatchewan[b]	$68.00	Included in a package that also covers cost of auto insurance.
Alberta	$93.00	Service charges included.
British Columbia	$64.00 to $160.00	Includes registration fee ($18) and driver's licence fee.

a The data are not fully comparable because some include service charges and others do not.
b These provinces apply different fees for electric vehicles. In Prince Edward Island, the rate is halved to $50 for hybrid vehicles and reduced to $0 for electric vehicles. In Quebec, the additional fee for luxury vehicles is reduced for electric vehicles and plug-in hybrid vehicles. In Saskatchewan, an additional fee of $150 applies to electric vehicles.

Sources: Official government agency websites for each province.

contribution in some regions.[13] These transfers from motorists to public transit financing can be justified by the principle of beneficiary pays. However, it is hard to tell exactly whether the amounts collected correspond to the benefits that motorists derive from public transit services.

Québec, "Coût d'immatriculation additionnel pour les véhicules de forte cylindrée" (https://saaq.gouv.qc.ca/saaq/tarifs-amendes/immatriculation/cout-immatriculation-additionnel-vehicules-forte-cylindree).

13 Société de l'assurance automobile du Québec, "Perception pour le transport en commun" (https://saaq.gouv.qc.ca/saaq/tarifs-amendes/immatriculation/cout-renouvellement/vehicules-promenade/contribution-transport-commun); and Québec, Transports et Mobilité durable, *Annual Report 2018-2019* (Quebec: Transports et Mobilité durable, 2019), at 26. This $30 contribution is applied in the regions of Montreal, Quebec, Gatineau, Trois-Rivières, Saguenay, and Sherbrooke and has not been increased since 1992.

Carbon Tax and Emission-Control Mechanisms

The Quebec government's cap-and-trade system for GHG emission allowances (referred to by its French acronym SPEDE) and carbon taxes constitute a relatively effective way of internalizing the social and environmental costs of the carbon content in the different types of fuel that result in emissions when combusted.[14] As with fuel taxes, these levies are proportional to the level at which internal combustion engine vehicles are used. In this sense, they constitute financing mechanisms that embody the polluter pays principle.

In Quebec, oil refining and fuel distribution require a SPEDE emissions permit. The cost of these permits is considered as a pump-price input borne by the end user.[15] British Columbia, too, has its own carbon tax measure. The other provinces are subject to the levy on fuel under the federal carbon pricing backstop.[16] The impact of these measures is estimated at about 17.6 ¢/L on the final sales price at the pump.[17] In Quebec, it is estimated at 12.5 ¢/L at a carbon price of $53/tonne (May 2024 auction).[18] Since these fiscal measures are borne by motorists when they use the roads, they are considered as a means of internalizing the environmental cost of road use. They thus fit with the polluter pays principle.

Tolls

Tolls are the most direct means of road financing based on the user pays principle. Their primary advantage is that pricing can vary by time of day, depending on traffic levels. However, the cost of implementing the pricing systems remains high, and tolls generate more discontent than any other mode of financing.[19]

Table 2 presents the active tolls in Canada in 2024. Numerous toll systems have been dismantled in recent years, including on the Champlain Bridge in Montreal, the Golden Ears and Port Mann bridges in Vancouver, and Highways 412 and 418 in Ontario. In Ontario, most of the tolls are on international bridges subject to

14 Georgina Santos, Hannah Behrendt, Laura Maconi, Tara Shirvani, and Alexander Teytelboym, "Part I: Externalities and Economic Policies in Road Transport" (2010) 28:1 *Research in Transportation Economics* 2-45 (https://doi.org/10.1016/j.retrec.2009.11.002).

15 Patrick González, *Le prix à la rampe de chargement : une étude du marché des produits pétroliers raffinés au Québec*, report submitted to Régie de l'énergie du Québec (Québec: Centre de Recherche en économie de l'Environnement, de l'Agroalimentaire, des Transports et de l'Énergie (CREATE), 2020) (www.regie-energie.qc.ca/storage/app/media/consommateurs/informations-pratiques/prix-petrole/analyses/Rapport-prix-a-la-rampe-PG_Final_2020.pdf).

16 Greenhouse Gas Pollution Pricing Act, SC 2018, c. 12, section 186, schedule 1.

17 Kalibrate, "Full Monty" (https://charting.kalibrate.com/Charting/FullMonty).

18 Canadian Taxpayers Federation, *25th Annual Gas Tax Honesty Report* (Calgary: Canadian Taxpayers Federation, 2023) (www.taxpayer.com/media/Gas-Tax-Honesty-Report-2023.pdf).

19 Jean-Philippe Meloche, *Towards a New Era in Road Pricing? Lessons from the Experience of First Movers*, Working paper no. 2019S-35 (Montreal: Center for Interuniversity Research and Analysis on Organizations (CIRANO), 2019) (https://cirano.qc.ca/files/publications/2019s-35.pdf).

TABLE 2 Tolls in Effect in Canada by Province, 2024

Province	Infrastructure	Amount (light vehicle)	Note
Prince Edward Island and New Brunswick	Confederation Bridge	$50.25	Rate for a return trip.
Quebec	A30 Express	$3.90	
	A25 Bridge	$10.52	During peak hours (with no customer account).
Ontario	Highway 407	34.43 ¢/km	During peak hours.
	Highway 407 ETR	62.05 ¢/km	Maximum during peak hours.
	Sault Ste. Marie International Bridge	$5.70	
	Blue Water Bridge	$6.00	
	Thousand Islands Bridge	$4.75	
	Seaway International Bridge (Three Nations Crossing)	$4.25	
	Ambassador Bridge	$11.00	
	Rainbow Bridge	$6.50	
	Queenston-Lewiston Bridge	$6.50	
	Whirlpool Rapids Bridge	$6.50	
	The Peace Bridge	$11.00	
	Aazoghan Bridge	$11.00	
	Detroit-Windsor Tunnel	$6.75	
	Ogdensburg-Prescott International Bridge	$4.25	
Nova Scotia	Cobequid Pass Highway 104	$4.00	Free for Nova Scotians.
	MacKay Bridge	$1.25	
	MacDonald Bridge	$1.25	
Alberta	Highway 93	$11.00 per adult for one day	Includes access to Banff, Jasper, and Kootenay National Parks, which this highway runs through.

Sources: Data taken from bridge and highway management organization websites in August 2024.

agreements between Canada and the United States. On the A25 Bridge in Montreal and on Highway 407 in Toronto, fees vary during peak hours to account for traffic effects. This form of dynamic pricing is justified by the polluter pays principle (because congestion is a form of pollution). Highway 407 is also a good example of a distance-based pricing scheme that works in Canada.

Except for the MacKay and Macdonald bridges in Halifax, all tolls presented in table 2 are enforced by public-private partnerships or agreements involving the federal government. These tolls seem harder to remove than those under full control of provincial governments. Revenues from private tolls like A25, A30, Highway 407, and Cobequid Pass Highway 104 are shared with provincial governments.

CHALLENGES OF ROAD FINANCING

It is unclear to what extent the instruments of road financing presented above contribute to financing the road networks in an optimal manner. It is likely that Canadian provinces will face major financial challenges in the coming years. It is also safe to say that road users do not fully bear the social and environmental costs that they generate.

Not Enough Revenues To Sustain the Road Network

Table 3 presents an estimation of the 2022 revenues from the road financing mechanisms presented in the first part of this article for Canada's two largest provinces: Quebec and Ontario. Ontario cut its fuel tax rates considerably in 2022 (as of July 1) and eliminated annual registration renewal fees entirely (as of March). Comparing the revenues from motorists against the road costs in these two provinces reveals a road financing shortfall of roughly $2 billion in Quebec and $3.8 billion in Ontario. This shortfall was covered in large part by the property taxes that finance municipal roads.

Non-motorists also benefit from roads when they receive public services provided by road vehicles and financed by general taxes (like police and fire services). Non-motorists use road infrastructure as pedestrians or cyclists. Roads are also used to hold some events, like festivals. In these cases, public financing of roads from general taxes can be justified under the beneficiary pays principle. To our knowledge, no study estimates the optimal share of road financing between road users and non-users. Economic theory rather supports the idea of self-financing roads. This idea originated in the seminal work of Mohring and Harwitz, published in 1962.[20] According to them, congestion pricing in optimal conditions raises the necessary revenues to finance the capital and operational costs of roads.[21] Using this idea of self-financing, table 3 suggests that the price of using the road network in Ontario

20 Herbert Mohring and Mitchell Harwitz, *Highway Benefits: An Analytical Framework* (Evanston, IL: Northwestern University Press, 1962).

21 Erik T. Verhoef and Herbert Mohring, "Self-Financing Roads" (2009) 3:5-6 *International Journal of Sustainable Transportation* 293-311 (https://doi.org/10.1080/15568310802259940).

TABLE 3 User-Based Revenues and Road Expenditures for Quebec and Ontario, 2022

	Quebec	Ontario	Note
	millions of dollars		
User-based revenues			
Fuel tax (provinces)	2,142	2,679	Revenues drawn from fuel taxes by the provincial governments. The rate was cut in Ontario as of July 1, 2022.
Driver's licence and vehicle registration fees	1,446	1,347	For Quebec, revenues include the SOFIL contribution, the contribution by motorists to public transit, and the additional contribution by Montreal motorists. In Ontario, vehicle registration renewal fees were abolished as of March 2022, but other fees and permits were maintained.
Federal excise tax on gasoline and diesel	1,016	1,778	
Tolls[a]	141	1,379	Highways 25 and 30 in Quebec and 407 in Ontario.
ARTM fuel surtax of 3 cents	87	—	
Total user-based revenues	**4,832**	**7,183**	
Road expenditures			
Provincial expenditures (Ministry of Transportation)	3,662	4,040	Public transportation expenditures excluded. Quebec: FORT expenditures + road maintenance. Ontario: Infrastructure management + operations.
Net municipal expenditures[b]	2,833	5,747	Garbage removal, snow removal, street lighting, traffic and parking. Expenditures net of transfers earmarked for roads already accounted for at the provincial level.
Federal expenditures	220	4	In Quebec, the amount includes expenditures on the Jacques Cartier Bridge, the Champlain Bridge, the federal portion of the Mercier Bridge, the Melocheville Tunnel, and part of the Bonaventure Highway, as well as a segment of Highway 15 leading up to the Champlain Bridge. In Ontario, the amount excludes expenditures on international bridges.

(Table 3 is concluded on the next page.)

TABLE 3 Concluded

	Quebec	Ontario	Note
	millions of dollars		
Cost of private infrastructures	101	1,180	This covers the cost of tolls net of user fees remitted to the provincial governments. It includes the operating costs of the concessions, the financing costs, and net profits.
Total road expenditures	6,816	10,971	
Shortfall	**(1,984)**	**(3,788)**	

SOFIL = Société de financement des infrastructures locales du Québec; ARTM = Autorité régionale de transport métropolitain; FORT = Fonds des réseaux de transport terrestre.

a Revenues from tolls on international bridges in Ontario were not taken into account.
b 2021 data in Quebec for municipalities.

Sources: Québec, Finances Québec, *Comptes publics* (Quebec City: Finances Québec); Québec, Ministère des Transports et de la Mobilité durable, *Rapports annuels de gestion* (Quebec City: Ministère des Transports et de la Mobilité durable); La Société les Ponts Jacques Cartier et Champlain, *Rapport annuel* (Quebec City: Les Ponts Jacques Cartier et Champlain); Autorité régionale de transport métropolitain, *Rapport annuel* (Montreal: Autorité régionale de transport métropolitain); Statistics Canada table 10-10-0016-01 (formerly CANSIM table 385-0033), "Canadian Government Finance Statistics for the Federal Government (x 1,000,000)"; Statistics Canada table 10-10-0017-01 (formerly CANSIM table 385-0034), "Canadian Government Finance Statistics for the Provincial and Territorial Governments (x 1,000,000)"; Statistics Canada table 10-10-0020-01 (formerly CANSIM table 385-0037), "Canadian Government Finance Statistics for Municipalities and Other Local Public Administrations (x 1,000,000)"; Statistics Canada table 23-10-0066-01 (formerly CANSIM table 405-0002), "Sales of Fuel Used for Road Motor Vehicles, Annual (x 1,000)"; Statistics Canada table 36-10-0450-01 (formerly CANSIM table 384-0047), "Revenue, Expenditure and Budgetary Balance—General Governments, Provincial and Territorial Economic Accounts (x 1,000,000)"; Société de l'assurance automobile du Québec (Saaq), *Rapport annuel* (Québec: Saaq); and Québec, ministère des Affaires municipales et de l'Habitation, *Sommation des données Municipalités locales—Rapport financier consolidé, Exercice terminé le 31 décembre 2022* (https://cdn-contenu.quebec.ca/cdn-contenu/adm/min/affaires-municipales/publications/finances_indicateurs_fiscalite/information_financiere/rapports_financiers_organismes_municipaux/2022/RAP_financier_2022_sommation_municipalites_locales.pdf). Ontario, Ministry of Transportation, "Expenditure Estimates 2024-25" (www.ontario.ca/page/expenditure-estimates#section-0). Ontario, Ministry of Municipal Affairs and Housing, *Municipal Financial Information Return 2022—Consolidated Statement of Operations: Expenses* (https://efis.fma.csc.gov.on.ca/fir/index.php/en/provincial-summary/year-2009-and-on/). 407 International Inc., *Consolidated Financial Statements—December 31, 2022*. Ministry of Municipal Affairs and Housing Municipal Finance Policy Branch.

and Quebec may be too weak. This produces network overuse and a resource allocation bias.[22]

Accounting for Externalities

Aside from the financial costs associated with maintaining and developing the road network, road use also engenders social and environmental costs. Road users' contributions are not just insufficient to ensure the maintenance and development of the road network, they also do not bear all the social and environmental costs of their GHG emissions (which contribute to climate change) or traffic congestion (which motorists cause).

The literature documents numerous impacts associated with road transportation that have social or environmental costs.[23] The value of these impacts to those who bear their effects (economic losses) can be estimated. Table 4 presents two environmental impacts linked to road transportation, the effects that they cause, examples of elements used to reflect the economic losses caused by these effects, and financial estimations of these impacts per kilometre travelled in Europe and in Canada.

Road network users assume a tax on their GHGs by way of the SPEDE in Quebec and carbon taxes in the other provinces. The amounts collected from users in Quebec and Ontario through these mechanisms are shown in table 5. These amounts constitute compensation for part of the externalities caused by road use. A calculation of the cost of traffic congestion and GHG emissions is also presented in table 5 for the two provinces, in order to measure the magnitude of the economic value of these externalities. The calculations rest on the hypotheses and results drawn from table 4. When the road financing shortfall and the externality costs are added up, table 5 shows that revenues from motorists are roughly $6 billion and $8.8 billion less than the economic cost of road use in Quebec and Ontario, respectively.

Against the current backdrop of a socio-ecological transition, we see that contributions for GHG emissions (SPEDE and carbon taxes) cover part of the cost of emissions but not the implicit subsidy for road use (the shortfall in table 3). In addition, no financial measure takes into account the social costs associated with traffic congestion.

Crumbling of the Fuel Tax Base

Thanks to improvements in technology, the fuel consumption of new vehicles in Quebec diminished significantly, from 9.5 to 8.7 litres/km from 2013 to 2021, despite

22 David G. Duff and Carl Irvine, *Road Pricing in Theory and Practice: A Canadian Perspective* (Vancouver: University of British Columbia, Peter A. Allard School of Law, 2005) (https://commons.allard.ubc.ca/cgi/viewcontent.cgi?article=1105&context=fac_pubs).

23 Erik Verhoef, "External Effects and Social Costs of Road Transport" (1994) 28:4 *Transportation Research Part A: Policy and Practice* 273-87 (https://doi.org/10.1016/0965-8564(94)90003-5).

TABLE 4 Externality Costs Associated with Greenhouse Gas Emissions and Traffic Congestion

Impacts and negative effects	Cost estimation method	Van Dender estimate (European Union)[a]	Recent estimate (Canadian dollars)
Greenhouse gases (global warming)	Crop yield reductions, protection against rising sea levels	2 ¢ to 4 ¢/km (gasoline-powered vehicles)	If cost of carbon is $80/tonne[b] 1.7 ¢/km
Traffic congestion caused by the addition of one vehicle coming to use one space on the road (increased travel time and decreased possibility of estimating travel time)	Estimation of marginal (additional) delay that a driver causes for everyone when they participate in traffic congestion and in the monetization of this time loss	16.8 ¢/km (urban area)	9.3 ¢/km for the Montreal CMA and 7.9 ¢/km for the Quebec City CMA[c]

CMA = census metropolitan area.

a Sources: Kurt Van Dender, *Taxing Vehicles, Fuels, and Road Use: Opportunities for Improving Transport Tax Practice*, OECD Taxation working papers no. 44 (Paris: OECD, 2019).

b Sources: Environment and Climate Change Canada, "Update to the Pan-Canadian Approach to Carbon Pollution Pricing 2023-2030" (www.canada.ca/en/environment-climate-change/services/climate-change/pricing-pollution-how-it-will-work/carbon-pollution-pricing-federal-benchmark-information/federal-benchmark-2023-2030.html) (price at April 1, 2024). Note that the social cost of carbon is higher, standing at $266 per tonne in 2024. See: Environment and Climate Change Canada, "Social Cost of Greenhouse Gas Emissions" (www.canada.ca/en/environment-climate-change/services/climate-change/science-research-data/social-cost-ghg.html).

c Source: Jérémie Dorval and Philippe Barla, "Does Quebec Have the Right Gasoline Tax? An Empirical Investigation" (2017) 43:4 *Canadian Public Policy* 350-62.

the fact that the average size of the vehicles increased over this period.[24] The progressive electrification of the vehicle fleet is also contributing to the reduction in fuel tax revenues, a trend that should grow rapidly. In fact, the intention to prohibit the sale of new gasoline-powered light vehicles as of 2035 renders the decline in revenues from fuel tax inevitable.

Figure 2 presents an estimate (non-predictive) of revenues from the fuel tax and driver's licence and vehicle registration fees through 2040 for Quebec.[25] At current

24 Pierre-Olivier Pineau and Benoit Vincent, *Tendances du parc Automobile québécois 2013-2021* (Montreal: HEC Montréal, Chaire de gestion du secteur de l'énergie, 2023) (https://energie.hec.ca/wp-content/uploads/2023/10/Rapport-ParcAutomobile_web.pdf).

25 Note that this exercise is intended more as a sensitivity analysis, because projecting the evolution of the tax bases for road users is complex and requires, among other things, estimation of the progression of the fleet of internal combustion engine vehicles, the number

TABLE 5 Shortfall Including Revenues and Externality Costs for Quebec and Ontario, 2022

	Quebec	Ontario
	millions of dollars	
Shortfall (see table 3)	**(1,984)**	**(3,788)**
Revenues from SPEDE and carbon taxes[a]	1,089	3,194
Negative externalities (costs)		
Greenhouse gases[b]	(1,600)	(2,500)
Traffic congestion[c]	(3,700)	(5,700)
Shortfall taking account of externalities	**(6,195)**	**(8,794)**

a Natural Resources Canada, "Fuel Consumption Levies in Canada" (https://natural-resources.canada.ca/domestic-international-markets/fuel-consumption-levies-canada).

b Estimate for 5.8 million conventional light combustion vehicles in Quebec and 9.2 million in Ontario (Statistics Canada table 23-10-0308-01, "Vehicle Registrations, by Type of Vehicle and Fuel Type") travelling 16,300 km per year on average in 2022. The cost of 1.7 ¢/km is taken from table 4.

c Congestion costs in Quebec correspond to those of the metropolitan regions of Montreal and Quebec City taken from Jérémie Dorval and Philippe Barla, "Does Quebec Have the Right Gasoline Tax? An Empirical Investigation" (2017) 43:4 *Canadian Public Policy* 350-62. Costs in Ontario correspond to those in the Toronto and Ottawa metropolitan areas and are calculated as a proportion of those in Quebec using proportions from a 2006 Transport Canada study. See Transports Canada, "Le coût de la congestion urbaine au Canada" (2006) (www.bv.transports.gouv.qc.ca/mono/1000014.pdf).

rates, revenues from the fuel tax could hover around $2.1 billion until 2026 before falling thereafter. In 2040, the estimated fuel tax revenues will derive essentially from the sale of diesel and biofuel for heavy vehicles. Quebec is not alone in this regard. All Canadian provinces are facing the same situation in the coming years.

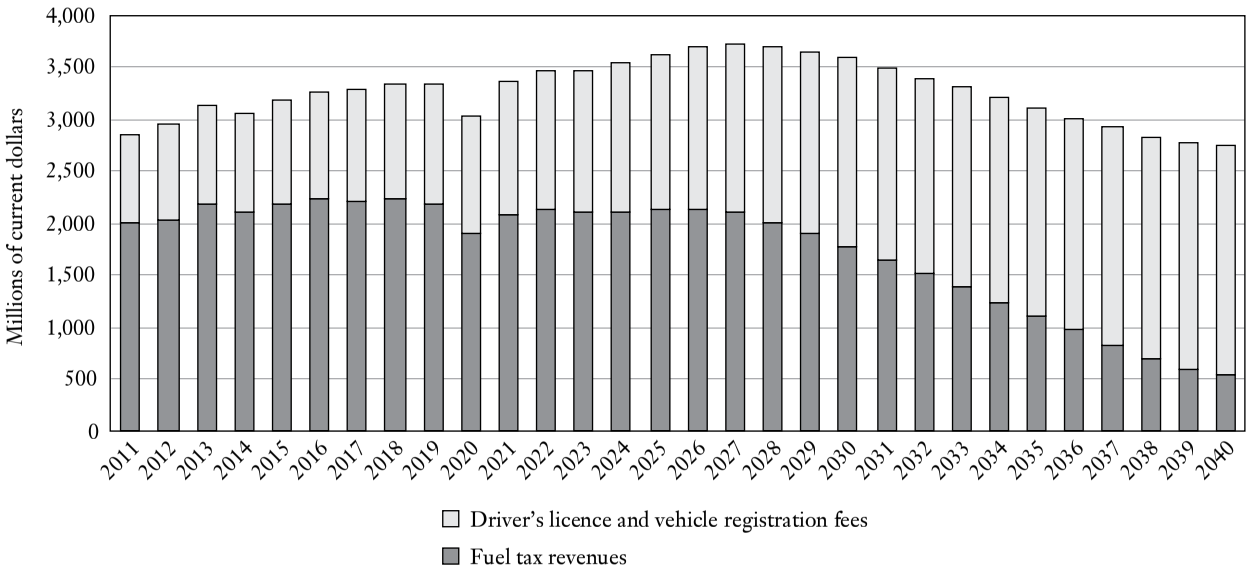
POSSIBLE SOLUTION: A DISTANCE-BASED TAX

If fuel taxes can no longer adequately contribute to road network pricing, vehicle registration fees cover only the fixed costs associated with the network, and carbon tax revenues are destined to disappear with the electrification of the vehicle fleet, then direct pricing seems like an inevitable solution.[26] This could take the form of a distance-based tax.

of kilometres driven annually by them, and the average consumption of these vehicles. This also involves drawing up a series of hypotheses, including those relating to demographics, the penetration rate of electric vehicles, and the technological evolution of internal combustion engines. See on this matter, Organisation for Economic Co-operation and Development and International Transport Forum (ITF), *Tax Revenue Implications of Decarbonising Road Transport: Scenarios for Slovenia* (Paris: OECD, 2019).

26 Wood, supra note 5.

FIGURE 2 Revenues from the Fuel Tax and Driver's Licence and Vehicle Registration Fees (Non-Predictive Estimation), in Millions of Current Dollars, Quebec



Sources: Actual data (until 2023): Fonds des réseaux de transport terrestre (FORT) financial statements submitted to the Conseil du trésor du Québec. Fuel tax projections for 2024 and 2025: FORT financial statements submitted to the Conseil du trésor du Québec. Other estimations: authors' calculations, see Michaël Robert-Angers, Jean-Philippe Meloche, and Luc Godbout, *Remplacer (éventuellement) la taxe sur les carburants par une taxe kilométrique?* Cahier de recherche no. 2024-06 (Sherbrooke, QC: Université de Sherbrooke, Chaire de recherche en fiscalité et en finances publiques, 2024) (https://cffp.recherche.usherbrooke.ca/remplacer-eventuellement-la-taxe-sur-les-carburants-par-une-taxe-kilometrique).

Distance-Based Tax

A distance-based tax is a rate applied to vehicles for each kilometre travelled on the road network. This levy primarily uses a global positioning system (GPS) to measure distances, but other technologies that are not GPS-dependent are also available for this purpose. Varying the tax rate by place and time of day makes it possible to limit certain negative externalities, such as traffic congestion.

There are very few existing examples of a distance-based tax that applies to all vehicles across an entire territory. New Zealand has used distance-based pricing since 1978 for all vehicles not powered by a type of fuel subject to the fuel excise duty (gasoline, compressed natural gas, or liquefied petroleum gas). All diesel-powered vehicles (including light vehicles) must therefore pay the distance-based tax. Moreover, heavy vehicles (3.5 tonnes or more) that use gasoline as fuel are nonetheless subject to the distance-based tax, but they are eligible for a reimbursement of the amount paid. Light electric vehicles ceased to be exempt from the distance-based tax as of April 1, 2024.[27]

In the United States, after conducting two pilot projects since 2006, Oregon became the first state to propose a permanent voluntary mileage-based tax program in 2015.[28] Motorists can choose to pay the mileage-based tax and get refunded for fuel tax, or pay the fuel tax. When revenues from fuel tax will be insufficient, the government of Oregon is planning to make it a compulsory program. Three other states have since followed suit with similar programs: Utah (2020), Virginia (2022), and Hawaii (2023). These states kept their fuel taxes and are hoping to replace registration surcharges for electric vehicles with this form of taxation. Furthermore, pilot projects are ongoing or have been completed in a dozen other states to date, and the Infrastructure Investment and Jobs Act of 2021 provides for carrying out a pilot project for the implementation of a national mileage-based tax.[29] Though states have been experimenting with mileage-based taxes since the early 2000s, their implementation in the United States on a voluntary basis remains relatively timid and has been carried out over a long stretch of time.

Enforcing a distance-based tax for all vehicles seems complex. After several feasibility studies, the Netherlands had to give up on their project based on GPS data, announced in 2009, for lack of political support.[30] The implementation of this tax is

27 New-Zealand, Ministry of Transport, "Buying a Light Vehicle" (www.transport.govt.nz/about-us/what-we-do/queries/buying-a-light-vehicle).

28 Oregon, Department of Transportation, "Learn About OReGO" (https://www.oregon.gov/odot/orego/Pages/Learn-More.aspx).

29 Garett Shrode, Jeff Davis, and Robert Puentes, "Driving Change: Advice for the National VMT Fee Pilot," *Eno Center for Transportation*, July 24, 2023 (https://enotrans.org/eno-resources/driving-change-advice-for-the-national-vmt-fee-pilot).

30 Özgül Ardiç, Jan Anne Annema, and Bert van Wee, "Non-Implementation of Road Pricing Policy in the Netherlands: An Application of the 'Advocacy Coalition Framework'" (2015) 15:2 *European Journal of Transport and Infrastructure Research* 116-46.

now planned for 2026, but for heavy vehicles only.[31] In Belgium, the Brussels region had hoped to have their *SmartMove* system running by 2022 but first had to obtain the approval of the neighbouring regions.[32] The *SmartMove* project is based on a smartphone app. The test phase begun in the fall of 2022 has no hard deadline.[33] After this test phase is completed, the government will decide whether to implement the project on a larger scale. So far, the project is not supported by any of the opposition groups, which is rendering its implementation difficult.[34]

Costs and Benefits of a Distance-Based Tax

Despite being conceptually appealing, distance-based taxes present a few major drawbacks. First, they do not enjoy a high level of social acceptability.[35] Such taxes are associated with a barrier to the use of public property, particularly by reduced-mobility and low-income individuals.[36] Moreover, though there is nothing to prevent resorting to non-GPS technology (such as non-location OBD-II device readings or manual entry of a photo of the odometer),[37] the perceived breach of privacy has a negative impact on the acceptance of such taxes.[38]

To overcome the problem of privacy, the Montreal Metropolitan Community (MMC)[39] has suggested a scheme in which all motorists who drive in its territory are required to pay a fixed cost for road usage with a pass, but they are free to provide

31 Netherlands, Ministerie van Infrastructuur en Waterstaat [Ministry of Infrastructure and Water Management], "Legislation Relating to the Heavy Goods Vehicle Charge" (www.vrachtwagenheffing.nl/english/legislation).

32 BX1, Médias de Bruxelles, "Taxe kilométrique : la Région lance un test pour l'application SmartMove," August 24, 2022 (https://bx1.be/categories/mobilite/taxe-kilometrique-la-region-lance-un-test-pour-lapplication-smartmove).

33 SmartMove, "SmartMove, What's It All About? (https://smartmove.brussels/en/introduction-2).

34 Pauline Delgume, "Des millions d'euros déjà dépensés pour SmartMove," *L'Écho*, October 2, 2022 (www.lecho.be/economie-politique/belgique/bruxelles/des-millions-d-euros-deja-depenses-pour-smartmove/10417417.html).

35 Communauté métropolitaine de Montréal, "Financement de la mobilité durable : Étude préliminaire pour une contribution kilométrique" (2023) (https://cmm.qc.ca/wp-content/uploads/2023/12/Synthese_Financement_de_la_mobilite_durable.pdf).

36 Alexandros Nikitas, Erel Avineri, and Graham Parkhurst, "Understanding the Public Acceptability of Road Pricing and the Roles of Older Age, Social Norms, Pro-Social Values and Trust for Urban Policy-Making: The Case of Bristol" (September 2018) 79 *Cities* 78-91 (https://doi.org/10.1016/j.cities.2018.02.024).

37 Azuga, "Mileage Reporting Options for Every Lifestyle" (https://www.azuga.com/downloads/mileage-reporting-options-for-successful-road-usage-charging).

38 Thomas Buckley, "Vehicle Miles Traveled VS Pay-at-the-Pump Gas Tax," *NewGeography*, December 30, 2021 (www.newgeography.com/content/007262-vehicle-miles-traveled-vs-pay-pump-gas-tax).

39 Communauté métropolitaine de Montréal, supra note 35.

their GPS information (by the means of their mobile phone or an OBD-II device) to reduce this charge. Since GPS information allows tax reduction instead of tax payment, this may lower most motorists' concerns about privacy. Daily or weekly passes purchased through an online payment portal may suit occasional drivers (for example, drivers who mostly drive outside the MMC). Heavy drivers and drivers concerned with privacy can choose to pay the full annual cost of the pass, while most drivers will prefer to share their GPS information to reduce the price of their annual road charge. It is anticipated that compliance with the tax would be ensured by automatic cameras that read licence plates, randomly scattered across the metropolitan area. A control of this type is already used in Germany for heavy vehicles[40] and planned to be used in other distance-based road pricing schemes like *SmartMove* in Brussels.[41]

Another obstacle facing the distance-based tax is its administrative cost. This has been estimated at about 10 percent[42] of the charge and could be even greater. This is much higher than the cost of the conventional modes of road financing, such as vehicle registration fees and fuel taxes, where the administrative cost amounts to less than 1 percent of revenues.[43]

Most of the less-costly solutions to applying a distance-based tax do not involve GPS and, consequently, forgo the possibility of modulated pricing that would allow traffic congestion costs to be internalized. This is a huge loss given that modulated pricing on the basis of road use to reduce traffic congestion constitutes a key benefit of a distance-based tax.[44] Although it may be true that the tax effectiveness of distance-based taxes remains low on account of their high administrative costs, they may be more economically effective than the more traditional instruments. This is because dynamic pricing, such as the system in place on Highway 407, makes for a better use of infrastructure—that is, it results in efficiency gains.[45] Cost-benefit analyses of all road-pricing schemes that integrate congestion charges yield positive results.[46] Despite consensus among economists about the efficiency of these tools (congestion charges and distance-based taxes), their implementation remains a political challenge.

40 Meloche, supra note 19.

41 SmartMove, supra note 33.

42 Benjamin Duquet, *Étude sur une éventuelle tarification kilométrique dans la région métropolitaine de Montréal et au Québec* (Montreal: Alliance Transit, 2020).

43 Robert S. Kirk and Marc Levinson, *Mileage-Based Road User Charges*, CRS Report no. R44540 (Washington, DC: Library of Congress, Congressional Research Service, 2016) (https://sgp.fas.org/crs/misc/R44540.pdf), at 4.

44 Alex Anas and Robin Lindsey, "Reducing Urban Road Transportation Externalities: Road Pricing in Theory and in Practice" (2011) 5:1 *Review of Environmental Economics and Policy* 66-88.

45 Jonas Eliasson, "Efficient Transport Pricing—Why, What, and When?" (December 2021) 1 *Communications in Transportation Research* (https://doi.org/10.1016/j.commtr.2021.100006).

46 Robin Lindsey and Georgina Santos, "Addressing Transportation and Environmental Externalities with Economics: Are Policy Makers Listening?" (October 2020) 82 *Research in Transportation Economics* (https://doi.org/10.1016/j.retrec.2020.100872).

In the Meantime: Raise Fuel Taxes

Implementing a distance-based tax is complex and takes time. Given the imbalance in the public finances of several Canadian provinces in 2024, and the imminent decline in revenues for road financing, solutions must be found for the shorter term. For now, we believe that authorities should consider raising the fuel tax. Though the number of litres of gasoline sold in Canada in 2023 was down slightly from 2019[47] and is not expected to return to pre-pandemic levels, it is also true that demand for gasoline is not expected to drop off sharply in the short term.[48] All this militates in favour of using this tax base more intensively.

CONCLUSION

Studies periodically confirm the relevance of resorting to the user pays principle when it comes to road network maintenance and development. In Canadian provinces, however, there is a growing gap between the charges borne by motorists and public expenditure on the network. This gap is currently being covered by other sources of government revenue.

Since fuel constitutes a tax base that will shrink over the coming years, new revenue sources must be found so as not to break with the principles established in this article. Among the possible solutions, a distance-based tax seems, in theory, to constitute an adequate substitute for the fuel tax. This solution stands out from the other mechanisms available, but it is relatively complex to implement. However, the technological advances that we are witnessing on various fronts should gradually lower this barrier.

The provincial governments should exercise leadership in implementing a clear plan for transitioning from the fuel tax to another mode of raising revenue. Given that a distance-based tax is the best solution, but the fixed costs of implementation are significant, it would make sense for cities and provinces to federate their initiatives. In our opinion, it would be wise also for the provincial governments to immediately begin to give serious thought to the type of pricing best suited to their purposes, because the cases that we have examined show that it takes nearly a decade of studies, pilot projects, and consultations before a solution is implemented.

Until a distance-based tax is put into effect, the growing road financing shortfall should be covered by raising fuel tax rates progressively. These increases would avoid having to rely excessively on general tax transfers and would allow financing to remain based on the principles of user pays and polluter pays. A fuel tax hike would also avoid a sharp increase in the charges borne by motorists when the shift to a distance-based tax becomes effective.

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47 Statistics Canada table 23-10-0066-01 (formerly CANSIM table 405-0002), "Sales of Fuel Used for Road Motor Vehicles, Annual (x 1,000)."

48 Canada Energy Regulator, *Canada's Energy Future 2023: Energy Supply and Demand Projections to 2050* (Ottawa: Canada Energy Regulator, 2023) (www.cer-rec.gc.ca/en/data-analysis/canada-energy-future/2023/canada-energy-futures-2023.pdf), at 56.

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Policy Forum: Comparing Canadian Output-Based Pricing Systems

Wei Cui*

PRÉCIS

Le public canadien s'attend largement à la disparition de la redevance fédérale sur les combustibles en 2025, et les politiciens et les journalistes évoquent désormais fréquemment la « tarification du carbone industriel » comme la principale ligne de défense encore en place dans le plan de réduction des émissions de gaz à effet de serre du Canada. Ce commentaire examine l'élément le plus important de cette ligne de défense, à savoir les systèmes fédéral et provinciaux de tarification fondés sur le rendement (STFR). Il rassemble des informations jusqu'ici obscures concernant trois caractéristiques de la conception des STFR : l'admissibilité, la rigueur des exigences en matière de réduction des émissions et le coût total pour les émetteurs.

L'étude constate que la mise en œuvre des STFR ne démarre pas très bien. De nombreux secteurs qui ne sont pas véritablement en concurrence avec des entreprises étrangères sont admissibles. Les provinces encouragent les installations à opter pour le STFR — c'est-à-dire à se soustraire à la tarification complète du carbone — avec peu de sélection. La plupart des provinces se contentent d'exiger des installations qu'elles réduisent lentement leurs émissions par rapport à leur rendement antérieur, au lieu de rattraper leurs homologues à faibles émissions. De plus, les installations à faibles émissions ne sont guère incitées à réduire davantage leurs émissions en raison de la faiblesse ou de l'absence de signaux de prix sur les marchés d'échange de droits d'émission.

ABSTRACT

The Canadian public widely anticipates the demise of the federal fuel charge in 2025, and politicians and journalists now frequently refer to "industrial carbon pricing" as the main line of defence still held in Canada's greenhouse gas emission reduction plan. This commentary examines the most important component of this line of defence—namely, federal and provincial output-based pricing systems (OBPS). It assembles hitherto obscure information with respect to three OBPS design features: eligibility, stringency of emission reduction requirements, and total cost to emitters.

The study finds that OBPS implementation is off to a weak start. Many sectors that do not genuinely compete with foreign firms are eligible to participate. Provinces

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encourage facilities to opt into OBPS—meaning, out of full carbon pricing—with little selection. Most provinces only require facilities to slowly reduce emissions relative to their past performance, instead of catching up to low-emission peers. And low-emission facilities face weak incentives to further reduce emissions due to weak or non-existent price signals on emissions-trading markets.

KEYWORDS: CARBON PRICING ■ EMISSIONS REDUCTION STRATEGY ■ EMISSIONS-TRADING SYSTEM ■ EMISSIONS-INTENSIVE AND TRADE-EXPOSED SECTOR ■ OUTPUT-BASED PRICING SYSTEM

CONTENTS

Introduction 78
OBPS Policy Objectives 80
Eligibility for Participation 82
The Eligibility Matrix 82
What Is EITE? 84
Stringency 85
Revenues from OBPS Regimes 90
Discussion 92

INTRODUCTION

Greenhouse gas (GHG) emissions from production processes represent a significant portion of Canada's total GHG emissions. Applying carbon pricing to incentivize emission reductions in production processes is therefore critical to achieving Canada's climate goals. At present, carbon pricing for this type of GHG emissions is mainly implemented through schemes commonly referred to as output-based pricing systems (OBPSs).[1] In essence, under an OBPS, carbon pricing is applied only to the extent that a producer's level of emissions per unit of productive output exceed a benchmark. Anyone subject to an OBPS avoids the cost of carbon pricing when it produces lower emissions per unit than the benchmark. Such partial exemption from carbon pricing, combined with increasing stringency in the applicable benchmark, creates emission reduction incentives while reducing the cost of carbon pricing for the producer. As an additional incentive, a producer can earn credits for emission reduction below the benchmark, which it can then sell to high emitters. A trading regime within each OBPS thus offers incentives for continued emission reduction, even for those already exempt from carbon pricing.[2]

A federal OBPS, introduced in the Greenhouse Gas Pollution Pricing Act, serves as a backstop where an "equivalent" provincial regime is not in place. It currently

1 In this commentary, provincial OBPSs include Alberta's Technology Innovation and Emissions Reduction (TIER) Regulation and Ontario's Emissions Performance Standards (EPS) programs.

2 Similar exemptions and opportunities for trading have long been offered in cap-and-trade regimes such as the one Quebec operates, through the free allocation and trading of emission allowances.

applies only to Manitoba, Prince Edward Island, Yukon, and Nunavut. Many provinces that implement the federal fuel charge—Alberta, New Brunswick, Newfoundland and Labrador, Nova Scotia, Ontario, and Saskatchewan—notably decided to introduce their own OBPS for industrial emissions. British Columbia also operates its own OBPS alongside its carbon tax, while Quebec's cap-and-trade system applies to both consumption and industrial emissions. This decentralized state of industrial carbon pricing both raises concerns about policy effectiveness and presents challenges to research.

Consider the pessimistic assessments made in a 2022 report from the Office of the Auditor General of Canada.[3] The report found that Environment and Climate Change Canada (ECCC) "had established weak requirements for provincial . . . large-emitter programs"[4] (referring to provincial OBPSs) and that "the department had recommended these weaker programs, which allowed some industries to benefit from larger breaks in carbon costs and would reduce the effectiveness of the carbon price."[5] For example, ECCC apparently "determined that provincial programs were sufficiently stringent so long as . . . the programs were not expected to have higher emissions than a scenario"[6] in which carbon pricing was entirely absent. ECCC did not require the provincial programs to cause emission reductions equivalent to the federal OBPS. The report notes that this lenient approach has contributed to large variations in the average cost of emissions across provinces, even within the same industries.

Contrast this with a March 2024 Canadian Climate Institute analysis,[7] which predicts that, in the coming years, provincial OBPSs—labelled in the analysis as "large emitter trading systems" or LETSs[8]—will be the largest drivers of incremental emission reduction in Canada under existing policies. The analysis declares that "climate policies are working, with industrial carbon pricing leading the pack" and that LETSs "are central to Canada's climate policy success."[9] Moreover, the Canadian Climate Institute has subsequently critiqued other analyses of the economic impact of carbon

3 Office of the Auditor General of Canada, *2022 Reports of the Commissioner of the Environment and Sustainable Development to the Parliament of Canada*, report 5, *Carbon Pricing—Environment and Climate Change Canada* (Ottawa: Office of the Auditor General of Canada, 2022).

4 Ibid., at paragraph 5.35.

5 Ibid.

6 Ibid., at paragraph 5.50.

7 Dale Beugin, Anna Kanduth, Dave Sawyer, and Rick Smith, "Which Canadian Climate Policies Will Have the Biggest Impact by 2030?" *440 Megatonnes*, March 21, 2024 (https://440megatonnes.ca/insight/industrial-carbon-pricing-systems-driver-emissions-reductions).

8 This is potentially misleading, because few OBPSs presently enjoy robust carbon markets or expect to enjoy them very soon. See Wei Cui, "Policy Forum: Are Carbon Contracts for Difference Well-Suited for Canada?" elsewhere in this feature.

9 Beugin et al., supra note 7.

pricing, claiming that they ignore variations across provincial LETSs and thereby overstate the cost of carbon pricing.[10]

Against this background, an understanding of the key features of and major variations across provincial OBPS regimes seems essential. However, provincial OBPS regimes are as obscure as they are controversial. Comparisons are hard to find. The most helpful comparisons I am aware of come from the International Carbon Action Partnership (ICAP), which treats the Canadian federal and provincial OBPSs (along with Quebec's cap-and-trade system) as emissions-trading schemes (ETSs) and summarizes them to facilitate comparisons with ETSs elsewhere in the world.[11] In this commentary, I try to provide a more nuanced comparison of provincial and federal OBPSs[12] in respect of three design features—namely, eligibility, stringency of emission reduction requirements, and total cost.[13]

After a brief statement of the overall purpose of an OBPS, the commentary examines, in turn, these features and policy questions associated with them. I offer a summary assessment at the end by referring to the recent controversy regarding the distribution analysis of Canadian carbon pricing by the Parliamentary Budget Office (PBO).

OBPS POLICY OBJECTIVES

Carbon pricing, whether applied to emissions from production or from consumption, forces producers and consumers to internalize the social cost of carbon emissions and creates broad incentives for emission reduction. However, one can maintain incentives for emission reduction while minimizing the private cost of carbon pricing by exempting a portion of emissions (for example, emissions unavoidable at a given time because of technology constraints). The desire to reduce producers' private cost of carbon pricing typically stems from two considerations.[14] First, when some jurisdictions (provinces or countries) impose higher prices on carbon emissions than others, production (and emissions) may relocate to jurisdictions with lower carbon prices.

10 Dave Sawyer, Sam Harrison, and Jotham Peters, "Industrial vs. Consumer Carbon Pricing: A Cost Comparison," *Canadian Climate Institute*, September 13, 2024 (https://climateinstitute.ca/industrial-vs-consumer-carbon-pricing-cost-comparison).

11 International Carbon Action Partnership, "ICAP ETS Map" (2024) (https://icapcarbonaction.com/en/ets).

12 I leave out Quebec's cap-and-trade system from the comparison both because its mechanisms are different from an OBPS and because, being longer established and integrated with the emissions market in California, it generates fewer policy concerns regarding strategic exemptions from carbon pricing.

13 I discuss the design of carbon credit trading, and the question of whether genuine price signals will emerge from Canadian OBPSs, in Cui, supra note 8.

14 Aside from deadweight loss from distortions of production decisions, carbon pricing represents private costs because it only generates transfers to the government from a social perspective.

This relocation undermines the emission reduction objective if the emission intensity of production is higher elsewhere (the leakage consideration). Second, higher private costs from carbon pricing also can make producers of traded goods less competitive on the international market (the competitiveness consideration), worsening national welfare from the perspective of individual countries.

Canada's federal and provincial OBPSs, which implement partial exemptions from carbon pricing, generally rely on the leakage and competitive rationales. However, these rationales are not beyond dispute. Consider bitumen extraction from oil sands, which is among the most polluting methods of producing oil.[15] If Canadian oil sand production declines because of carbon pricing, oil production may increase elsewhere in the world. But if, on average, such additional oil production elsewhere is less emissions-intensive than extraction from oil sands, the world is better off precisely *because* production moves from Canada to elsewhere. The relatively high emission intensity of Canadian oil production moots the leakage argument.

Similarly, how carbon pricing affects competitiveness on the international market is complex. Competitiveness concerns are usually regarded as strong for emissions-intensive, trade-exposed (EITE) sectors, but the fact that a sector is trade-exposed does not necessarily imply that the international market is competitive. For example, electricity is traded across the American and Canadian borders, but the utilities on both sides are regulated monopolies, and the volume of electricity trade depends much more on whether a local utility is able to meet local demand than on prices. Inferring "competition" from the trade exposure of electricity is a stretch. One major deviation of Canadian OBPSs from ETSs in the European Union and elsewhere is that they cover electricity generation. The implied classification of the electricity sector as EITE would raise eyebrows for outside observers.

Overall, when carbon pricing is generally in place, an OBPS stands for (partial) exemption from carbon pricing and *lower* incentives for emission reduction. In this light, consider the claims made by the Canadian Climate Institute (cited above) that LETSs will be the largest driver of incremental emission reduction in Canada and that fuel charges play a much smaller role. These claims are less informative than they may appear. For one, the oil and gas sector contributes the most to Canada's stubbornly high level of emissions. *Any* regime that incentivizes emission reductions in this sector will probably be the biggest driver in overall Canadian emission reduction. This does not show that the current carbon-pricing regimes for oil and gas—provincial OBPSs—are well designed. Moreover, the fact that the fuel charge makes a relatively small contribution to total emission reduction is purely a function of how much is carved out of it by OBPSs—especially industrial fuel use. It is not an intrinsic feature of fuel charge design itself.

15 Megan He et al., "Total Organic Carbon Measurements Reveal Major Gaps in Petrochemical Emissions Reporting" (2024) 383:6681 *Science* 426-32.

ELIGIBILITY FOR PARTICIPATION

Participation in the federal or a provincial OBPS can be either mandatory or voluntary. The obligation of, or eligibility for, either type of participation may also depend on the annual emissions of a facility, its sector or product, or a combination of both. This leads to a surprisingly complex matrix—laid out in table 1 below—for the basic task of just comparing participation criteria across systems.

The Eligibility Matrix

What explains this complexity? If an OBPS represents an exemption from carbon pricing, then emitters will have incentives to join the OBPS if it imposes significantly lower costs than fuel charges. From this perspective, there is no need for *mandatory* participation. However, an OBPS is also a way of implementing carbon pricing: emissions above the relevant benchmark will attract costs at the carbon price (or lower prices at which emission allowances, permits, or credits are traded). If, say, the fuel charge is suspended federally or provincially, but OBPSs continue, mandatory participation in an OBPS retains some carbon pricing. The possibility that "industrial carbon pricing" needs to be a stand-alone institution without broader carbon pricing thus seems necessary to rationalize mandatory OBPS participation.

Canadian OBPS regimes use two types of criteria to determine mandatory participation. The first is the size of the emitter, defined in terms of tonnes of carbon dioxide equivalent (tCO_2e) annual emissions. In both the federal and all provincial OBPSs, participation is mandatory for large emitters; however, the definition of "large" varies, as can be seen in column 2 of table 1. A second type of criteria is the nature of the emitter's business. Again, as a benchmark, participation in the federal OBPS is mandatory only for emitters engaged in an enumerated category of industrial activities. These are delineated (presumably) to reflect the leakage and competitive concerns motivating exemptions from carbon pricing. British Columbia, which has the lowest size threshold, imposes a similar condition in that only facilities producing specifically regulated products face mandatory participation. By contrast, Alberta imposes *no* sector or product conditions on mandatory participation, even though it imposes the highest size threshold.

Other provinces come closer in substance to Alberta than to British Columbia. New Brunswick, Newfoundland and Labrador, and Nova Scotia, for example, define "industrial facility" to include broadly any facility engaged in (1) manufacturing and processing; (2) mining, quarrying, and oil and gas extraction; or (3) electricity generation, regardless of whether its sector or product is EITE. Saskatchewan takes a similar approach. Ontario, although it enumerates more specific categories of regulated sectors, also broadly includes most manufacturing activities. Emitter size is therefore likely the most important determinant of mandatory participation in these provinces.

Canadian OBPSs also adopt a mixture of size requirements and sector and product requirements to determine eligibility for *voluntary* participation. Since firms would opt in to an OBPS only when the cost of carbon pricing is lower under the OBPS, one

TABLE 1 Criteria for Mandatory or Voluntary Participation in OBPS Regimes

	Mandatory participation		Voluntary participation	
	Size requirement	Sector/product requirement	Size requirement	Sector/product requirement
Federal	$\geq$ 50,000 tCO_2e/year in 2014 or after	Enumerated industrial activities	$\geq$ 10,000 tCO_2e/year in 2017 or after	Enumerated industrial activities
Alberta	$\geq$ 100,000 tCO_2e in or after 2016, or have imported $>$ 10,000 tonnes of hydrogen in or after 2023	None	Emit $>$ 2,000 tCO_2e annually	In an EITE sector
			None	Compete against a facility regulated under TIER or owners/operators of multiple small conventional oil and gas facilities (can opt in as an aggregate facility)
British Columbia	$\geq$ 10,000 tCO_2e/year	Regulated products	None	Produce a regulated product
Ontario	$\geq$ 50,000 tCO_2e/year in 2014 or after	Enumerated industrial activities	$\geq$ 10,000 tCO_2e/year	Engage in a regulated industrial activity
Saskatchewan	Industrial facilities $>$ 25,000 tCO_2e/year and electricity facilities $>$ 10,000 tCO_2e/year	Industrial or electricity facility	None	Sector covered by OBPS program or demonstrate that they operate in an EITE sector
New Brunswick	$\geq$ 50,000 tCO_2e/year in 2015 or after	Industrial facility	$>$ 10,000 tCO_2e/year	Industrial facility
Newfoundland and Labrador	$\geq$ 25,000 tCO_2e/year in 2016 or after	Industrial facility	$>$ 15,000 tCO_2e/year	Industrial facility
Nova Scotia	$\geq$ 50,000 tCO_2e/year in 2023 or after	Industrial facility	$\geq$ 10,000 tCO_2e/year	Industrial facility

would expect voluntary participation in an OBPS to be subject to meaningful restrictions. Here, the federal and most provincial OBPSs tend to adopt the same sector and product conditions as for mandatory participation, ranging from the more restrictive (federal and British Columbia) to the more lenient (that is, covering most or all industrial and electricity-generating activities). Alberta, which does not have a sector or product condition for mandatory participation, requires anyone that wishes to opt in to the TIER program either (1) to be in an EITE sector and emit 2,000 tCO_2e or more annually, (2) compete against a facility regulated under TIER,[16] or (3) operate multiple small conventional oil and gas facilities.

A minimum size threshold for voluntary participation has less obvious justifications. One rationalization is that if a facility's emissions are sufficiently low, the private cost savings from an OBPS may outweigh the marginal administrative cost of admitting an additional participant.[17] Therefore, the lower such marginal administrative costs, the lower the size threshold for voluntary participation should be.[18] Notably, British Columbia imposes no size threshold for voluntary participation, and Saskatchewan removed a previous 10,000 tCO_2e/year threshold in 2022. Similarly, Alberta imposes a relatively low size threshold for facilities in EITE sectors to opt in.

What Is EITE?

It is useful to consider how different OBPSs explicitly define EITE sectors.[19] The federal EITE criteria measure "emission intensity" using the full carbon-pricing costs of a sector divided by the gross value added for the sector. The "trade exposure" of a sector is determined by the ratio of (1) the total dollar value of end products exported from or imported into the sector to (2) the total dollar value of end products produced by or imported into the sector. Any sector is deemed to face medium or high EITE risk (that is, it is an EITE sector) if it has (1) emission intensity ≥ 1 percent and trade exposure ≥ 10 percent, (2) emission intensity ≥ 3 percent, or (3) trade exposure ≥ 80 percent.[20]

16 Here we see an instance of "exemption creep": exempting some facilities on purported competitive grounds may lead to exempting other facilities by virtue of purported competition with the first set of exempted facilities.

17 The facility would presumably, on its own, balance its carbon-pricing cost savings from participation against the compliance costs of the OBPS.

18 An alternative rationale is that carbon leakage is less of a concern for small emitters.

19 EITE is relevant not only for participation eligibility, but also, as we will see below, for regulatory stringency.

20 Environment and Climate Change Canada, *The Policy Regarding Voluntary Participation in the Output-Based Pricing System* (Gatineau, QC: Environment and Climate Change Canada, 2024), appendix A. In determining eligibility for voluntary participation in Alberta's TIER program, EITE sectors are defined explicitly in the same way as they are in the federal criteria. Technology Innovation and Emissions Reduction Regulation, Alta. Reg. 133/2019, section 4.

Compare this with the European Union's current definition of EITE sectors (which are eligible for the allocation of free allowances under the EU ETS):[21] a sector is EITE if (1) the direct and indirect costs induced by carbon pricing increase production costs by at least 5 percent of gross value added, and (2) the sector's trade intensity with non-EU countries (imports and exports) is above 10 percent. A sector or subsector is also deemed to be exposed if (1) the sum of direct and indirect additional costs is at least 30 percent, or (2) the non-EU trade intensity is greater than 30 percent. At least in terms of emission intensity, therefore, the Canadian federal criteria for EITE sectors are more expansive.

Ontario appears to have adopted an even weaker definition of EITE.[22] Trade exposure of greater than or equal to 10 percent is sufficient to classify a sector as medium or high risk. Before 2022, a high-risk sector was one where emission intensity—defined as emissions (tCO_2e) over value added in millions of dollars—exceeded 1,000. In 2022, Ontario proposed two alternative emission intensity measures: (1) the direct carbon cost as a share of *revenue* (not of value added), or (2) the estimated ratio of direct and indirect carbon costs to the industry's gross value added (GVA). On the first measure, any sector with emission intensity ≥ 3 percent is deemed EITE. On the second measure—which is more similar to the federal criteria—if the direct and indirect carbon cost to GVA ratio exceeds 3 percent, the sector is EITE, again regardless of its degree of trade exposure.

Other provinces, such as British Columbia and Saskatchewan, have not recently published general criteria for selecting products and sectors for OBPS. In Nova Scotia, a definition of EITE is used to identify sectors that benefit from slower increases in emission stringency standards. However, the regulation uses a puzzling definition of emission intensity: it is obtained by dividing the "direct emissions of the *regulated facility*" (emphasis added)—presumably measured in tCO_2e—by the "gross value added for the *sector*" (emphasis added), presumably measured in dollars, and this supposedly would result in a percentage.[23]

STRINGENCY

Once regulated by an OBPS, a firm's emission reduction incentives depend on the stringency of the performance standard it faces: a lax standard—that is, a high benchmark emission intensity—means that the firm will have less emissions subject

21 European Commission, "Carbon Leakage" (https://climate.ec.europa.eu/eu-action/eu-emissions-trading-system-eu-ets/free-allocation/carbon-leakage_en).

22 Ontario, Emissions Performance Standards Program, *Proposed Regulatory Amendments for Emissions Performance Standards Program 2023-2030* (Toronto: EPSP, 2022) (https://prod-environmental-registry.s3.amazonaws.com/2022-08/Proposed%20Regulatory%20Amendments%20for%20EPS%20Program%202023-2030.pdf).

23 Nova Scotia, Environment and Climate Change, *Output-Based Pricing System Reporting and Compliance Standard* (Halifax: Environment and Climate Change, 2023), at 19, paragraph 5.3(6) (https://climatechange.novascotia.ca/sites/default/files/uploads/output-based-pricing-system-reporting-and-compliance-standard.pdf).

to carbon pricing or more emission reduction credit to sell. Canadian OBPSs vary significantly in terms of how the emission standard is set and how fast stringency tightens (see table 2).

The federal OBPS generally adopts sector-based emission standards.[24] A further "reduction factor" of 80 percent, 90 percent, or 95 percent is applied to the average intensity to arrive at the standard for a sector or product. The choice of reduction factor depends on whether the sector or product faces "elevated risks" of leakage and competitiveness impacts. Since 2023, a further "tightening rate" is applied: a 2 percent fixed annual percentage reduction in most output-based standards is required. For a few sectors with "very high" EITE risk—cement, lime, petrochemicals, iron and steel and certain aluminum, and organic basic chemicals—a 1 percent tightening rate applies.[25] Notably, the tightening rates apply to industrial process emissions, where reductions are commonly claimed to be difficult to achieve. By contrast, provincial OBPSs tend not to impose a reduction target on such emissions.[26]

For 19 specifically listed sectors and products, the federal OBPS also uses facility-specific standards.[27] Such standards are also relevant for facilities that opt in to the OBPS: there may not be enough opt-in facilities in the same sectoral or product segment to develop a general standard. Reduction factors apply to facility-specific standards just as they do to sectoral standards, but tightening rates apparently do not.[28]

The federal approach can be contrasted with several provincial approaches. The BC OBPS sets standards for regulated operations by reference to provincial production-weighted average emission intensities. British Columbia also employs the concept of a reduction factor: the factor applicable to most products is 65 percent, though it is higher for a few products.[29] In the meantime, the tightening rate is 1 percent per year. In other words, British Columbia has more stringent standards at the outset than the federal OBPS standards, but stringency increases at a slower pace.

Alberta's TIER program is even more different from the federal OBPS; Alberta applies "facility-specific benchmarks" that refer to a regulated facility's historical

24 These start with the "production-weighted average emissions intensity" of all large emitter facilities producing similar products across Canada.

25 Due to purported uncertainties relating to the interaction between the OBPS and the proposed Clean Electricity Regulations, no tightening rate is applied to the generation of electricity using fossil fuels.

26 For extensive discussion, see Environment and Climate Change Canada, *Review of the OBPS Regulations: Consultation Paper* (Gatineau, QC: Environment and Climate Change Canada, 2021) (www.canada.ca/en/environment-climate-change/services/climate-change/pricing-pollution-how-it-will-work/output-based-pricing-system/2022-review-consultation.html).

27 See Output-Based Pricing System Regulations, SOR/2019-266, section 37. See also ibid., at schedule 1.

28 See ibid., at section 37. Contrast with the use of tightening rates in ibid., at sections 36 and 36.2.

29 These factors are 80 percent for copper mining; 85 percent for lead-zinc smelting; 90 percent for cement, chemical processing, and lime products; and 95 percent for aluminum smelting.

TABLE 2 Comparing Stringency of OBPS Standards

	Nature of standard	Increasing stringency	Special exemptions
Federal	Mainly sector-based	"Reduction factor" of 80% (90% or 95% for products facing "high risk") Annual tightening rate 2% (1% for products facing "high risk")	No exemption for industrial process emissions from tightening rate
Alberta	Mainly facility-based	Reduction (from 2013 to 2015 intensity) of 12% by 2022 Annual tightening rate of 2% after 2022	Industrial process emissions exempt from tightening
British Columbia	Mainly sector-based	Reduction factor of 65% (higher for select products) Annual tightening rate of 1%	Industrial process emissions exempt from tightening
Ontario	Mainly facility-based	Relative to a 2022 baseline, 2.4% in 2023 and 1.5% per year from 2024 to 2030	No exemption for industrial process emissions from tightening rate
Saskatchewan	Facility-based other than electricity	Annual reduction of 1.67% for oil and gas, 1.25% for others	No exemption for industrial process emissions from tightening rate
New Brunswick	Facility-based other than electricity	Annual reduction of 1%	Industrial process emissions exempt from tightening
Newfoundland and Labrador	Mainly facility-based	Annual reduction of 2%	Industrial process emissions exempt from tightening
Nova Scotia	Facility-based other than electricity	Annual reduction of 1% for EITE sectors, 1.5% for others	Industrial process emissions exempt from tightening

emission intensity. The program requires a 2 percent annual reduction for 2023 and beyond. Sector-based benchmarks are relevant only to low emitters: they can choose to use a "high-performance benchmark" based on the average emission intensity of the top-performing 10 percent of facilities for a given sector or product if such a benchmark is more lenient.[30] TIER's predecessor industrial pricing regime in Alberta actually used product-specific benchmarks, but this was abandoned other than for power generation facilities. Thanks to facility-specific benchmarks, the emission intensity standards to which Alberta oil sands facilities are subject can vary by a full order of magnitude. The worst performing facility can have three or even five times the emission intensity described in high-performing benchmarks.[31]

Ontario also mainly adopts facility-specific standards under its EPS program. A 2023-24 policy consultation announced the government's intention to transition to broader applications of sector-based standards,[32] but both the design of such standards and the timeline of such a transition were deferred for future discussion. Under the current EPS regime, sector-based standards apply only in a subset of industries[33] relating to specific cement, iron and steel, petroleum, ammonia, and other commodity products; electricity generation; and thermal energy cogeneration. All other facilities use facility-specific standards.[34] A "stringency factor," requiring annual reductions of 1.5 percent from 2024 through 2030, applies to both "fixed process" and "non-fixed process" emissions, in line with the federal approach of not exempting industrial process emissions from increased stringency.

Saskatchewan adopts facility-specific standards for all regulated entities except the electricity generation sector.[35] The only general requirement is for facilities to reduce their individual emission intensities by 20 percent (oil and gas) or 15 percent

30 Newfoundland and Labrador is another province that offers a sector benchmark option (see Letter from Deputy Minister Valerie Snow to Deputy Minister Christine Hogan (Government of Newfoundland and Labrador, Environment and Climate Change, "Re: Carbon Pricing System Assessment Against 2023-2030 Federal Benchmark," letter to Deputy Minister, Environment and Climate Change Canada, September 2, 2022 (www.gov.nl.ca/ecc/files/Carbon-Pricing-Systems-Federal-Benchmark-NL-Response-Detailed.pdf).

31 Emma Dizon and Grant Bishop, *Strengthening TIER for Alberta's Low-Carbon Growth: Measuring Credit Oversupply Risks in Alberta's Carbon Market* (Toronto: Clean Prosperity, 2024).

32 Ontario, Regulatory Amendments To Clarify Program Requirements and Improve Program Efficiency for Emissions Performance Standards (EPS) and GHG Reporting Programs, Ontario notice, ERO number 019-7649 (https://ero.ontario.ca/notice/019-7649).

33 See Ontario, Ministry of the Environment, Conservation and Parks, "GHG Emissions Performance Standards and Methodology for the Determination of the Total Annual Emissions Limit" (March 2024), at 7-14, methods A-C (https://prod-environmental-registry.s3.amazonaws.com/2024-04/GHG%20EPS%20and%20Methodology%20for%20determination%20of%20TAEL_March%202024%20(EN)_1.pdf).

34 See, ibid., at 15-40, methods D-G.

35 The Management and Reduction of Greenhouse Gases (Standards and Compliance) Regulations, RRS c. M-2.01, reg. 3, section 11.

(all other sectors) linearly over a 12-year period. Similar practices are found in Newfoundland and Labrador, New Brunswick, and Nova Scotia.

Finally, note that a tightening factor can play two different roles. First, it may simply be a regulatory tool, setting the targets for continued emission reductions. The ambition of 20 percent emission reduction over a 10-year horizon converts to a reduction factor of 2 percent per year. Viewed this way, the relative uniformity of tightening factors in Canadian OBPSs may be attributed to the federal government setting the emission reduction ambition and provinces following its lead. In this spirit, one can compare Canada's emission reduction ambitions with those adopted elsewhere: in 2023, for example, the European Union increased the annual "linear reduction factor" in its ETS to 4.3 percent (4.4 percent from 2028).[36]

A second role of the tightening factor is price maintenance in emissions trading markets. As facilities reduce emissions, fewer will need to fulfill compliance obligations by purchasing emission credits from others, and more facilities will have emission credits to sell. The increasing supply of and diminishing demand for emission credits will depress their price, which erodes emission reduction incentives below the benchmark. Tightening performance standards can help balance the supply and demand of emission credits. When the federal OBPS introduced its 2 percent tightening rate in 2023, the goal of "ensuring a robust market for credits" was emphasized.[37] And one criterion that the federal government uses to assess the adequacy of provincial OBPSs is whether they ensure that "there is net demand for credits; that is, the total compliance obligation must exceed the total credits available."[38]

Viewing the tightening factor as a price-maintenance tool, however, implies that it needs to be adjusted in light of other factors that affect the market price of emission credits. For example, if "offset credits" (credits for emission reduction other than those earned under an OBPS) are introduced into an OBPS trading market, they depress the price of earned credits, which in turn may create pressure to increase the tightening rate.[39] Moreover, since the robustness of price signals on emission markets can be affected by many different factors (including what other price-maintenance tools are used), there is no reason to expect tightening factors to be as uniform as is now observed in Canada.

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36 European Union, Directive (EU) 2023/959 of the European Parliament and of the Council of 10 May 2023 amending Directive 2003/87/EC Establishing a System for Greenhouse Gas Emission Allowance Trading Within the Union and Decision (EU) 2015/1814 Concerning the Establishment and Operation of a Market Stability Reserve for the Union Greenhouse Gas Emission Trading System, OJ L 130, May 16, 2023.

37 See especially Environment and Climate Change Canada, supra note 26, at section 3.1.1.3.

38 Ibid.

39 For an example of provincial deliberation regarding the trade-off between introducing offset credits and increasing the tightening rate, see Government of Saskatchewan, "Saskatchewan Output-Based Performance Standards Program 2023: Discussion Paper" (2022) (https://pubsaskdev.blob.core.windows.net/pubsask-prod/133800/Saskatchewan%252BOBPS%252BProgram%252BDiscussion%252BPaper.pdf).

REVENUES FROM OBPS REGIMES

Under both full carbon pricing and a regulatory approach to emission reduction, production costs increase because polluters need to implement costly abatement. Full carbon pricing imposes a further private cost on the polluter: even when carbon pricing and regulation secure the same level of emission reduction, the polluter still has to make payments to the government for remaining emissions under carbon pricing.[40] OBPS mitigates this private cost by allowing emissions below the performance standard to go unpriced. Further, it reduces the abatement cost of some polluters by rewarding them with proceeds from the sale of emission credits.

Information about the revenue raised by OBPS regimes does not capture the amount of private savings relative to the full carbon-pricing alternative. Nor does it capture the social gains from more efficient allocation of abatement efforts through emissions trading. However, for a given level of emission reductions, it may reflect differences in private costs between a purely regulatory approach and a carbon-pricing approach.

Table 3 lays out the limited information now available on revenue raised by Canadian OBPS regimes. Only four regimes have disclosed such information. Alberta's TIER system currently raises more than half a billion dollars per year. More interesting, however, is the large fluctuation in TIER revenue—a $300 million, or 35 percent, drop—from 2022 to 2023. This was solely the result of greater use of emission offsets and emission performance credits in 2023 relative to 2022: the total level of priced emissions was the same during both years.[41] Another large fluctuation—a 10-fold revenue increase from 2022-23 to 2023-24—is observed in Saskatchewan. This is explained by the expansion of its OBPS to the electricity generation sector.[42]

40 See Michael Keen, Ian Parry, and James Roaf, "Border Carbon Adjustments: Rationale, Design and Impact" (2022) 43:3 *Fiscal Studies* 209-34 (https://doi.org/10.1111/1475-5890.12307). This is purely a private cost, because the payment merely represents a transfer from a social perspective. In contrast, the cost of abatement is both a private and a social cost.

41 Government of Alberta, "Alberta Industrial Greenhouse Gas Compliance, Summary of 2023 Compliance Results under the Technology Innovation and Emissions Reduction (TIER) Regulation" (https://open.alberta.ca/dataset/c0cb77ca-fac0-4171-89af-0048e2189120/resource/daa8cc55-c35b-40d6-9c75-1e030df36450/download/epa-alberta-industrial-greenhouse-gas-compliance-2023.pdf).

42 See Saskatchewan, Ministry of Environment, *Annual Report 2023-2024* (Regina: Ministry of Environment, 2024). The $336.3 million in 2022-23 represents OBPS payments from the electricity sector alone. For 2024-25, it has been reported that $326.3 million of the $351.3 million budgeted OBPS revenue comes from the electricity sector. Alec Salloum, "Sask. Expects $351.3M from Provincial Carbon Tax in 2024-25," *Regina Leader-Post*, April 3, 2024 (https://leaderpost.com/news/saskatchewan/sask-expects-351-3m-from-provincial-carbon-tax-in-2024-25).

TABLE 3 Information on Revenue from OBPS Regimes

	Revenue from OBPS (latest years)	Claim of cost saving relative to federal OBPS
Federal	Not available	na
Alberta	$864 million (2022) $564 million (2023)	
British Columbia	na (OBPS new in 2024)	
Ontario	$131 million (forecasted for 2023)[a]	$1.1 billion for the 2023-2030 period[b]
Saskatchewan	$29.3 million for 2022-23 > $336.3 million for 2023-24 $351.3 million budgeted for 2024-25	$3.7 billion for the 2023-2030 period[c]
New Brunswick	na	Federal collection was $25.9 million for the 2019-2022 period[d]
Newfoundland and Labrador	na	
Nova Scotia	$185,800 (2022)[e]	

a Mike Crawley, "Ontario Now Has a Carbon Tax on Industry. What Will Doug Ford's Government Do with the Revenue?" *CBC*, January 11, 2023 (www.cbc.ca/news/canada/toronto/ontario-industrial-carbon-pricing-emissions-performance-standards-1.6709624).

b Ontario, *Emissions Performance Standards (EPS) Program Regulatory Amendments for the 2023-2030 Period* (Toronto: EPSP, 2022) (https://ero.ontario.ca/notice/019-5769).

c Saskatchewan, Ministry of Environment, *Annual Report 2022-2023* (Regina: Ministry of Environment, 2023), at 4.

d Environment and Climate Change Canada, "Output-Based Pricing System Proceeds Fund" (www.canada.ca/en/environment-climate-change/services/climate-change/carbon-pollution-pricing-proceeds-programming/output-based-pricing-system-proceeds-fund.html).

e Government of Newfoundland and Labrador, "Management of Greenhouse Gas Act Legislative Review 2016-2022" (www.gov.nl.ca/ecc/files/Management-of-Greenhouse-Gas-Act-Legislative-Review-2016-2022.pdf).

Saskatchewan's heavy reliance on coal for electricity generation[43] may explain the magnitude of its OBPS revenue: $350 million (for 2024-25). By contrast, Ontario projected just $131 million of revenue for 2023, even though its economy is 10 times larger than Saskatchewan's.

Finally, in promoting their OBPS programs, at least two provinces made estimates of how much private saving was achieved when they prevented the federal OBPS from applying. Ontario projected $1.1 billion of such savings over an eight-year period, which means that its OBPS imposes half the cost of the federal OBPS. Likewise, Saskatchewan estimated a cost saving of $3.7 billion over the eight-year period, implying a cost reduction from the federal OBPS of almost 60 percent.

43 Energy Rates, "The Main Electricity Sources in Canada by Province" (https://energyrates.ca/the-main-electricity-sources-in-canada-by-province).

DISCUSSION

The foregoing examination of Canadian OBPS regimes sheds light on the recent controversy generated by a 2023 PBO study.[44] The study was intended to provide an update of its 2022 "Distributional Analysis of Federal Carbon Pricing."[45] Both studies, employing similar methodologies, found that Canadian carbon pricing will have an overall negative impact on the Canadian economy,[46] reducing Canadian gross domestic product in 2030, for example, by 1.3 percent. However, the 2023 study initially purported to analyze only the federal *fuel charge*: this is a different goal from the 2022 study, which analyzed the impact of "carbon pricing." The different goal of the 2023 study would have dictated that the PBO isolate the economic impact of the federal fuel charge, instead of quantifying the joint (and larger) impact of the fuel charge and OBPS regimes. The PBO failed to do this. In 2024, the PBO came under criticism for "exaggerating" the negative effect of the federal fuel charge, and for implicitly (under the guise of impartial policy analysis) supporting the ascendant anti-carbon-pricing political rhetoric in Canada. Critics have further asserted that the magnitude of the PBO's estimated negative impact of carbon pricing is implausible.[47]

The analysis in this commentary suggests three rejoinders to these critiques. First, although the PBO has revised its 2023 study to quantify the economic impact of the federal fuel charge alone,[48] it is not clear that separating the two components of Canadian carbon pricing is meaningful. Fundamentally, OBPS regimes represent carveouts from comprehensive carbon pricing. OBPS regimes without carbon pricing in the background would be quite difficult to interpret. The OBPS carveout is mostly (if poorly) justified on the basis of protecting EITE sectors. Such a policy can be implemented in different ways—for example, through free allowances under ETS regimes. It is unnecessary (as well as impossible) to distinguish between consumer and industrial carbon prices. For this reason, it is also conversely difficult to make sense of the Canadian federal fuel charge as a stand-alone policy instrument. It is defined as much by what is carved out of it as by what it covers.

Second, in modelling the joint impact of OBPS and the federal fuel charge on the Canadian economy, the PBO used a hypothetical "federal-equivalent" OBPS. Especially given the numerous introductions of and changes to provincial OBPSs since 2023, this seems quite reasonable. However, as we have seen, several provincial OBPS

44 Office of the Parliamentary Budget Officer, *A Distributional Analysis of the Federal Fuel Charge Under the 2030 Emissions Reduction Plan* (Ottawa: PBO, 2023).

45 Office of the Parliamentary Budget Officer, *A Distributional Analysis of Federal Carbon Pricing under A Healthy Environment and A Healthy Economy* (Ottawa: PBO, 2022).

46 Both reports explicitly indicate that they do not attempt to account for the economic and environmental costs of climate change: carbon pricing in Canada alone will not stop climate change, making it impossible to quantify the climate benefit of Canadian carbon pricing.

47 See Sawyer et al., supra note 10.

48 Office of the Parliamentary Budget Officer, *A Distributional Analysis of the Federal Fuel Charge—Update* (Ottawa: PBO, 2024).

regimes were designed explicitly to reduce (substantially) the cost on industry of carbon pricing. Participation in OBPS regimes was significantly expanded in all provinces relative to federal OBPS design. Stringency targets were lowered in most provincial regimes, and none introduced more stringent targets. All these factors suggest substantially diminished incentives for emission reduction. And, at least in their major design features,[49] there is no indication that provincial OBPS regimes achieved any innovation to compensate for their weakening of incentives through scope and stringency.

In other words, if most of the negative impact of carbon pricing on the Canadian economy the PBO projects is attributable to the "federal-equivalent" OBPS, then its projection is too *optimistic*, in that it assumes a much stronger set of incentives for emission reduction than is actually offered through provincial OBPSs. In reality, such incentives have already been undermined. The negative impact of (hypothetically robust) carbon pricing is simply the flip side of this illusion. Ironically, those who called on the PBO to give a "truer" estimate of the costs of carbon pricing effectively demanded *two* layers of fiction: on top of the fiction that OBPS regimes' emission reduction incentives have not been eroded by the provinces, it asks for a further stretching of the imagination by portraying the fuel charge as a stand-alone instrument that may be repealed.

Third, some critics of the PBO analysis have suggested that the PBO should assume that business costs will be reduced by superior technology, cheaper alternatives to paying the carbon price through purchasing emission credits, returning OBPS revenue entirely to businesses, additional government subsidies, and "regional differentiation" in business-friendly rules for participation and stringency.[50] There is no question that adopting different modelling assumptions could substantially change the estimated economic impact of OBPS regimes. But there is little reason to think that many of these alternative policy parameters represent good OBPS design, or that, in an environment with weak emission reduction incentives, superior technologies will simply miraculously emerge.

The basic idea of carbon pricing is that reducing GHG emissions sufficiently to save the planet will require very costly changes to our lives, and using price signals is the *least* costly way to pursue such reduction. Perpetuating the illusion that "carbon pricing should hardly cost us anything at all" undermines public understanding of this basic rationale. The objections to the PBO analysis seem to reflect an unfortunate drift of our policy discourse in this direction. Together with the listless unfolding of provincial OBPSs, such drift hardly brightens the outlook for Canadian climate policy.

49 Because provincial OBPS regimes inherently shrink the size of the emissions trading markets, many are less likely to support robust price signals. Emissions trading under provincial OBPSs is considered in Cui, supra note 8.

50 Sawyer et al., supra note 10.

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Policy Forum: Are Carbon Contracts for Difference Well Suited for Canada?

Wei Cui*

PRÉCIS

Au moins jusqu'à la publication du budget fédéral 2024, de nombreux politiciens canadiens, groupes de réflexion sur la politique climatique et groupes industriels encourageaient l'usage des contrats sur différence pour le carbone (CDC) en complément de la tarification du carbone. Ce commentaire invite à la prudence face à l'adoption généralisée des CDC. L'auteur commence par observer que la conception actuelle des systèmes provinciaux de tarification fondés sur le rendement (STFR) n'est pas compatible avec l'attente de systèmes délivrant des signaux de prix robustes. Il affirme que les CDC dépendent de ces signaux de prix et qu'ils ne constituent pas une politique viable pour encourager l'émergence de tels signaux. L'auteur affirme ensuite qu'il est difficile de justifier que le gouvernement parie contre lui-même sur la « politique de tarification » du carbone. Une abondante littérature spécialisée s'oppose depuis longtemps à ce que l'on fournisse aux entreprises une « certitude » quant aux changements politiques futurs en général, et il n'y a guère de raison de penser que la tarification du carbone soit différente à cet égard. L'auteur conclut que, dans l'ensemble, l'utilisation des CDC devrait rester étroitement ciblée.

ABSTRACT

At least up to the release of the federal 2024 budget, many Canadian politicians, climate policy think tanks, and industry groups promoted carbon contracts for difference (CCfD) to complement carbon pricing. This commentary urges caution against the broad adoption of CCfDs. The author begins by noting that the current designs of provincial output-based pricing systems (OBPS) are not consistent with the expectation of the systems delivering robust price signals. He argues that CCfDs depend on such price signals, and they are not a plausible policy for encouraging the emergence of such signals. The author then argues that it is hard to justify the government making a bet against itself on the "policy price" of carbon. An extensive scholarly literature has long argued against providing businesses with "certainty" against future policy changes in general, and there is little reason to think carbon

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pricing is relevantly different. The author concludes that, overall, the use of CCfDs should remain narrowly targeted.

KEYWORDS: CARBON CONTRACT FOR DIFFERENCE ■ CARBON PRICING ■ CLIMATE CHANGE ■ EMISSIONS-TRADING SYSTEM ■ OUTPUT-BASED PRICING SYSTEM ■ POLICY CERTAINTY

CONTENTS

Introduction 96
The Bane of Fragmented Carbon Markets 98
When Should Governments Compensate for Policy Changes? 101
The Wisdom of Keeping CCfDs Narrowly Targeted 104

INTRODUCTION

Over the last two years, a seemingly obscure, wonkish idea has gained surprising popularity among Canadian politicians, climate policy think tanks, and industry groups: carbon contracts for difference (CCfD). Very abstractly speaking, a CCfD is a contract issued by the government to private parties that insures against a change in the announced path for future carbon prices. This concept can be implemented in various ways, but one example would be a contract that guarantees the counterparty that any emission reductions the latter achieves would have a specific cash value (for example, $100 per tonne). For firms whose future revenue streams depend on the carbon price, CCfDs can remove uncertainty regarding future cash flow attributable to fluctuations in the carbon price.

The federal government first mentioned the idea of CCfDs in the 2022 fall economic statement as one of the offerings that would be available through the Canada Growth Fund (CGF). The CGF is a public investment vehicle launched in 2022 to attract private capital to build Canada's clean economy.[1] By the time Budget 2024 was released, there was reportedly already "substantial demand from industry and other stakeholders for [CCfDs] as a tool to . . . [provide] certainty around carbon pricing."[2] Budget 2024 suggests that the CGF "will continue offering bespoke CCfDs . . . with a focus on provinces contributing significantly to . . . emissions reductions."[3] Further, the CGF will "explore ways to broaden its approach, for example, by developing off-the-shelf contracts"[4] and issue them through competitive auctions. The potential demand for CCfDs may be so great, indeed, that the government is "exploring the possibility of a government backstop of certain CCfD liabilities of the [CGF]."[5]

1 Canada, Department of Finance, Fall Economic Statement 2022, November 3, 2022, at 22.

2 Canada, Department of Finance, 2024 Budget, Budget Plan, April 16, 2024, at 190.

3 Ibid.

4 Ibid.

5 Ibid.

Meanwhile, think tanks such as Canadian Climate Institute and Clean Prosperity have tirelessly advocated for CCfDs.[6] Industry groups have also lobbied for them.[7]

The development of CCfDs in Canada is still preliminary, and their scope and design are in flux. For example, in its first "carbon contract," signed in December 2023, the CGF committed to purchase up to 1 million tonnes of carbon credits per year (for 15 years), at the price of $86.5 per tonne, from an entity called Entropy, in which CGF and Brookfield Asset Management jointly invested.[8] This "carbon credit offtake" agreement ensures that Entropy will fetch at least $86.5 for each tonne of carbon credit it generates through its carbon capture and sequestration operations.

Though some commentators labelled this agreement a CCfD, others think of CCfDs more in line with futures contracts without physical delivery. This latter idea is illustrated by another CGF investment made in June 2024:[9] the CGF agreed to bet against Markham District Energy on the "policy price" adopted in Ontario's Emission Performance Standards (EPS) regime. If the carbon price imposed by the EPS is less than the strike price of $100 per tonne, the CGF will pay the difference for up to 20,000 tonnes per year (for 10 years) to Markham District Energy. If the EPS carbon price is higher than the strike price, however, the difference in price will be paid from Markham District Energy to the CGF. This "two-way settlement" contract is intended to support Markham District Energy's investment in a wastewater heat recovery technology, presumably by ensuring that it can sell its carbon credits for at least (but also no more than) $100 per tonne.

6 See Jason Clark, Michael Bernstein, Dale Beugin, Blake Shaffer, and Jake Wadland, *Closing the Carbon-Pricing Certainty Gap* (Toronto: Clean Prosperity and Canadian Climate Institute, October 2022) (https://climateinstitute.ca/wp-content/uploads/2022/10/Closing_the_Carbon-Pricing_Certainty_Gap.pdf); and Etienne Rainville, "Carbon Contracts for Difference Face Transparency and Eligibility Barriers That We Need To Overcome," *Clean Prosperity*, May 7, 2024 (https://cleanprosperity.ca/carbon-contracts-for-difference-face-challenges-with-transparency-and-eligibility-barriers-that-we-need-to-overcome).

7 Letter from Advanced Biofuels Canada, Alberta's Industrial Heartland, Business Council of Alberta, Canadian Steel Producers Association, Carbon Engineering, Concrete Association of Canada, Canadian Chamber of Commerce, CHFCA, Chemistry Industry Association of Canada, Clean Prosperity, Electricity Canada, Enhance, Entropy, Explorers and Producers Association of Canada, Giatec, International CSS Knowledge Centre, Kiwetinohk Energy, and Pembina Institute to Deputy Prime Minister and Minister of Finance, Chrystia Freeland, August 2, 2023 (https://cleanprosperity.ca/wp-content/uploads/2023/08/CCfD-Industry-Joint-Letter.pdf).

8 Brookfield Asset Management, "Canada Growth Fund Announces Strategic Investment in Entropy Inc. and Carbon Credit Offtake Commitment," *Press Release*, December 21, 2023 (https://bam.brookfield.com/press-releases/canada-growth-fund-announces-strategic-investment-entropy-inc-and-carbon-credit).

9 Canada Growth Fund, "Carbon Contracts Strategy Backgrounder" (June 2024) (https://d2apye5bf031b.cloudfront.net/documents/26.06.2024-CGF-Carbon-Contracts-Strategy-Explainer-vDistribution-EN.pdf).

Yet a third type of CCfD widely discussed in Canada[10] is a futures contract on the carbon price on a particular emissions trading market. A CCfD designed for Alberta's Technology Innovation and Emissions Reduction (TIER) program, for example, would require the issuer to guarantee a minimum price for emission performance credits (EPCs) traded in the TIER system. Although private parties had announced an intention to launch an "environmental futures market" in which bets can be made about EPC prices,[11] the idea of a CCfD is for the government to act as a counterparty in such bets.

In this commentary, I urge caution against the broad adoption of CCfDs, and explain why the recent enthusiasm for CCfDs may be misplaced. I begin by noting the problem that the current designs of provincial output-based pricing systems (OBPSs) are not consistent with the expectation of the systems delivering robust price signals. I argue that CCfDs depend on such price signals, and they are not a plausible policy for encouraging the emergence of such signals. I then argue that it is hard to justify the government making a bet against itself on the "policy price" of carbon. An extensive scholarly literature has long argued against providing businesses with "certainty" against future policy changes in general, and there is little reason to think that carbon pricing is relevantly different. Overall, the use of CCfDs should remain narrowly targeted.

THE BANE OF FRAGMENTED CARBON MARKETS

Canada's OBPS regimes are sometimes compared with emissions trading systems (ETSs) in other countries. Indeed, in a recent World Bank report, Canada is treated as contributing a quarter (9 out of 36) of the global sample of *all* carbon markets.[12] However, this reveals a weakness of Canadian carbon pricing, not a strength. As table 1 shows, Canada's fragmentation results in several Canadian OBPS regimes including as few as 15 regulated facilities. Even the federal OBPS included only 52 facilities in 2022. The number of active sellers and buyers in each regime is presumably even smaller.

It is questionable whether markets so small can sustain robust price signals. This is the first problem with Canadian carbon markets, and it is a structural one with no easy solution: the reason why Canada has so many "carbon markets" is the zeal with which provinces would like to set their own rules for industrial emissions.[13] And it does not make sense to link carbon markets when the credits are generated on the basis of very different standards.

10 Dale Beugin, "What Are Contracts for Difference?" *Climate Institute*, March 23, 2023 (https://climateinstitute.ca/what-are-contracts-for-difference).

11 ICE, "ICE To Launch Environmental Futures Market Based on Alberta's Carbon Program," *News Release*, July 6, 2023 (https://ir.theice.com/press/news-details/2023/ICE-to-Launch-Environmental-Futures-Market-Based-on-Albertas-Carbon-Program/default.aspx).

12 These include the Quebec cap-and-trade program as well as the OBPS regimes implemented by the federal government and seven provinces. See World Bank, *State and Trends of Carbon Pricing 2024* (Washington, DC: World Bank, 2024).

13 See Wei Cui, "Comparing Canadian Output-Based Pricing Systems," elsewhere in this feature.

TABLE 1 Emission Credits Trading Under Canadian OBPS Regimes

	Number of entities in system	Limitations on the use of earned credits	Credit expiry	Information on market price
Federal	2022: 26 mandatory and 26 voluntary	None	5 years	None
Alberta	2022: 455 regulated facilities	Maximum proportion of compliance that can be met with credits: 60% in 2023, increasing by 10% per year to 90% in 2026	5 years for EPCs and 6 years for offset credits	Private estimates[a]
British Columbia	Unknown (107 entities under previous CleanBC Industrial Incentive Program)	In 2024, a maximum of 50% of obligation can be met with compliance units (earned credits and/or offset units), reducing to 40% for 2025, and 30% for 2026-2030	None	None
Ontario	2023: 216	None	5 years	None
Saskatchewan	2023: 166	None	None	None
New Brunswick	2023: 15 (including voluntary)	None	7 years	None
Newfoundland and Labrador	2022: 15	No limitation on earned credits; only 80% of emissions above target can be met with purchased credits	7 years	None
Nova Scotia	2023: 7 mandatory and 8 voluntary	None	7 years	None

EPC = emission performance credit.

a World Bank, *State and Trends of Carbon Pricing 2024* (Washington, DC: World Bank, 2024), at 27; Emma Dizon and Grant Bishop, *Strengthening TIER for Alberta's Low-Carbon Growth: Measuring Credit Oversupply Risks in Alberta's Carbon Market* (Toronto: Clean Prosperity, 2024), at 17-18.

A second problem is that, under prevailing designs, there is a high risk that oversupplies of carbon credits will emerge, even in the larger trading markets. Dizon and Bishop recently analyzed this possibility for Alberta's TIER program.[14] Like other OBPS regimes, carbon credits and offsets are traded "over the counter" in TIER, and there is no exchange or quoted price. After consulting with market players, Dizon

14 Emma Dizon and Grant Bishop, *Strengthening TIER for Alberta's Low-Carbon Growth: Measuring Credit Oversupply Risks in Alberta's Carbon Market* (Toronto: Clean Prosperity, 2024).

and Bishop report that credits and offsets under TIER are trading at a significant and widening discount (37.5 percent in 2024) relative to the "policy price"—the schedule of escalating carbon prices announced by the federal government, which all provinces currently follow. Market participants thus appear to be anticipating low credit and offset prices in the future. Moreover, "net obligations"—emissions above facility benchmarks minus credits and offsets created by emission reductions—have declined relative to TIER-regulated emissions. This decline reflects reductions in emission intensities among TIER-regulated facilities that outpace the benchmark tightening dictated by TIER.

This raises the question of whether provincial governments have adopted measures to support prices in their carbon markets. Table 1 shows that some, but not all, provinces required carbon credits to expire after a few years. This limits the supply of credits and should help support their price. Aside from this rule, however, there is currently no evidence of provincial adoption of ongoing price-maintenance measures. Some provinces initially set the "tightening rate" of the emission intensity benchmarks to reduce the possibility of a permanent oversupply. But no province has adopted what Dizon and Bishop call "adaptive tightening rates"—accelerated increases in stringency when emission reduction is happening faster than the tightening rate initially required.

Interestingly, some provinces' OBPS rules seem to convey expectations about market prices for carbon credits. Alberta initially limited the capacity of facilities emitting above their benchmarks to use purchased credits to offset compliance obligations (60 percent in 2023). This limit is liberalized by 10 percent per year until it reaches 90 percent in 2026. This may be interpreted as in line with an expectation that market prices will be too low in the earlier years, such that facilities need to be disciplined by the policy price to a greater extent. As the market price of emission credits increases over time (along with the policy price), facilities can be allowed to use traded credits more liberally. By contrast, British Columbia's OBPS provides that in 2024, a maximum of 50 percent of compliance obligation can be met with earned credits and/or offset units, but this percentage is *reduced* to 40 percent in 2025, and fixed at 30 percent from 2026 to 2030. It appears that British Columbia intends to maximize regulated facilities' exposure to full carbon pricing even though, by reducing the demand for carbon credits, it would also suppress their prices.

The intentions behind the provincial governments' control of Canadian OBPS regimes in respect of market prices are therefore uncertain. This poses a challenge for CCfDs that reference market carbon prices. The challenge is also arguably graver than the present lack of price transparency in OBPS markets. When the prices of credit trades are unknown, it certainly seems hard to settle bets on them.[15] But suppose that provincial carbon registries are developed to encourage greater disclosure of trading information, and that third-party appraisers emerge to estimate the fair value of credits on the basis of past credit issuances and retirements. These measures

15 Ibid., at 20 (emphasizing price transparency as a precondition for CCfDs to function).

may help solve the problem of settling a CCfD, but would not remedy the problem of a market where emissions credits are traded at prices far lower than the policy price of carbon. In such a market, a CCfD that sets the strike price at levels close to the policy price would cost the government dearly, while one that sets the strike place at very low levels would both deliver little benefit for the CCfD's private holder and put the government in a posture of shorting itself.

Remarkably, some commentators on the CCfD seem to suggest that the lack of price transparency and the risk of oversupply in Canadian carbon markets are not problems for concluding CCfDs. Rather, they claim that CCfDs are actually *solutions* to these problems. For example, it has been argued that if the federal government promises to offer CCfDs widely, provincial governments will have incentives to mandate price transparency in their markets: doing so would allow market participants to benefit from the federal insurance against low carbon market prices.[16] This argument seems fallacious. Provincial governments have very good reasons to promote price transparency already. For one, governments should be on guard against the oversupply of credits; a direct way of monitoring such oversupply is to look at prices. Moreover, as Dizon and Bishop point out, price transparency makes the carbon market fairer for new entrants[17] and can also help the regulator to detect collusion among market participants.[18] Why are these reasons insufficient to motivate provincial governments to mandate transparency, and why would the promise of large government payments under CCfDs to private parties alone provide such motivation? It certainly seems here that CCfDs are being proposed for the wrong purpose.

But if this argument is problematic, so is another, even more popular argument made by CCfD advocates. This is the idea that CCfDs allow the (federal) government to signal its commitment to adequate carbon pricing in the future.[19] The reasoning is that if the government allows the market price of carbon to drop too low relative to a pre-set price, it would lose large amounts of money under CCfDs; therefore, it would be motivated by CCfDs to keep carbon price high, for example, by deploying price-maintenance tools for carbon markets. The question for this argument is, again, why does the government not have strong motivations already to support carbon trading prices, for example, through adaptive tightening of stringency? Why should the risk of handouts under CCfDs be what motivates governments to embrace good policy?

WHEN SHOULD GOVERNMENTS COMPENSATE FOR POLICY CHANGES?

Suppose that in the near future, Canadian OBPS regimes are not reformed to ensure that emissions credits trade at prices sufficiently close to the policy carbon price. This is a state of policy failure that Canadians need to take action to rectify. Absent

16 Rainville, supra note 6.

17 Dizon and Bishop, supra note 14, at 17.

18 Ibid., at 36.

19 Dizon and Bishop, for example, make this argument (ibid., at 30).

such action, policy failure would persist. The suggestion that the government should compensate private parties, through CCfDs, for the "contingency" that better policies do not emerge is equivalent to encouraging private parties to act as though better policies are already in place.

To see more fully why this is misguided, consider the idea of CCfDs referencing the policy carbon price.[20] Does it ever make sense for the government to financially guarantee private parties that it will impose a minimum policy carbon price in the future? There are strong reasons to think the answer is no. All government policies can change in the future. And many policy changes significantly affect the financial value of investments. For example, when tax rates unexpectedly go up for the income tax, the goods and services tax, or the property tax, past investments suffer windfall losses.[21] Conversely, when tax rates go down unexpectedly, existing investments enjoy windfall gains. In this sense, the value of investments is always exposed to policy uncertainty, whether through taxation, regulation, spending, or other measures. Clearly, it would not make sense for any government to promise that its policies will never change.

Nonetheless, there are long and diffuse intellectual traditions arguing that when the government changes policies, it should compensate private parties whose interests are negatively affected (or grandfather past investments by exempting them from the new policy). Such arguments have been closely scrutinized by scholars of law and economics in recent decades and shown to be unpersuasive[22] for several basic reasons. First, when there is genuine policy uncertainty—for example, uncertainty analogous to natural disasters—the marketplace itself can provide mechanisms for risk diversification. The government is not generally better placed to insure against such uncertainty. Indeed, any insurance must deal with issues of moral hazard—making sure that the insured does not make inefficient and excessive investments notwithstanding known risk—and there is little evidence that the government is well prepared to monitor this.

Second, private parties often enjoy windfall gains as a result of unexpected policy changes. Consistency would require the government to tax back such windfall gains: there is no reason why the public, through the government, should bear the financial losses brought by policy changes but not enjoy the gains.

Third, traditional arguments for government compensation for policy changes often posit that the government tends to ignore the private cost of policy changes, or

20 One should be skeptical about the attraction to private parties of a CCfD of this kind. Canadian OBPS regimes already ensure that facilities do not face this price on most of their emissions. Therefore, no emission reduction project would presume that the policy price reflects the financial value of the emissions reduction it achieves.

21 Michael J. Graetz, "Legal Transitions: The Case of Retroactivity in Income Tax Revision" (1977) 126:1 *University of Pennsylvania Law Review* 47-87.

22 See Louis Kaplow, "An Economic Analysis of Legal Transitions" (1986) 99:3 *Harvard Law Review* 509-617; and Louis Kaplow, *Transition Policy: A Conceptual Framework*, NBER Working Paper no. 9596 (Cambridge, MA: National Bureau of Economic Research, 2003).

that only the risk of fiscal loss would force the government to adopt superior policy. These postulates about government behaviour, however, are rarely consistently applied[23] and are not backed by strong evidence.

CCfDs referencing policy carbon prices secure compensation for private parties when the government changes its current policy of imposing a high carbon price in the future. Given the general objections against governments providing compensation for policy changes, is there anything special about carbon-pricing policy that mitigates the force of such objections?[24] To put it differently, one can ask, in respect of all of the arguments that have been offered for CCfDs, why can such arguments not be made about all other investments that have social value?

Some proponents of CCfDs have provided the following answer: in adopting carbon pricing, the government suffers some form of time inconsistency.[25] Time inconsistency refers to situations where a government with the same set of preferences and objectives may choose different policies at different times—for example, before versus after private investments are made. A classic illustration is that a government's ex ante optimal policy may be one of not taxing capital (to encourage investment). Once investments are made, however, the optimal policy becomes one of taxing such investment, since it no longer distorts investment decisions. When such time inconsistency is known, the socially optimal level of investment may not be achievable. The best outcome can be attained only if a government can somehow commit itself to not changing policy. If carbon pricing faces a time inconsistency problem, a CCfD can potentially serve as such a commitment device.

However, scholars have actually not been able to offer a coherent specification of the time inconsistency problem for carbon pricing.[26] Indeed, the time path of carbon pricing that Canada has chosen suggests the opposite. Canada supposedly sets its

23 *Transition Policy*, ibid., at section VI.

24 On the surface, it might seem that CCfDs with two-way settlement allow the government to gain financially from policy change, and thus address the second objection above. However, unless the policy carbon price translates into financial gain for the private contractual party, it is unclear how the government can secure itself against credit risk under CCfDs referencing the policy carbon price: the government can always be counted on to honour its payment obligations, but it is not clear that the private party can.

25 See Olga Chiappinelli and Karsten Neuhoff, *Time-Consistent Carbon Pricing: The Role of Carbon Contracts for Differences*, DIW Berlin discussion paper no. 1859 (Berlin: Deutsches Institut für Wirtschaftsforschung, 2020).

26 An earlier survey reports that there is no consensus on the existence or nature of the time inconsistency problem in carbon pricing (see Steffen Brunner, Christian Flachsland, and Robert Marschinski, "Credible Commitment in Carbon Policy" (2012) 12:2 *Climate Policy* 255-71, at 258). Chiappinelli and Neuhoff, supra note 25, illustrate the challenges of identifying such a problem. They develop a model where, under carbon pricing, consumers do not benefit at all from the development of abatement technology: owners of such technology capture the entire benefit in the form of profits. They also assume a government that maximizes the sum of consumer surplus and carbon pricing revenue rather than social welfare. That such idiosyncratic assumptions are needed to specify a time inconsistency problem is telling.

carbon price on the basis of the social cost of carbon (SCC). In theory, there is no reason not to adopt that full carbon price *now*.[27] But Canada has chosen to gradually increase its carbon price such that the SCC (estimated in 2022 to be approximately $170 per tonne of carbon dioxide equivalent [tCO_2e]) will be reflected in the carbon price only in 2030. This gradual escalation can naturally be interpreted as being based on the judgment that $170 per tCO_2e would not be a politically feasible carbon price now: the gradual increase conveys the aspiration that the electorate will adjust over time to carbon pricing. Whether this aspiration will be fulfilled is uncertain—and that is the reason for calls for CCfDs. Regardless, the very nature of this aspiration indicates that the government's optimal choice is not one that changes over time from high to low carbon pricing.

THE WISDOM OF KEEPING CCfDs NARROWLY TARGETED

Guaranteeing carbon prices can not only be quite expensive for the government, but also potentially provide large windfalls to private parties and/or subsidize inefficient investments. Dizon and Bishop, for example, modelled a hypothetical carbon capture, utilization, and storage project in Alberta (based on actual reported projects). This model showed that if the project were guaranteed a carbon price at a 10 percent discount on the current federal carbon price schedule, it would have a net present value (NPV) of a whopping $658 million—a giant windfall for the holder of the guarantee. In fact, even a price of $95/$tCO_2e$ would result in an NPV of $158 million. For the project to break even (that is, NPV = 0), a carbon price of only $78/$tCO_2e$ is needed when the financing cost is 8 percent, and the breakeven carbon price is even lower with a lower financing cost.[28] Contrast this with the $86.5/$tCO_2e$ strike price of the Entropy CCfD[29]—excessively favourable terms under CCfDs clearly seem to be a concern.

Clean technology investments have both private and social value, but in this regard they are no different from many other investments. If there are no good arguments generally for asking the government to insure investors against policy changes that could negatively affect their investments, insuring the value of clean technology investments must have some special justification. In fact, it appears that elsewhere, CCfDs are discussed as tools for achieving more specific purposes. For

27 Roberton C. Williams, "Environmental Taxation," in Alan J. Auerbach and Kent Smetters, eds., *The Economics of Tax Policy* (New York: Oxford University Press, 2017), at 49-73 (https://doi.org/10.1093/acprof:oso/9780190619725.003.0004).

28 Dizon and Bishop, supra note 14, at section 3. Indeed, the authors show that the 45Q sequestration tax credit under the US Inflation Reduction Act would give the hypothetical project only a $36 million NPV. This is relevant because competition with US incentives is one of the original reasons that CCfDs were proposed in Canada.

29 See Brookfield Asset Management, supra note 8. The Canada Growth Fund, supra note 9, states that it always seeks to minimize "concessionality" in its investments.

example, by guaranteeing the revenue of a project, lower debt financing may become available, allowing more projects to be undertaken.[30] Similarly, a government guarantee of revenue may be needed to stimulate uniquely important investments, just as government purchase agreements were deemed essential for the rapid development of COVID-19 vaccines.

In Canada, the promotion of CCfDs has increasingly been justified by much more generic rationales, such as giving businesses certainty and competing with incentives offered by the US Inflation Reduction Act. One should not let the novelty of CCfDs as a policy instrument obscure the well-known shortcoming of such arguments. The perceived "broad demand" for CCfDs should be resisted.

30 Jorn C. Richstein and Karsten Neuhoff, "Carbon Contracts-for-Difference: How To De-Risk Innovative Investments for a Low-Carbon Industry" (2022) 25:8 *iScience* (https://doi.org/10.1016/j.isci.2022.104700). Compare this argument for CCfDs with the fact that, in the Entropy deal (see supra note 8), the CGF was not only the CCfD issuer but also an equity investor.

CANADIAN TAX JOURNAL / REVUE FISCALE CANADIENNE (2025) 73:1, 107
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Douglas J. Sherbaniuk Distinguished Writing Award

JOSH JONES AND JEFFREY LOVE

Josh Jones and Jeffrey Love are the 2024 recipients of the Canadian Tax Foundation's Douglas J. Sherbaniuk Distinguished Writing Award. Their paper, "Recent Developments in Asset Management," was published in the *2023 Conference Report*. The paper was selected by a committee of experienced tax professionals as the best writing published by the Foundation in 2023-24. The award, which is conferred annually, is named for the Foundation's late director emeritus.

Josh Jones, a partner at Blakes, provides advice on all areas of Canadian domestic and international income tax law, with a focus on cross-border mergers and acquisitions, corporate reorganizations, and investment funds, including exchange-traded funds (ETFs), public financings, and structured products.

Jeffrey Love, a partner at KPMG Law LLP, specializes in asset management (mutual funds, ETFs, closed-end funds, pooled funds), wealth management (including registered plans and broker-dealers), banking, leasing, capital markets, and private equity taxation matters. He also advises clients on resolving tax disputes.

Prix d'excellence en rédaction Douglas J. Sherbaniuk

JOSH JONES ET JEFFREY LOVE

Josh Jones and Jeffrey Love sont les récipiendaires 2024 du Prix d'excellence en rédaction Douglas J. Sherbaniuk de la Fondation canadienne de fiscalité. Leur article intitulé « Recent Developments in Asset Management » a été publié dans le *2023 Conference Report*. Leur article a été retenu par un comité composé de professionnels en fiscalité à titre de meilleur article publié par la Fondation en 2023-24. Ce prix, décernée annuellement, est nommé à la mémoire du défunt directeur emeritus de la Fondation.

Josh Jones, associé de Blakes, est un expert en droit fiscal canadien, offrant des conseils sur les aspects nationaux et internationaux de l'imposition des revenus. Il est spécialisé dans les fusions et acquisitions transfrontalières, les restructurations d'entreprises, les fonds d'investissement, y compris les fonds négociés en bourse (FNB), les financements publics et les produits structurés.

Jeffrey Love, associé chez KPMG cabinet juridique s.r.l./S.E.N.C.R.L. se spécialise dans la gestion d'actifs (fonds communs de placement, FNB, fonds de placement fermé, caisse en gestion commune), la gestion de patrimoine (notamment les régimes enregistrés et les comptes de courtiers en valeurs mobilières), les services bancaires, le crédit-bail, les marchés des capitaux et les placements privés. Il offre également des conseils juridiques à ses clients pour les aider à régler des litiges fiscaux.

Canadian Tax Foundation Regional Student-Paper Awards

Each year, the Canadian Tax Foundation awards up to four regional student-paper prizes. Depending on the merit of the papers received, one prize may be awarded for each of four regions of the country: Atlantic Canada (the Canadian Tax Foundation-McInnes Cooper Award); Quebec (the Canadian Tax Foundation-Osler Hoskin Harcourt Award); Ontario (the Canadian Tax Foundation-Fasken Martineau DuMoulin Award); and western Canada (the Canadian Tax Foundation-Bert Wolfe Nitikman Foundation Award). Papers must be written as a requirement of a tax-related course, including directed research courses, and can address any aspect of the Canadian tax system, including comparative analyses, tax policy, tax compliance, tax planning, and tax system design. Papers may be written in either English or French and must be recommended for award consideration by the professor or instructor of the course.

Papers will be reviewed by three independent reviewers, and abstracts (of 400 words or less) of the award-winning papers will be published in the *Canadian Tax Journal*. The authors of the winning papers will also receive a cash prize from the firms or institutions sponsoring the awards and a one-year membership in the Foundation, entitling them to receive complimentary copies of many of the currently issued Foundation publications, including the *Canadian Tax Journal*, *Canadian Tax Highlights*, *Tax for the Owner-Manager*, and the annual tax conference report, along with one year of complimentary access to TaxFind, the Foundation's online research database. As members of the Foundation, winners can also take advantage of generous discounts on other publications as well as discounted registration fees for Foundation conferences and courses.

Submissions to the student-paper competition should be addressed to the Canadian Tax Foundation, Student-Paper Competition, 145 Wellington Street West, Suite 1400, Toronto, ON M5J 1H8, or e-mailed to CTF_Awards@ctf.ca. Entries must be accompanied by a letter of recommendation from the professor or instructor of the tax course for which the paper was written and must include the student's name and e-mail address if known. The submission deadline for the 2024-25 academic year is June 30, 2025.

THE CANADIAN TAX FOUNDATION-FASKEN MARTINEAU DUMOULIN AWARD FOR ONTARIO

Ella Rowley (2023-24 recipient)

The Canadian Tax Foundation is pleased to announce that Ella Rowley is the winner of the Canadian Tax Foundation-Fasken Martineau DuMoulin Award for the best Ontario paper of 2023-24 dealing with an aspect of Canadian taxation.

Ms. Rowley's paper, "Examining the Impact of the New Mandatory Disclosure Rules on Solicitor-Client Privilege," was written for Professor Sunita Doobay's International Taxation course in the Juris Doctor program at Queen's Law School.

Ella graduated from Queen's Law School with a Juris Doctor degree in May 2024 and was awarded the Heenan Blaikie LLP Scholarship for her upper-year course paper. She is currently completing her articles at Wildeboer Dellelce LLP and will be called to the bar in June 2025.

ABSTRACT

This paper examines the impact of Canada's expanded mandatory disclosure rules, introduced by Bill C-47, on solicitor-client privilege. While the rules aim to address aggressive tax avoidance by requiring detailed reporting of certain transactions, there are concerns of whether these rules interfere with solicitor-client privilege. Specifically, the new requirements may force lawyers into conflicts of interest, cause inadvertent disclosure of privileged information, and impose obligations on non-legal advisors who lack privilege protections. The paper explores these challenges in light of the constitutional principles, ethical duties, and international standards underlying solicitor-client privilege.

Prix régionaux du meilleur article par un étudiant de la Fondation canadienne de fiscalité

Chaque année, la Fondation canadienne de fiscalité (FCF) décerne jusqu'à quatre prix régionaux pour des articles rédigés par des étudiants. Selon la qualité des articles qui ont été soumis, un prix peut être décerné pour chacune des quatre régions du pays : le Canada atlantique (le Prix FCF-McInnes Cooper); le Québec (le Prix FCF-Osler Hoskin Harcourt); l'Ontario (le Prix FCF-Fasken Martineau DuMoulin); et l'ouest canadien (le Prix FCF-Bert Wolfe Nitikman Foundation). Les articles doivent avoir été rédigés dans le cadre d'un cours lié à la fiscalité, comprenant les cours de travaux dirigés, et ils peuvent porter sur tout aspect du régime fiscal canadien, y compris les analyses comparatives, la politique fiscale, l'observation des règles fiscales, la planification fiscale et la conception du régime fiscal. Les articles peuvent être rédigés en anglais ou en français et une lettre de recommandation du professeur ou du chargé d'enseignement du cours doit être au dossier.

Les articles sont évalués par trois examinateurs indépendants, et des précis (de 400 mots ou moins) des articles primés seront publiés dans la *Revue fiscale canadienne*. Les auteurs des articles primés recevront aussi une récompense en argent des organismes ou des sociétés qui commanditent le prix ainsi qu'une adhésion d'une année à la FCF, leur donnant le droit de recevoir des exemplaires gratuits d'un grand nombre d'ouvrages publiés par la FCF, dont *Revue fiscale canadienne*, *Faits saillants en fiscalité canadienne*, *Actualités fiscales pour les propriétaires exploitants* ainsi que le Rapport de la conférence annuelle en fiscalité, avec un accès d'un an à TaxFind en ligne, l'outil de recherche électronique de données de la FCF. À titre de membre de la FCF, les lauréats bénéficient également de réductions appréciables sur le prix d'autres publications ainsi que sur les frais d'inscription aux conférences et aux cours offerts par la FCF.

Les dossiers de participation au concours du meilleur article rédigé par un étudiant doivent être transmis par la poste à la FCF, Concours du meilleur article rédigé par un étudiant, 145 Wellington Street West, Suite 1400, Toronto, ON M5J 1H8, ou par courriel à CTF_Awards@ctf.ca. Les dossiers doivent être accompagnés d'une lettre de recommandation du professeur ou du chargé d'enseignement du cours en fiscalité dans le cadre duquel l'article a été rédigé ainsi que des nom et adresse courriel de l'étudiant si connue. La date d'échéance de présentation des dossiers pour l'année universitaire 2024-25 est le 30 juin 2025.

PRIX DE LA FONDATION CANADIENNE DE FISCALITÉ-OSLER HOSKIN HARCOURT POUR LE QUÉBEC

Ella Rowley (récipiendaire 2023-24)

La Fondation canadienne de fiscalité a le plaisir d'annoncer que Ella Rowley est la lauréate du Prix Fondation canadienne de fiscalité-Osler Hoskin Harcourt pour le meilleur article de 2023-24 de la province de Québec qui traite d'un aspect de la fiscalité canadienne.

L'article de Mlle Rowley, intitulé « Examining the Impact of the New Mandatory Disclosure Rules on Solicitor-Client Privilege », a été rédigé pour le cours de fiscalité internationale dispensé par la professeure Sunita Doobai, dans le cadre du programme de doctorat en droit (Juris Doctor) à la Faculté de droit de l'Université Queen's.

Ella a obtenu son doctorat en droit de la Faculté de droit de l'Université Queen's en mai 2024 et a remporté la bourse Heenan Blaikie LLP pour son travail de recherche de troisième cycle. Elle effectue présentement un stage chez Wildeboer Dellelce LLP et devrait prêter serment au Barreau en juin 2025.

PRÉCIS

Ce texte analyse l'impact des règles élargies de divulgation obligatoire du Canada, introduites par le projet de loi C-47, sur le secret professionnel des avocats. Bien que ces règles soient conçues pour lutter contre l'évasion fiscale abusive en exigeant la divulgation détaillée de certaines opérations, on se demande si elles ne vont pas à l'encontre du secret professionnel des avocats. En effet, les récentes modifications pourraient contraindre les avocats à se retrouver en situation de conflit d'intérêts, ce qui pourrait entraîner une divulgation involontaire d'informations confidentielles et pourrait imposer des obligations aux conseillers non juridiques qui ne bénéficient pas de la protection du privilège. Ce texte examine ces défis en les éclairant à la lumière des principes constitutionnels, des obligations déontologiques et des normes internationales qui régissent le secret professionnel des avocats.

Wayne Adams Young Practitioner Writing Award

In 2014, the Canadian Tax Foundation presented the inaugural Best Newsletter Article by a Young Practitioner Award. This year, Wayne Adams retired after 13 years as the Foundation's Director of Membership and Community Relations. Part of Wayne's role has been to support and grow the young practitioner (YP) groups in cities across the country. To honour his contributions, the award has been renamed the Wayne Adams Young Practitioner Writing Award.

Newsletter articles, in addition to being a valuable service to the profession in their own right, are often a stepping stone to lengthier pieces of writing, such as articles in the *Canadian Tax Journal* and papers for Foundation conferences. For a YP, early success in publishing newsletter articles may lead to a tax career in which writing is a regular and ongoing part of the individual's contribution to the profession.

The Foundation defines a YP as an individual who has 10 years or less of experience working in the taxation field after becoming fully qualified (for example, after receiving their professional designation). This year's award is given for the best newsletter article that (1) was written solely by one or more authors who was a YP at the time of publication, and (2) appeared in any of the four newsletters published by the Foundation in 2023: *Canadian Tax Focus*, *Tax for the Owner-Manager*, *International Tax Highlights*, and *Perspectives on Tax Law and Policy*. This year, most of the 58 articles eligible for the award appeared in *Canadian Tax Focus*, which generally publishes only articles of which the author (or one of the co-authors) is a YP. Four eligible articles appeared in the *Tax for the Owner-Manager*, and five articles appeared in *International Tax Highlights*.

A total of 10 of the articles eligible for the award were reviewed by a three-member committee whose members are all past winners of this award. The criteria applied by the committee were essentially the same as the criteria for the Foundation's Douglas J. Sherbaniuk Distinguished Writing Award. The members of the committee were

- Erica Hennessy, McCarthy Tétrault LLP, Calgary;
- James Painter, Anthem Properties Group Ltd., Vancouver; and
- Henry Shew, Our Family Office, Toronto.

The committee gave the awards to three authors in respect of the following two articles:

- Alex Kerslake and Alex Cook (both of PricewaterhouseCoopers LLP, Toronto: alex.g.kerslake@pwc.com and alex.cook@pwc.com), "Interactions of the EIFEL Regime with Discretionary Trusts" (2023) 13:1 *Canadian Tax Focus* 7-8.
- Graham Morton (McKenzie Lake Lawyers LLP: graham.morton@mckenzielake.com), "Personal and Prescribed Trusts for Employees" (2023) 23:1 *Tax for the Owner-Manager* 8-9.

YPs (and anyone else) interested in writing for the Foundation's newsletters are invited to contact the newsletter editors: Alan Macnaughton (amacnaughton@uwaterloo.ca) for *Canadian Tax Focus*, Joan Jung (jejung@millerthomson.com) for *Tax for the Owner-Manager*, Jeffrey Trossman (jeffrey.trossman@blakes.com) for *Perspectives on Tax Law and Policy*, and Angelo Nikolakakis (angelo.nikolakakis@ca.ey.com) for *International Tax Highlights*. In Quebec, prospective contributors to the newsletters are invited to contact Éric Hamelin (eric.hamelin@usherbrooke.ca) of the Université de Sherbrooke, French content editor of *Canadian Tax Focus*, or Carl Deslongchamps (cdeslongchamps@ctf.ca) of the Quebec office.

Individuals interested in participating in any of the events and activities of the Foundation's YP chapters across Canada are invited to contact either the chair of their local chapter's steering committee or Robyn Corrigan (rcorrigan@ctf.ca) of the national office. For the Montreal and Quebec City chapters, they are invited to contact Carl Deslongchamps (cdeslongchamps@ctf.ca) of the Quebec office.

There are YP chapters in Calgary, Edmonton, Halifax, Kelowna, Kitchener-Waterloo, London, Mississauga, Montreal, Ottawa, Quebec City, Saskatoon, Toronto, Vancouver, and Winnipeg.

Prix Wayne Adams du meilleur article rédigé par un jeune praticien

En 2014, la Fondation canadienne de fiscalité a décerné le tout premier Prix du meilleur article de bulletin rédigé par un jeune praticien. Cette même année, Wayne Adams a pris sa retraite après avoir dirigé pendant 13 ans le service de l'adhésion et des relations avec les membres de la communauté de la Fondation. Il a aidé à soutenir et à développer les groupes de jeunes praticiens (JP) dans les villes partout au pays. Pour lui rendre hommage, le prix a été renommé le Prix Wayne Adams du meilleur article rédigé par un jeune praticien.

Les articles de bulletins, en plus d'offrir un service précieux à la profession, servent souvent de point de départ à des écrits plus longs, comme des articles publiés dans la *Revue fiscale canadienne* ou des contributions aux conférences de la Fondation. Commencer sa carrière en tant que JP en rédigeant des articles pour les bulletins peut mener à un cheminement en fiscalité où la rédaction sera un apport constant et crucial à la prestation de ses services à la profession.

Selon la Fondation, une personne ayant moins de dix ans d'expérience professionnelle en fiscalité après l'obtention de ses qualifications (telles qu'un titre professionnel) est considérée comme une JP. Ce prix est décerné à l'article le plus remarquable d'un bulletin qui remplit deux critères. Premièrement, il doit avoir été entièrement rédigé par un ou plusieurs auteurs qui étaient des JPs au moment de sa publication. Deuxièmement, il doit avoir été publié dans l'un des quatre bulletins de la Fondation en 2023 : *Focus sur la fiscalité canadienne*, *Actualités fiscales pour les Propriétaires exploitants*, *International Tax Highlights* et *Perspectives en fiscalité et en politique fiscale*. Parmi les 58 articles en lice pour le prix cette année, la plupart ont été publiés dans *Focus sur la fiscalité canadienne*, un bulletin spécialisé dans la publication d'articles écrits par un auteur (ou l'un de ses coauteurs) qui est un JP. Quatre de ces articles ont aussi été publiés dans *Actualités fiscales pour les Propriétaires exploitants*, et cinq autres ont été diffusés dans *International Tax Highlights*.

Un groupe de sélection, composé de trois anciens lauréats du prix, a examiné les 10 textes admissibles. Les critères qu'ils ont appliqués correspondaient à ceux utilisés pour attribuer le Prix d'excellence en rédaction Douglas J. Sherbaniuk, remis par la Fondation. Les membres du jury étaient :

- Erica Hennessy, McCarthy Tétrault S.E.N.C.R.L., s.r.l., Calgary;
- James Painter, Anthem Properties Group Ltd., Vancouver; et
- Henry Shew, Our Family Office, Toronto.

Le jury a attribué des prix à trois auteurs pour ces deux articles :

- Alex Kerslake et Alex Cook (tous deux de PricewaterhouseCoopers S.E.N.C.R.L., s.r.l., Toronto : alex.g.kerslake@pwc.com et alex.cook@pwc.com), « Interactions of the EIFEL Regime with Discretionary Trusts » (2023) 13:1 *Focus sur la fiscalité canadienne* 7-8.
- Graham Morton (McKenzie Lake Lawyers LLP, graham.morton@mckenzielake.com), « Personal and Prescribed Trusts for Employees » (2023) 23:1 *Actualités fiscales pour les Propriétaires exploitants* 8-9.

Les JP (ainsi que toute autre personne intéressée) souhaitant écrire des articles pour les bulletins de la Fondation sont invités à contacter les rédacteurs en chef des bulletins respectifs : Alan Macnaughton (amacnaughton@uwaterloo.ca) pour *Focus sur la fiscalité canadienne*, Joan Jung (jejung@millerthomson.com) pour *Actualités fiscales pour les Propriétaires exploitants*, Jeffrey Trossman (jeffrey.trossman@blakes.com) pour *Perspectives en fiscalité et en politique fiscale*, et Angelo Nikolakakis (angelo.nikolakakis@ca.ey.com) pour *International Tax Highlights*. Pour le Québec, toute personne désirant contribuer aux bulletins peut communiquer avec Éric Hamelin (eric.hamelin@usherbrooke.ca), rédacteur en chef du contenu français de *Focus sur la fiscalité canadienne*, à l'Université de Sherbrooke, ou avec Carl Deslongchamps (cdeslongchamps@ctf.ca), au bureau du Québec.

Toute personne désireuse de participer aux événements et aux activités de l'une des divisions de JPs de la Fondation au Canada est invitée à communiquer avec le ou la responsable du comité directeur de sa division régionale ou avec Robyn Corrigan (rcorrigan@ctf.ca) au bureau national. Pour les divisions de Montréal et de Québec, il faut plutôt s'adresser à Carl Deslongchamps (cdeslongchamps@ctf.ca) au bureau du Québec.

On compte des divisions de jeunes praticiens à Calgary, Edmonton, Halifax, Kelowna, Kitchener-Waterloo, London, Mississauga, Montréal, Ottawa, Québec (ville), Saskatoon, Toronto, Vancouver et Winnipeg.

Canadian Tax Foundation Lifetime Contribution Award

As of 2016, the Canadian Tax Foundation honours each year individuals who, through their volunteer efforts and body of work, have made substantial and outstanding contributions to the Foundation during their careers. The Lifetime Contribution Award is the most prestigious award conferred by the Foundation. The selection committee takes into account the individual's contributions to Foundation publications and conferences, service on the board of governors and other committees, and participation in other organizations and activities that further the Foundation's purposes.

The 2024 recipients were Marlene Cepparo and the Hon. Marshall Rothstein.

For further information about the nomination and selection process for this award, see the Foundation website.

Prix de la Fondation canadienne de fiscalité pour une contribution exceptionnelle

Depuis 2016, la Fondation canadienne de fiscalité rend hommage chaque année à des personnes qui, par leur travail bénévole et leurs réalisations, ont contribué de façon importante et exceptionnelle à la Fondation au cours de leur carrière. Le Prix pour une contribution exceptionnelle est le prix le plus prestigieux décerné par la Fondation. Le comité de sélection prend en compte la contribution de la personne aux publications et aux conférences de la Fondation, son travail au sein du conseil des gouverneurs et d'autres comités, ainsi que sa participation à d'autres organisations et activités qui contribuent à la réalisation des objectifs de la Fondation.

Les lauréats de 2024 étaient Marlene Cepparo et l'Honorable Marshall Rothstein.

Pour obtenir de plus amples renseignements sur le processus de nomination et de sélection pour ce prix, consultez le site Web de la Fondation.

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Finances of the Nation

David Lin*

SURVEY OF PROVINCIAL AND TERRITORIAL BUDGETS, 2024-25

For almost 60 years, the Canadian Tax Foundation published an annual monograph, Finances of the Nation, *and its predecessor,* The National Finances. *In a change of format, the 2014* Canadian Tax Journal *introduced a new "Finances of the Nation" feature, which presents annual surveys of provincial and territorial budgets and topical articles on taxation and public expenditures in Canada. This article surveys the 2024-25 provincial and territorial budgets.*

The underlying data for the Finances of the Nation *monographs and for the articles in this journal will be published online in the near future.*

KEYWORDS: BUDGETS ■ PROVINCIAL TAXES ■ TERRITORIAL ■ GOVERNMENT FINANCE ■ GOVERNMENT EXPENDITURES ■ PROGRAM BUDGETING

CONTENTS

Introduction 120
Summary Information 120
Provincial and Territorial Budgets by Jurisdiction 136
British Columbia (Table 12) 145
Tax Highlights 145
Tax Changes 145
Alberta (Table 13) 148
Tax Highlights 148
Tax Changes 148
Saskatchewan (Table 14) 151
Tax Highlights 151
Tax Changes 151

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Manitoba (Table 15) 153
Tax Highlights 153
Tax Changes 153
Ontario (Table 16) 156
Tax Highlights 156
Tax Changes 156
Quebec (Table 17) 157
Tax Highlights 157
Tax Changes 157
New Brunswick (Table 18) 160
Tax Highlights 160
Tax Changes 160
Nova Scotia (Table 19) 162
Tax Highlights 162
Tax Changes 162
Prince Edward Island (Table 20) 163
Tax Highlights 163
Tax Changes 163
Newfoundland and Labrador (Table 21) 165
Tax Highlights 165
Tax Changes 165
Yukon (Table 22) 166
Tax Highlights 166
Tax Changes 166
Northwest Territories (Table 23) 168
Tax Highlights 168
Tax Changes 168
Nunavut (Table 24) 170
Tax Highlights 170
Tax Changes 170

INTRODUCTION

This article has two distinct parts. First, it sets out tables and charts that show aggregate figures related to projected 2024-25 budget revenues and expenditures for the various provinces and territories, using the accounting methods of the jurisdiction, as well as tables that show corporate income tax rates, personal income tax brackets and rates, and other matters. Second, the article summarizes the projected budget revenues and expenditures in tabular form and also summarizes the tax changes in narrative form, for each province and territory.

SUMMARY INFORMATION

Continuing the trend from the previous fiscal year, the common theme that continued to dominate the budgets delivered by the provinces and territories in 2024 was affordability for their residents. The provinces and territories continued to deliver a wide range of measures in an attempt to improve affordability for their

residents and reduce the burden of everyday living. As a result, the provinces and territories generally did not introduce significant tax changes in the budgets that they delivered for the year.

Yukon and the Northwest Territories continued to forecast budgetary surpluses for the 2024-25 fiscal year, of $119 million and $294 million, respectively. Nunavut forecasted a budgetary deficit of $21 million, owing to significant investment in the community to address the territory's historical infrastructure deficit.

British Columbia's 2024 budget, tabled on February 22, 2024, shows a projected budgetary deficit of $7.9 billion for the 2024-25 fiscal year. This is largely due to the government's investments in the future of the province by way of an investment of "$13 billion more in operating funding across the fiscal plan to support a growing population and invest in new priority measures."[1] These measures are focused on easing the pressure of everyday costs, delivering more homes for people, and strengthening the services that residents are relying on.

Alberta's 2024 budget, tabled on February 29, 2024, shows a projected budgetary surplus of $367 million for the 2024-25 fiscal year. Alberta's economic outlook forecasts continued budgetary surpluses through to the 2026-27 fiscal year; however, the province's revenue is volatile owing to Alberta's reliance on non-renewable resource revenue and related corporate income tax revenue.

Saskatchewan's 2024 budget, tabled on March 20, 2024, shows a projected budgetary deficit of $273 million for the 2024-25 fiscal year, including a revision of the 2023 budget from a projected surplus of over $1 billion to a projected deficit of $483 million, largely as a result of a decrease in non-renewable resource revenue. A return to a budgetary surplus is forecast for the 2025-26 fiscal year and onward.

Manitoba's 2024 budget, tabled on April 2, 2024, shows a projected budgetary deficit of $796 million for the 2024-25 fiscal year. Like several other provinces, Manitoba has balanced budget legislation, the Fiscal Responsibility and Taxpayer Protection Act[2] (FRTPA), which requires the government not to incur a deficit greater than a baseline amount and penalizes ministers by reducing their salaries if the Act is contravened. Like other provinces, Manitoba changed the legislation to reset the baseline amount for 2020-21 to the deficit reported and allowed the government to exclude COVID-19 pandemic expenditures.[3] The 2024 budget, the first tabled by the New Democratic Party of Manitoba since it formed the government in 2023, indicates that the government inherited a historic deficit but that it is "committed to getting back to balance in four years."[4] The province's medium-term outlook forecasts a return to a small budgetary surplus by the 2027-28 fiscal year.

1 British Columbia, Ministry of Finance, 2024 Budget, Budget and Fiscal Plan, 2024/25-2026/27, February 22, 2024, at 1.

2 CCSM c. F84.

3 The Fiscal Responsibility and Taxpayer Protection Amendment Act, SM 2021, c. 42.

4 Manitoba, Department of Finance, 2024 Budget, Budget Plan, April 2, 2024, at 32.

Ontario's 2024 budget, tabled on March 26, 2024, shows a projected budgetary deficit of $9.8 billion for the 2024-25 fiscal year, despite the 2023 budget forecasting a return to a budgetary surplus by this fiscal year. Ontario states that the downward revision to the medium-term fiscal plan is due to "slower projected growth and other factors beyond the provincial government's control—such as lower tax assessments and the federal government's cap on international student study permit applications."[5]

In 2020, amendments were made to the Fiscal Sustainability, Transparency and Accountability Act, 2019[6] that paused the requirement to include a recovery plan to return to a balanced budget in the 2020-21 fiscal year. The province's 2024 budget forecasts a return to a small budgetary surplus in the 2026-27 fiscal year.

Quebec's 2024 budget, tabled on March 12, 2024, projects a budgetary deficit of almost $8.8 billion for the 2024-25 fiscal year, excluding any deposits of dedicated revenues in the Generations Fund, a fund dedicated exclusively to repaying the province's debt. Quebec's Balanced Budget Act[7] (BBA) requires that the government balance the budget within five years subsequent to a budgetary deficit arising as a result of a disaster, a significant deterioration of economic conditions, or a change in federal programs of transfer payments to the provinces that would substantially reduce transfer payments to Quebec. The 2021 budget indicated that "[t]he government wishes to suspend the effects of the *Balanced Budget Act* as of 2021-2022 in order to gradually reduce the deficit without hindering services to Quebecers or a sustainable recovery of economic growth,"[8] and amended the BBA to eliminate the obligation to table a budget that restores fiscal balance and to implement measures to reduce the budget overruns. The 2023 budget noted that "the Minister of Finance is lifting the suspension of these effects as of the end of fiscal 2022-2023."[9] Accordingly, the 2023 budget included a plan to restore the province to a balanced budget by the 2027-28 fiscal year. However, the 2024 budget forecasts a budgetary deficit "due to a significant deterioration in economic conditions compared with those prevailing when Budget 2023-2024 was tabled."[10] In accordance with the BBA, the government has committed to presenting a budget in the subsequent fiscal year with shrinking deficits that will restore fiscal balance by the 2029-30 fiscal year.

Most of the Atlantic provinces again report budgetary deficits in their budgets for the 2024-25 fiscal year. New Brunswick continues to be the exception, with its 2024 budget, tabled on March 19, 2024, forecasting a budgetary surplus of $41 million for the 2024-25 fiscal year and continued budgetary surpluses through to the

5 Ontario, Ministry of Finance, 2024 Budget, March 26, 2024, at 143.

6 SO 2019, c. 7, schedule 30.

7 CQLR c. E-12.00001.

8 Québec, Finances Québec, 2021-2022 Budget, Budget Plan, March 25, 2021, at H.23.

9 Québec, Finances Québec, 2023-2024 Budget, Budget Plan, March 21, 2023, at H.28.

10 Québec, Finances Québec, 2024-2025 Budget, Budget Plan, March 12, 2024, at G.68.

2026-27 fiscal year. Nova Scotia's 2024 budget, tabled on February 29, 2024, projects a budgetary deficit of $467 million for the 2024-25 fiscal year, with continued budgetary deficits through to the 2027-28 fiscal year. The 2024 budget states that "[t]he projected deficits reflect the government's commitment to making investments in priority areas for Nova Scotians such as healthcare, housing and affordability."[11]

Prince Edward Island's 2024 budget, tabled on February 29, 2024, projects a budgetary deficit of $85 million for the 2024-25 fiscal year and continued budgetary deficits through to the 2026-27 fiscal year, with no indication of how the province plans to return to a balanced budget. Newfoundland and Labrador's 2024 budget, delivered on March 21, 2024, projects a budgetary deficit of $152 million for the 2024-25 fiscal year, but forecasts a return to a balanced budget for the 2025-26 fiscal year onward.

Overall, the provinces and territories continued to deliver status quo budgets for the 2024-25 fiscal year, with very few income tax changes, but significant investments and budget measures to try to improve affordability for their residents.

Table 1 aggregates the projected budget revenue and expenditure items in each province and territory for the 2024-25 fiscal year. The figures reflect the budget summaries presented in the second part of this article. The different jurisdictions' budget projections are not strictly comparable, owing in part to accounting differences across the provinces and territories.[12] The placement of the various jurisdictions' figures in a single table remains useful as a way of illustrating trends and distinctions that can stimulate discussion. The provinces and territories are listed in descending order based on each jurisdiction's original budget projection of its expected tax revenue.

Figure 1 presents similar information and includes surpluses and deficits at the right of the figure. Each projected revenue source amount is shown as a percentage of total revenues, and the projected surplus or deficit is shown as a percentage of total expenditures. Figure 2 shows projected tax revenues by source as a percentage of total revenues. Figure 3 shows projected expenditures by spending category as a percentage of total expenditures, and health-care expenditures per capita.

The provinces and territories have the primary responsibility for education, health, and social services expenditures. Across all jurisdictions, health-care expenditures for the 2024-25 fiscal year averaged 39.1 percent of total expenditures, as shown

11 Nova Scotia, Department of Finance and Treasury Board, 2024 Budget, Budget Plan, February 29, 2024, at 6.

12 For a discussion of accounting differences between Canadian jurisdictions, see Colin Busby and William B.P. Robson, *Credibility on the (Bottom) Line: The Fiscal Accountability of Canada's Senior Governments, 2013*, C.D. Howe Institute Commentary no. 404 (Toronto: C.D. Howe Institute, 2014). For a reconciliation of changes in the Alberta budget, see Ronald Kneebone and Margarita Wilkins, "Recent Changes to Provincial Government Budget Reporting in Alberta" (2018) 11:1 *SPP Communiqué* [University of Calgary School of Public Policy] 1-8 (https://doi.org/10.11575/sppp.v11i0.43275).

TABLE 1 Provincial and Territorial Revenues and Expenditures, Budget Projections, Fiscal Year 2024-25

Province/territory	Tax revenue	Federal transfers	Other sources of revenue[a]	Total revenues	Total expenditures	Adjustments[b]	Surplus/ (deficit)
			millions of dollars				
Ontario	144,687	36,252	24,751	205,690	(214,496)	(1,000)	(9,806)
Quebec[c]	95,039	29,397	25,865	150,301	(157,577)	(1,500)	(8,776)
British Columbia	49,214	14,446	17,863	81,523	(89,434)		(7,911)
Alberta	28,645	12,640	32,252	73,537	(71,170)	(2,000)	367
Manitoba	10,324	8,291	4,822	23,437	(24,133)	(100)	(796)
Saskatchewan	9,723	3,780	6,359	19,862	(20,135)		(273)
Nova Scotia	8,346	5,313	2,185	15,844	(16,519)	208	(467)
New Brunswick	6,499	4,896	1,901	13,296	(13,255)		41
Newfoundland and Labrador	4,405	2,412	3,479	10,296	(10,448)		(152)
Prince Edward Island	1,557	1,251	339	3,147	(3,232)		(85)
Northwest Territories	383	2,118	132	2,633	(2,230)	(109)	294
Nunavut	171	2,665	138	2,046	(2,895)	(50)	(21)
Yukon	190	1,429	427	2,974	(1,877)	(100)	119

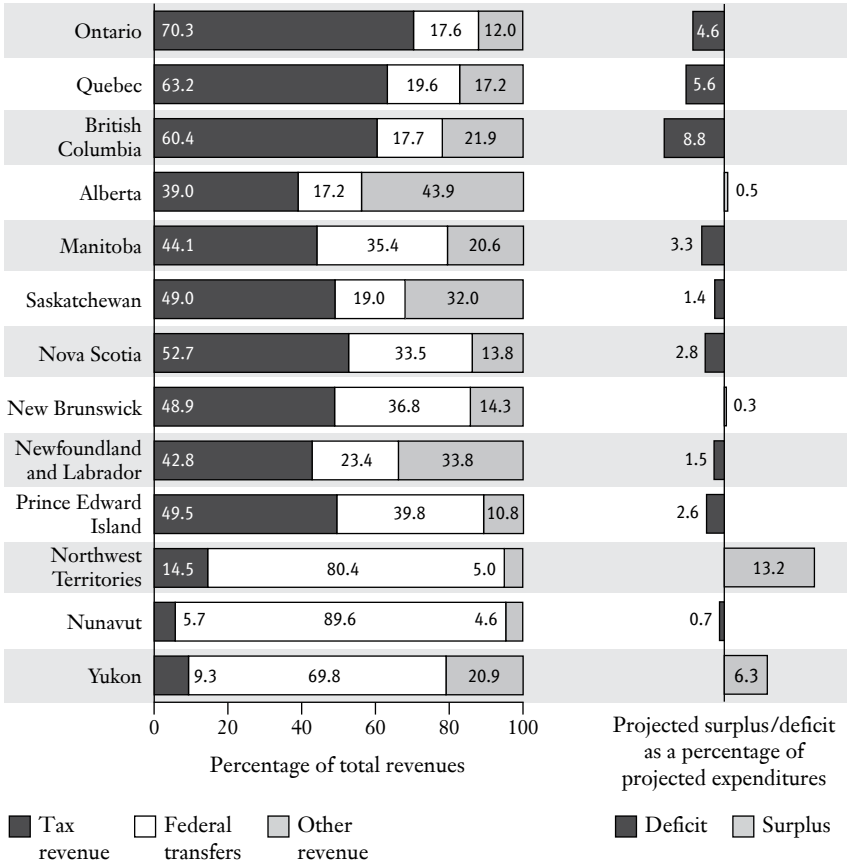
a Other sources of revenue may include, but are not limited to, resource royalties; premiums, fees, and licences; commercial Crown corporation transfers; and investment income.

b Adjustments included consolidation numbers (in some cases) and transfers to and from reserve funds.

c Taxfilers in Quebec qualify for the Quebec abatement, which reduces their federal income tax by 16.5 percentage points. Of this amount, 13.5 percentage points relate to opting-out arrangements for certain federal-provincial programs, such as hospital care and social welfare, where Quebec increased its personal income taxes by an equivalent amount. Quebec receives the value through increased provincial tax revenue, while other provinces receive the corresponding amounts in cash. The remaining 3.0 percentage points relate to the youth allowances recovery, which the federal government recovers each year from Quebec. None of the amounts presented in this table and elsewhere in this article are adjusted for the Quebec abatement.

Source: Based on provincial and territorial budget documents cited in the source notes for tables 12-24.

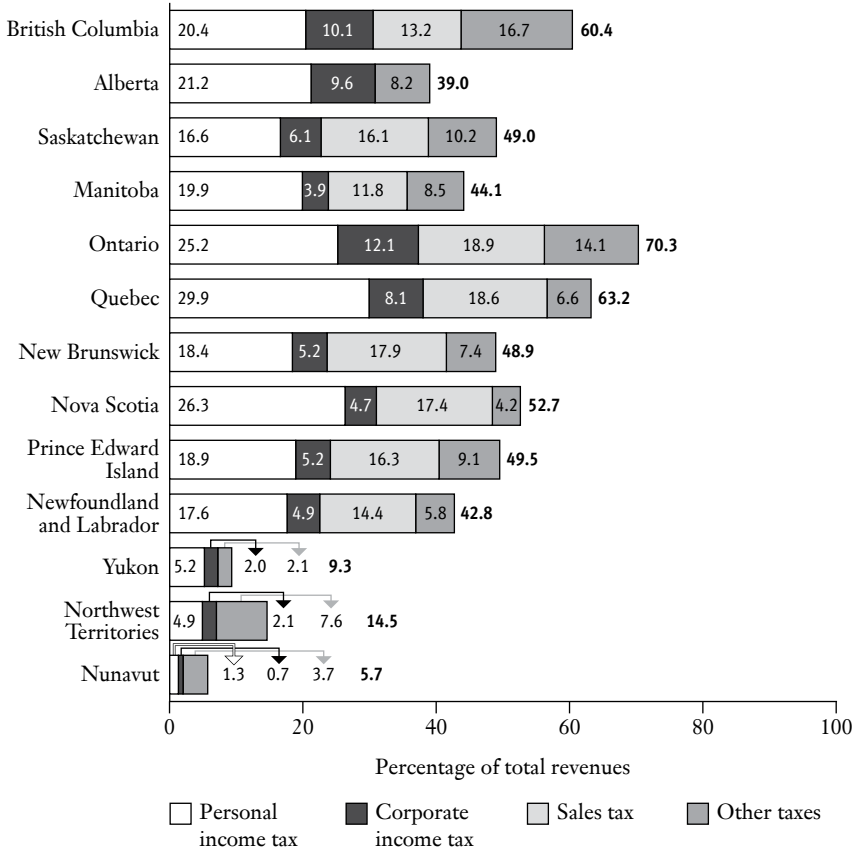
FIGURE 1 Projected Provincial and Territorial Revenues by Source, as a Percentage of Total Revenues, and Projected Surplus/Deficit as a Percentage of Projected Expenditures, Fiscal Year 2024-25



Source: Based on provincial and territorial budget documents cited in the source notes for tables 12-24 and the data summary in table 1.

in table 2. For example, for the 2024-25 fiscal year, Ontario projected health-care and long-term-care expenditures of $84,961 million, or 39.61 percent of total expenditures ($214,496 million, as shown in table 16). In contrast, in the territories, projected spending on health care in 2024-25 accounted for 18.72 percent of total expenditures for Nunavut, 28.88 percent for the Northwest Territories, and 32.18 percent for Yukon. However, on a per capita basis, the results for the territories vis-à-vis Ontario appeared to reverse. These trends are reflected in table 3, which sets out the health-care expenditures (as projected in the 2018-19 to 2024-25 budgets) as a percentage of total expenditures and per capita in Ontario and the territories.

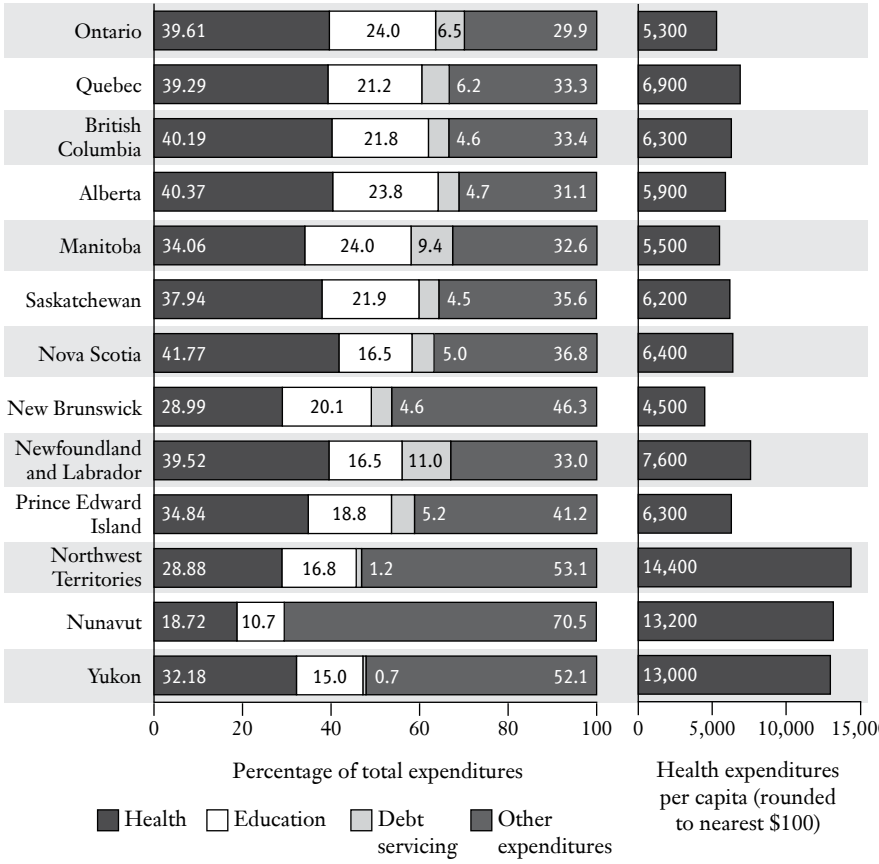
FIGURE 2 Projected Provincial and Territorial Tax Revenues by Source as a Percentage of Total Revenues, Fiscal Year 2024-25



Source: Based on provincial and territorial budget documents cited in the source notes for tables 12-24.

Table 4 sets out the health-care expenditure projections for all the provinces and territories for 2024-25 as a percentage of total expenditures and per capita. Again, these amounts may not be strictly comparable, given accounting differences in the way COVID-19-related health expenditures are reported. Some provinces and territories have carved out COVID-19-related health expenditures into separate line items that may not be reflected in the health-care expenditures reported in this table. In addition, demographic factors, including the age distribution of the population, will vary between provinces and territories, and will likely affect their health-care expenditures. An article in this feature in 2020 examined the sustainability of Canada's public debt and provincial debt given the economic shock from

FIGURE 3 Projected Provincial and Territorial Expenditures by Spending Category as a Percentage of Total Expenditures, Fiscal Year 2024-25



Source: Based on provincial and territorial budget documents cited in the source notes for tables 4 and 12-24.

the COVID-19 pandemic and the potential effect of aging on provincial health expenditures.[13]

Table 5 shows the provincial and territorial surpluses and deficits since the (revised) budget projections for 2019-20 and also includes figures set out in the most recently issued 2024-25 budgets for planned or targeted budgetary surpluses or deficits for the ensuing two, three, or four fiscal years. The short-term and medium-term outlooks in the 2024-25 budgets indicate that about half of the provinces and

13 Trevor Tombe, "Provincial Debt Sustainability in Canada: Demographics, Federal Transfers, and COVID-19," Finances of the Nation feature (2020) 68:4 *Canadian Tax Journal* 1083-1122.

TABLE 2 Provincial and Territorial Health-Care Expenditures, Budget Projections, Fiscal Years 2021-22 to 2024-25

Province/territory	Health-care expenditures				Percentage of total expenditures			
	2021-22	2022-23	2023-24	2024-25	2021-22	2022-23	2023-24	2024-25
	millions of dollars				*percent*			
Ontario	69,781	75,165	81,009	84,961	37.49	37.84	39.58	39.61
Quebec	52,358	55,842	59,015	61,909	40.35	40.18	39.91	39.29
British Columbia	26,106	27,685	30,927	35,944	40.55	38.99	38.08	40.19
Alberta	21,418	22,018	26,446	28,732	37.36	37.08	39.60	40.37
Manitoba	6,624	6,741	7,226	8,220	34.08	34.98	33.03	34.06
Saskatchewan	6,535	6,824	7,056	7,640	38.24	38.73	37.81	37.94
Nova Scotia	5,333	5,471	6,186	6,900	42.76	41.16	41.74	41.77
New Brunswick	3,097	3,266	3,623	3,843	29.15	28.87	29.81	28.99
Newfoundland and Labrador	3,420	3,592	3,795	4,129	36.60	38.13	38.53	39.52
Prince Edward Island	846	911	1,045	1,126	33.81	34.22	33.79	34.84
Northwest Territories	597	595	610	644	29.66	28.94	27.65	28.88
Nunavut	496	472	502	542	21.32	18.81	17.95	18.72
Yukon	490	510	528	604	29.38	29.11	29.78	32.18

Note: Owing to accounting differences between provinces and territories, direct comparison of the numbers above is not strictly appropriate. This is especially true for the 2021-22 through 2022-23 fiscal years because of potential variations in the reporting of COVID-19 expenditures, which would affect the health-care expenditures reported.

Source: Based on provincial and territorial budget documents cited in the source notes for tables 12-24.

TABLE 3 Health-Care Expenditures in Ontario and the Territories as a Percentage of Total Expenditures and per Capita, 2018-19 to 2024-25

	Health-care expenditures as a percentage of total expenditures				Health-care expenditures per capita	
Fiscal year	Ontario	Nunavut	Northwest Territories	Yukon	Ontario	Territorial (Nunavut, Northwest Territories, Yukon) range
	percent				*dollars*	
2018-19	38.13	18.81	26.97	32.21	4,300	10,400-11,200
2019-20	38.97	21.54	27.52	30.88	4,400	10,900-12,000
2020-21	34.56	21.31	27.53	30.29	4,400	11,000-12,600
2021-22	37.49	21.32	29.66	29.38	4,700	11,400-13,100
2022-23	37.84	18.81	28.94	29.11	5,000	11,600-13,000
2023-24	39.58	17.95	27.65	29.78	5,200	11,800-13,600
2024-25	39.61	18.72	28.88	32.18	5,300	13,000-14,400

Sources: Numbers for 2018-19 are from Vivien Morgan, "Survey of Provincial and Territorial Budgets, 2018-19," Finances of the Nation feature (2019) 67:1 *Canadian Tax Journal* 81-160, at 91. Numbers for 2019-20 through 2023-24 are from David Lin, "Survey of Provincial and Territorial Budgets, 2019-20," Finances of the Nation feature (2020) 68:1 *Canadian Tax Journal* 185-250, at 196; "Survey of Provincial and Territorial Budgets, 2020-21," Finances of the Nation feature (2021) 69:1 *Canadian Tax Journal* 145-215, at 156; "Survey of Provincial and Territorial Budgets, 2021-22," Finances of the Nation feature (2022) 70:1 *Canadian Tax Journal* 125-85, at 136; "Survey of Provincial and Territorial Budgets, 2022-23," Finances of the Nation feature (2023) 71:1 *Canadian Tax Journal* 217-72, at 228; and "Survey of Provincial and Territorial Budgets, 2023-24," Finances of the Nation feature (2024) 72:1 *Canadian Tax Journal* 131-82, at 142. Numbers for 2024-25 are from this article. Population data are from Statistics Canada table 17-10-0009-01 (formerly CANSIM table 051-0005), "Population Estimates, Quarterly," averaged for the 2024 calendar year (www150.statcan.gc.ca/t1/tbl1/en/tv.action?pid=1710000901). Because the budget numbers were estimated and the population data can vary, the per capita numbers are rounded to the nearest hundred dollars.

territories expect to remain in or return to balanced budget positions in future years. British Columbia, Quebec, Nova Scotia, Prince Edward Island, and Nunavut are forecasting budgetary deficits in future fiscal years without a forecasted return to a balanced budget. These projections are subject to changes in the economic forecasts made at the time the budgets were prepared, which could prove to be significant.

On the basis of budget projections in the tables set out in the second part of this article, projected aggregate income tax revenue in the 2024-25 budgets of all provinces and territories was $146.4 billion from personal income tax and $56.6 billion from corporate income tax, for total revenue of $203.0 billion from income tax. Projected aggregate sales tax revenue was $90.7 billion, for a total of $147.3 billion from sources other than personal income tax (that is, corporate income tax and sales tax). Bucking the trend that has been established since 2014, in 2024-25 the provinces and territories expect to collect more tax revenue from corporate tax and sales tax combined than from personal income tax. This appears to be driven by a

TABLE 4 Health-Care Expenditures as a Percentage of Total Expenditures and per Capita, Budget Projections, 2024-25

Province/territory	Health-care expenditures	Population	Health-care expenditures as a percentage of total expenditures	Health-care expenditures per capita
	millions of dollars	*'000s*	%	*dollars*
British Columbia	35,944	5,678.2	40.19	6,300
Alberta	28,732	4,863.7	40.37	5,900
Saskatchewan	7,640	1,236.6	37.94	6,200
Manitoba	8,220	1,488.8	34.06	5,500
Ontario	84,961	16,068.5	39.61	5,300
Quebec	61,909	9,029.0	39.29	6,900
New Brunswick	3,843	851.3	28.99	4,500
Nova Scotia	6,900	1,073.9	41.77	6,400
Prince Edward Island	1,126	177.9	34.84	6,300
Newfoundland and Labrador	4,129	544.0	39.52	7,600
Yukon	604	46.5	32.18	13,000
Northwest Territories	644	44.7	28.88	14,400
Nunavut	542	41.0	18.72	13,200

Note: Owing to accounting differences between provinces and territories, direct comparison of the numbers above is not strictly appropriate. Because the budget numbers were estimated and the population data can vary, the per capita numbers are rounded to the nearest hundred dollars.

Sources: Table 2; and population data from Statistics Canada table 17-10-0009-01 (formerly CANSIM table 051-0005), "Population Estimates, Quarterly," averaged for the 2024 calendar year (www150.statcan.gc.ca/t1/tbl1/en/tv.action?pid=1710000901).

slowdown in the growth of personal income tax and corporate income tax revenues forecasted by the provinces and territories in 2024-25. Surprisingly, the 2024 federal fall economic statement projects continued growth in both personal income tax revenue and corporate income tax revenue for the 2024-25 fiscal year, with $232.6 billion of revenue forecasted from personal income tax, $86.8 billion from corporate income tax, and $13.5 billion from non-resident income tax, for a total of $332.9 billion from income tax, plus $51.9 billion from sales tax[14]—for a total of $152.2 billion from sources other than personal income tax (corporate income tax, non-resident income tax, and sales tax). The 2024 federal fall economic statement notes that the increase in personal income tax revenues is "[d]ue to stronger than expected employment growth and rising wages."[15] See table 6 for a tabular

14 Canada, Department of Finance, Fall Economic Statement, December 16, 2024, at 196, table A1.7.

15 Ibid., at 197.

TABLE 5 Revised, Projected, and Planned Provincial and Territorial Surpluses and Deficits, 2019-20 and Onward

Province/territory	2019-20 budget [revised]	2020-21 budget[a] [revised]	2021-22 budget [revised]	2022-23 budget [revised]	2023-24 budget [revised]	2024-25 plan	2025-26 plan	2026-27 plan	2027-28 plan	2028-29 plan
					millions of dollars					
British Columbia	274 [1,354]	(13,643) [(8,144)]	(9,698) [(483)]	(5,461) [3,592]	(4,216) [(5,914)]	(7,911)	(7,773)	(6,288)		
Alberta	(8,704) [12,152]	(21,239) [(20,192)]	(18,221) [(3,207)]	511 [10,390]	2,371 [5,234]	367	1,437	2,640		
Saskatchewan	34 [(319)]	(2,130) [(1,865)]	(2,611) [(2,185)]	(463) [1,147]	1,018 [(483)]	(273)	19	225	340	
Manitoba	(360) [(325)]	(2,048) [(2,080)]	(1,597) [(1,393)]	(548) [(378)]	(363) [(1,997)]	(796)	(532)	(266)	18	
Ontario	(9,024) [(8,672)]	(38,468) [(38,468)]	(33,108) [(13,496)]	(19,850) [(2,170)]	(1,313) [(2,977)]	(9,806)	(4,600)	500		
Quebec	2,504 [2,638]	(338) [(3,226)]	(9,170) [(3,897)]	(3,005) [(1,670)]	(1,625) [(4,221)]	(8,776)	(6,267)	(1,790)	(1,390)	(1,269)
New Brunswick	23 [98]	(299) [(13)]	(245) [488]	35 [863]	41 [247]	41	39	30		
Nova Scotia	34 [41]	(779) [(706)]	(585) [108]	(506) [(259)]	(279) [40]	(467)	(609)	(576)	(360)	
Prince Edward Island	2 [(4)]	(173) [(120)]	(112) [(27)]	(93) [(66)]	(98) [(86)]	(85)	(60)	(31)		

(Table 5 is concluded on the next page.)

TABLE 5 Concluded

Province/territory	2019-20 budget [revised]	2020-21 budget[a] [revised]	2021-22 budget [revised]	2022-23 budget [revised]	2023-24 budget [revised]	2024-25 plan	2025-26 plan	2026-27 plan	2027-28 plan	2028-29 plan
					millions of dollars					
Newfoundland and Labrador	1,924 [1,114]	(1,838) [(1,644)]	(825) [(400)]	(351) [784]	(160) [(433)]	(152)	58	52	68	60
Yukon	(6) [(19)]	4 [(7)]	(7) [25]	39 [44]	48 [2]	119	128	74	142	82
Northwest Territories	60 [(70)]	203 [(31)]	69 [28]	131 [3]	178 [(150)]	294	316	195	123	
Nunavut	(34) [(56)]	(30) [(21)]	(14) [16]	40 [68]	(8) [(15)]	(21)	(181)	(44)		

a Because of COVID-19, the budgeted amounts presented are from the province's or territory's budget or fiscal update, whichever was released later in the year.

Source: Based on provincial and territorial budget documents cited in the source notes for tables 12-24.

TABLE 6 Comparison of Projected Revenues from Personal and Corporate Income Tax, Sales Tax, and Non-Resident Tax—Federal, Provincial, and Territorial Jurisdictions, 2018-19 to 2024-25

	Federal						Provincial and territorial				
	PIT	CIT	Non-resident tax	Sales tax	Income tax	Non-PIT	PIT	CIT	Sales tax	Income tax	Non-PIT
Fiscal year	(1)	(2)	(3)	(4)	(1+2+3)	(2+3+4)	(5)	(6)	(7)	(5+6)	(6+7)
						millions of dollars					
2018-19	161.4	47.3	8.3	37.7	217.0	93.3	99.9	34.2	64.6	134.0	98.8
2019-20	170.4	46.3	9.7	40.8	226.4	96.8	105.8	35.8	67.1	141.5	102.8
2020-21	162.1	39.2	9.9	29.4	211.2	78.5	107.2	26.0	60.4	133.2	86.4
2021-22	185.6	57.3	10.6	42.0	253.5	109.9	108.4	30.4	68.4	138.8	98.8
2022-23	209.4	91.0	13.8	47.2	314.2	152.0	126.7	43.6	78.5	170.3	122.1
2023-24	218.0	79.8	13.4	52.1	311.2	145.3	145.5	54.5	84.4	200.0	138.9
2024-25	232.6	86.8	13.5	51.9	332.9	152.2	146.4	56.6	90.7	203.0	147.3

CIT = corporate income tax; PIT = personal income tax.

Sources: Numbers for 2018-19 are from Vivien Morgan, "Survey of Provincial and Territorial Budgets, 2018-19," Finances of the Nation feature (2019) 67:1 *Canadian Tax Journal* 81-160, at 96. Numbers for 2019-20 through 2023-24 are from David Lin, "Survey of Provincial and Territorial Budgets, 2019-20," Finances of the Nation feature (2020) 68:1 *Canadian Tax Journal* 185-250, at 200; "Survey of Provincial and Territorial Budgets, 2020-21," Finances of the Nation feature (2021) 69:1 *Canadian Tax Journal* 145-215, at 161; "Survey of Provincial and Territorial Budgets, 2021-22," Finances of the Nation feature (2022) 70:1 *Canadian Tax Journal* 125-85, at 141; "Survey of Provincial and Territorial Budgets, 2022-23," Finances of the Nation feature (2023) 71:1 *Canadian Tax Journal* 217-72, at 232; and "Survey of Provincial and Territorial Budgets, 2023-24," Finances of the Nation feature (2024) 72:1 *Canadian Tax Journal* 131-82, at 146. Numbers for 2024-25 are from this article and from Canada, Department of Finance, Fall Economic Statement, December 16, 2024, at 196, table A1.7.

TABLE 6A Projected Tax Revenues for Provinces and Territories, by Category and per Capita, 2024-25

Province/territory	PIT	CIT	Sales tax	Other	Total	Per capita
			millions of dollars			*dollars*
British Columbia	16,638	8,236	10,762	13,578	49,214	8,700
Alberta	15,604	7,028	na	6,013	28,645	5,900
Saskatchewan	3,295	1,209	3,196	2,023	9,723	7,900
Manitoba	4,670	918	2,754	1,982	10,324	6,900
Ontario	51,936	24,915	38,832	29,004	144,687	9,000
Quebec	44,952	12,116	27,991	9,980	95,039	10,500
New Brunswick	2,440	690	2,381	988	6,499	7,600
Nova Scotia	4,174	749	2,756	667	8,346	7,800
Prince Edward Island	594	164	514	285	1,557	8,800
Newfoundland and Labrador	1,816	506	1,486	597	4,405	8,100
Yukon	107	41	na	42	190	4,100
Northwest Territories	128	56	na	199	383	8,600
Nunavut	40	21	na	110	171	4,200
Total and per capita average	146,394	56,649	90,672	65,468	359,183	8,700

CIT = corporate income tax; PIT = personal income tax.

Sources: Based on provincial and territorial budget documents cited in the source notes for tables 12-24, and on population data from Statistics Canada table 17-10-0009-01 (formerly CANSIM table 051-0005), "Population Estimates, Quarterly" averaged for the 2024 calendar year (www150.statcan.gc.ca/t1/tbl1/en/tv.action?pid=1710000901).

presentation of the revenue projections set out above, compared to projections for fiscal years 2018-19 to 2023-24. Table 6A shows the projected tax revenues for each province and territory as detailed in the 2024-25 budgets, including total and per capita amounts.

Table 7 shows the statutory corporate income tax rates in the provinces and territories for 2024.

From a personal income tax perspective, most jurisdictions have established a higher tax rate bracket for high income earners over the past decade. Prince Edward Island's 2023 budget introduced personal income tax reform measures, replacing its previous three brackets with five brackets and eliminating the surtax effective for the 2024 taxation year. These changes increased the top combined marginal tax rate in the province from 51.37 percent in 2023 to 51.75 percent in 2024. With the implementation of Prince Edward Island's tax reform measures, Ontario is the only province or territory in Canada that continues to charge a surtax on high income earners.

Personal income tax amounts are indexed for inflation in most provinces and all three territories. In 2024, there are only two provinces that do not automatically index personal income tax amounts for inflation: Nova Scotia and Prince Edward Island. Nova Scotia's 2024 budget introduces the automatic indexation of personal

TABLE 7 Provincial and Territorial Corporate Income Tax Rates, 2024

Province/territory	General rate	M & P rate	Small business rate	Small business limit[a]
		percent		*dollars*
British Columbia	12.0	12.0	2.0	500,000
Alberta	8.0	8.0	2.0	500,000
Saskatchewan[b]	12.0	10.0	1.0	600,000
Manitoba	12.0	12.0	0.0	500,000
Ontario	11.5	10.0[c]	3.2	500,000
Quebec	11.5	11.5	3.2	500,000
New Brunswick	14.0	14.0	2.5	500,000
Nova Scotia	14.0	14.0	2.5	500,000
Prince Edward Island	16.0	16.0	1.0	500,000
Newfoundland and Labrador[d]	15.0	15.0	2.5	500,000
Yukon	12.0	2.5	0.0	500,000
Northwest Territories	11.5	11.5	2.0	500,000
Nunavut	12.0	12.0	3.0	500,000

M & P = manufacturing and processing.

a The small business limit is reduced by the greater of $0.10 ($0.12 in Saskatchewan) for every $1 of taxable capital employed in Canada in the preceding year by the Canadian-controlled private corporation (CCPC) on an associated basis in excess of $10 million and $5 ($6 in Saskatchewan) for every $1 of passive investment income earned by the CCPC on an associated basis in excess of $50,000 (except in Ontario and New Brunswick). This business limit is shared by all associated CCPCs.

b Saskatchewan's small business rate was reduced to 0 percent effective October 1, 2020. However, the small business rate was scheduled to increase to 1 percent effective July 1, 2022, and 2 percent (the small business rate in effect prior to the reduction in 2020) effective July 1, 2023. In August 2022, the Saskatchewan four-point affordability plan extended the small business rate reduction and delayed restoration of the rate to 2 percent until July 1, 2024. On July 1, 2023, the small business corporate tax rate increased from 0 to 1 percent because of the delayed restoration of the small business rate. Saskatchewan's 2024 budget delayed the restoration of the small business rate for an additional year until July 1, 2025.

c In Ontario, the M & P rate applies to income from manufacturing, processing, farming, mining, logging, and fishing operations carried on in Canada and allocated to the province.

d Newfoundland and Labrador's 2024 budget reduced the small business rate from 3 percent to 2.5 percent, effective January 1, 2024.

Source: Based on provincial and territorial budget documents cited in the source notes for tables 12-24.

income tax amounts for inflation effective for the 2025 taxation year. As part of the personal income tax reform measures introduced by Prince Edward Island in its 2023 budget, the province's new 2024 brackets appear to have been adjusted for inflation compared to the brackets that were in effect for the 2023 taxation year. Further, Prince Edward Island's 2024 budget notes that the government "will continue to reform our tax system by raising the thresholds of each tax bracket and lowering the tax rates for the first four brackets,"[16] which is slightly short of introducing automatic indexation for inflation.

All federal, provincial, and territorial marginal personal income tax rates on ordinary income and interest, as well as surtaxes, are shown in graphic form in figure 4 as a function of taxable income. Table 8 sets out the provincial and territorial personal income tax brackets and rates for 2024.

Table 9 shows the sales tax rates in each jurisdiction for 2024. British Columbia, Saskatchewan, and Manitoba imposed a separate provincial sales tax (PST). Ontario and the Atlantic provinces—Newfoundland and Labrador, Nova Scotia, New Brunswick, and Prince Edward Island—are harmonized sales tax (HST) participating provinces that harmonize sales taxes with the federal goods and services tax (GST). Quebec has its own Quebec sales tax (QST), which applies in a manner similar to the GST. Alberta and the three territories do not impose their own sales taxes. There were no changes to provincial or territorial sales tax rates in 2024.

PROVINCIAL AND TERRITORIAL BUDGETS BY JURISDICTION

Table 10 summarizes the dates of the 2024-25 budgets for the various provinces and territories, the name and title of the person who delivered the budget, and the estimated budgetary surplus or deficit.

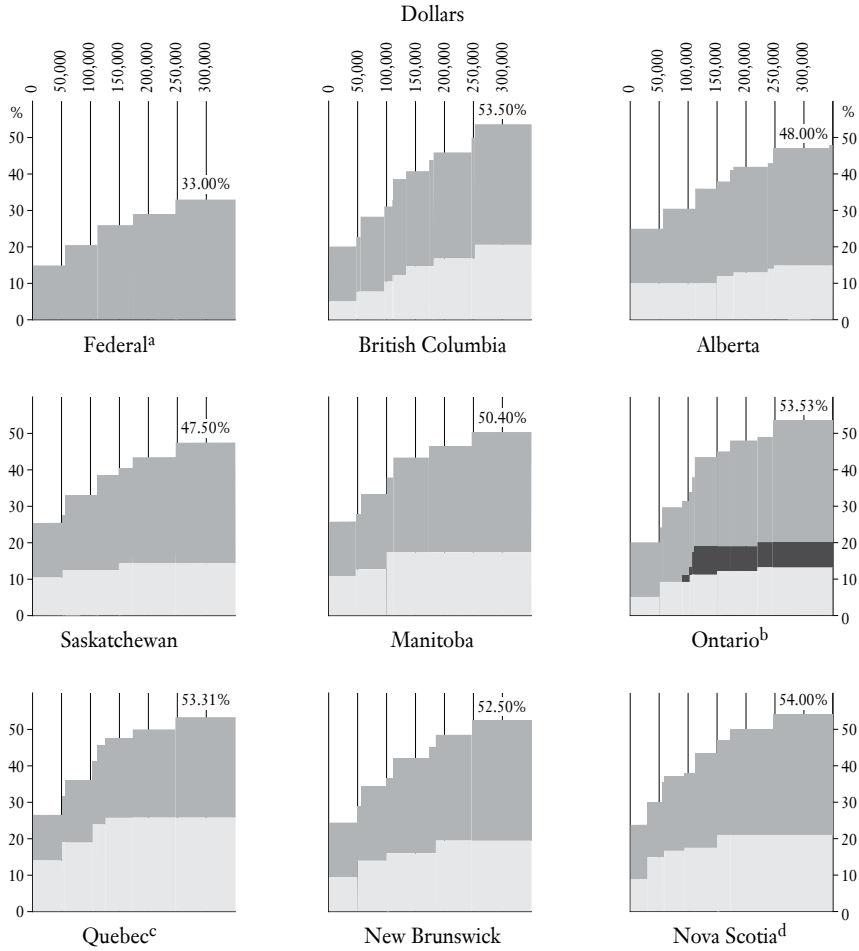
Table 11 sets out the research and development (R & D) tax credits in each province and territory available in 2024. The table details rates and indicates whether the credit is refundable and otherwise eligible for a carryforward period. In some cases, the credit is also available to an individual. An article in this feature in 2017 focused on the policy behind these subsidies from an economic viewpoint.[17]

The second part of this article presents, for each province and territory, selected fiscal figures, highlights of tax changes, and a narrative summary of tax changes with accompanying tables. The figures for any particular jurisdiction are difficult to compare across jurisdictions owing to differences in accounting and fiscal reporting. Where relevant, and where the information is accessible, notes that refer to differences in accounting and/or presentation are appended to the tables; it is beyond the

16 Prince Edward Island, Department of Finance, 2024 Budget, Budget Address, February 29, 2024, at 14.

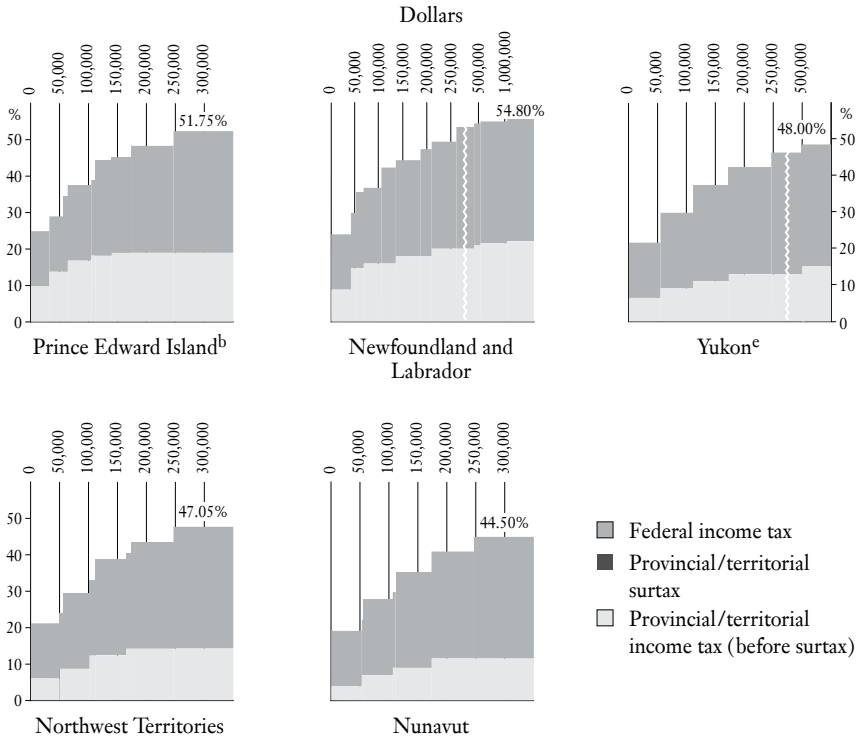
17 Daria Crisan and Kenneth J. McKenzie, "Tax Subsidies for R & D in Canada, 1981-2016," Finances of the Nation feature (2017) 65:4 *Canadian Tax Journal* 951-81.

FIGURE 4 Personal Income Tax Marginal Rates Applicable to Taxable Income, 2024



(Figure 4 is concluded on the next page.)

FIGURE 4 Concluded



a The federal basic personal amount is reduced when a taxpayer's net income is $173,205 or more. The federal rates presented do not reflect this clawback of the basic personal amount.

b Surtax calculations assume that the only credit claimed by the taxpayer is the basic personal amount.

c Federal income tax has been reduced by 16.5 percentage points to reflect the provincial abatement.

d Nova Scotia's basic personal amount is increased by up to $3,000 if taxable income is under $75,000. The provincial rates do not reflect the tax savings from an increased basic personal amount.

e Yukon's basic personal amount is reduced when a taxpayer's net income is $173,205 or more. The territorial tax rates presented do not reflect this clawback of the basic personal amount.

Source: Data compiled by the author.

TABLE 8 Provincial and Territorial Personal Income Tax Brackets and Rates, 2024

Province/territory	Tax bracket	Rate	Surtax (percentage of regular tax) and top combined rate[a]
	dollars	*percent*	
British Columbia	0 to 47,937	5.06	
	over 47,937 to 95,875	7.70	
	over 95,875 to 110,076	10.50	
	over 110,076 to 133,664	12.29	
	over 133,664 to 181,232	14.70	
	over 181,232 to 252,752	16.80	
	over 252,752	20.50	Top combined rate of 53.50%
Alberta	0 to 148,269	10.00	
	over 148,269 to 177,922	12.00	
	over 177,922 to 237,230	13.00	
	over 237,230 to 355,845	14.00	
	over 355,845	15.00	Top combined rate of 48.00%
Saskatchewan	0 to 52,057	10.50	
	over 52,057 to 148,734	12.50	
	over 148,734	14.50	Top combined rate of 47.50%
Manitoba[b]	0 to 47,000	10.80	
	over 47,000 to 100,000	12.75	
	over 100,000	17.40	Top combined rate of 50.40%
Ontario	0 to 51,446	5.05	Surtax equal to 20% of basic provincial tax greater than $5,554
	over 51,446 to 102,894	9.15	Additional surtax equal to 36% of basic provincial tax greater than $7,108
	over 102,894 to 150,000	11.16	
	over 150,000 to 220,000	12.16	
	over 220,000	13.16	Top combined rate of 53.53%
Quebec	0 to 51,780	14.00	
	over 51,780 to 103,545	19.00	
	over 103,545 to 126,000	24.00	
	over 126,000	25.75	Top combined rate of 53.31%
New Brunswick	0 to 49,958	9.40	
	over 49,958 to 99,916	14.00	
	over 99,916 to 185,064	16.00	
	over 185,064	19.50	Top combined rate of 52.50%
Nova Scotia[c]	0 to 29,590	8.79	
	over 29,590 to 59,180	14.95	
	over 59,180 to 93,000	16.67	
	over 93,000 to 150,000	17.50	
	over 150,000	21.00	Top combined rate of 54.00%

(Table 8 is concluded on the next page.)

TABLE 8 Concluded

Province/territory	Tax bracket	Rate	Surtax (percentage of regular tax) and top combined rate[a]
	dollars	*percent*	
Prince Edward Island[d]	0 to 32,656	9.65	
	over 32,656 to 64,313	13.63	
	over 64,313 to 105,000	16.65	
	over 105,000 to 140,000	18.00	
	over 140,000	18.75	Top combined rate of 51.75%
Newfoundland and Labrador	0 to 43,198	8.70	
	over 43,198 to 86,395	14.50	
	over 86,395 to 154,244	15.80	
	over 154,244 to 215,943	17.80	
	over 215,943 to 275,870	19.80	
	over 275,870 to 551,739	20.80	
	over 551,739 to 1,103,478	21.30	
	over 1,103,478	21.80	Top combined rate of 54.80%
Yukon	0 to 55,867	6.40	
	over 55,867 to 111,733	9.00	
	over 111,733 to 173,205	10.90	
	over 173,205 to 500,000	12.80	
	over 500,000	15.00	Top combined rate of 48.00%
Northwest Territories	0 to 50,597	5.90	
	over 50,597 to 101,198	8.60	
	over 101,198 to 164,525	12.20	
	over 164,525	14.05	Top combined rate of 47.05%
Nunavut	0 to 53,268	4.00	
	over 53,268 to 106,537	7.00	
	over 106,537 to 173,205	9.00	
	over 173,205	11.50	Top combined rate of 44.50%

a The top federal rate, used to arrive at the top combined rate, is 33 percent.
b Manitoba's 2023 budget increased the thresholds for all individual tax brackets for 2024, returning to annual indexation in 2025.
c Personal tax brackets are not indexed for inflation in 2024. Nova Scotia's 2024 budget introduces indexation, effective for the 2025 taxation year.
d Personal tax brackets are not indexed for inflation. Prince Edward Island's 2023 budget announced personal income tax bracket reform, including the elimination of the surtax, which came into effect for the 2024 taxation year.

Source: Based on provincial and territorial budget documents cited in the source notes for tables 12-24.

TABLE 9 Provincial and Territorial Sales Tax Rates, Percent, 2024

Province/territory	GST or federal portion of HST	Provincial portion of HST	PST and QST	Combined[a]
British Columbia	5		7	12
Alberta	5			5
Saskatchewan	5		6	11
Manitoba	5		7	12
Ontario	5	8		13
Quebec	5		9.975	14.975
New Brunswick	5	10		15
Nova Scotia	5	10		15
Prince Edward Island	5	10		15
Newfoundland and Labrador	5	10		15
Yukon	5			5
Northwest Territories	5			5
Nunavut	5			5

GST = goods and services tax; HST = harmonized sales tax; PST = provincial sales tax; QST = Quebec sales tax.

a The rates shown do not yield comparable tax burdens for all jurisdictions. For example, GST and HST allow input tax credits for underlying taxes, eliminate sales tax on exports, and also cover a wider range of goods and services than PST.

Source: Based on provincial and territorial budget documents cited in the source notes for tables 12-24.

scope of this article to analyze differing accounting practices of each jurisdiction and the differences in those practices between jurisdictions. Notes to each table also refer to the jurisdiction's significant resource revenue, if any. The "tax highlights" box at the beginning of each provincial/territorial section contains some of the more important tax changes and, where possible, lists them in order of precedence. The narrative summaries of tax changes are categorized under the following eight headings:

1. ***Corporate income tax:*** rates, credits, deductions, inclusions, reporting, business income matters, and other items.
2. ***Personal income tax:*** rates, credits, deductions, inclusions, and other items. This category may include the taxation of unincorporated businesses.
3. ***Sales tax:*** HST, GST, PST, QST.
4. ***Excise taxes:*** alcohol, tobacco, cannabis, and carbon taxes.
5. ***Resource-related matters:*** resource deductions, credits, royalties, and other items.

TABLE 10 Provincial and Territorial Surplus/(Deficit) Projections, Fiscal Year 2024-25

Province/territory	Budget date	Finance minister	Projected surplus/ (deficit)
			millions of dollars
British Columbia	February 22, 2024	Brenda Bailey	(7,911)
Alberta	February 29, 2024	Nate Horner[a]	367
Saskatchewan	March 20, 2024	Jim Reite[b]	(273)
Manitoba	April 2, 2024	Adrien Sala	(796)
Ontario	March 26, 2024	Peter Bethlenfalvy	(9,806)
Quebec	March 12, 2024	Eric Girard[c]	(8,776)
New Brunswick	March 19, 2024	René Legacy[d]	41
Nova Scotia	February 29, 2024	John A. Lohr[e]	(467)
Prince Edward Island	February 29, 2024	Jill Burridge[f]	(85)
Newfoundland and Labrador	March 21, 2024	Siobhan Coady[g]	(152)
Yukon	March 7, 2024	Sandy Silver[h]	119
Northwest Territories	May 24, 2024	Caroline Wawzonek	294
Nunavut	February 26, 2024	Lorne Kusugak	(21)

a President of the Treasury Board and minister of finance.
b Minister of finance and deputy premier.
c Minister of finance and minister responsible for relations with English-speaking Quebecers.
d Minister of finance and Treasury Board.
e Minister of finance and Treasury Board.
f Minister of finance and chair of the Treasury Board.
g Minister of finance and deputy premier.
h Premier and minister of finance.

Source: Based on provincial and territorial budget documents cited in the source notes for tables 12-24.

6. ***Real estate taxes:*** land transfer taxes, property taxes, and taxes targeting real estate activities.
7. ***Pensions:*** includes proposed studies.
8. ***Other:*** a catchall category that includes corporate capital tax, general anti-avoidance rule and other anti-avoidance initiatives, partnership and trust matters not covered above, and other items.

These categories have been selected for organizational purposes and for ease of reference only. Some categories may overlap (for example, categories 1, 2, 4, and 5).

TABLE 11 Provincial and Territorial Research and Development (R & D) Tax Credits, 2024[a]

Province/territory	R & D tax credit rate (%)	Is credit refundable?	Unused credits: Carryback (taxation years)	Unused credits: Carryforward (taxation years)	Who can claim the credit?
Alberta[b]	8 to 20	✓	na	na	Corporation[c]
British Columbia					
Qualifying CCPC[d]	10	✓	na	na	Corporation
Other corporation	10	✗	3	10	Corporation
Manitoba	15	✓[e]/✗	3	20	Corporation
New Brunswick	15	✓	na	na	Corporation
Newfoundland and Labrador	15	✓	na	na	Corporation and individual
Northwest Territories	na	na	na	na	
Nova Scotia	15	✓	na	na	Corporation
Nunavut	na	na	na	na	
Ontario					
Innovation tax credit[f]	8	✓	na	na	Corporation
Business research institute tax credit[g]	20	✓	na	na	Corporation
R & D tax credit	3.5	✗	3	20	Corporation
Prince Edward Island	na	na	na	na	
Quebec[h]					
R & D wage tax/ credit[i]	14 to 30	✓	na	na	Corporation and individual
University R & D tax credit[j]	14 to 30	✓	na	na	Corporation and individual
Private partnership pre-competitive tax credit[k]	14 to 30	✓	na	na	Corporation and individual
Tax credit on fees paid to a research consortium	14 to 30	✓	na	na	Corporation and individual
Saskatchewan[l]					
Qualifying CCPC[m]	10	✓	na	na	Corporation
Other corporation	10	✗	3	10	Corporation
Yukon	15[n]	✓	na	na	Corporation and individual

na = not available; CCPC = Canadian-controlled private corporation.

(Table 11 is continued on the next page.)

TABLE 11 Continued

a Provincial and territorial tax credits are government assistance for federal tax purposes and thus reduce expenditures eligible for the federal R & D deduction and federal tax credit.

b In the 2019 budget, the Alberta government withdrew the R & D tax credit. Eligible R & D expenses incurred in 2020 will no longer qualify for any Alberta R & D tax credit. Alberta's recovery plan released in late 2020 announced a new innovation employment grant (IEG), which is similar to the previous Alberta R & D tax credit and is available for Alberta R & D expenditures incurred after December 31, 2020. The IEG provides a refundable credit of a base 8 percent of the corporation's eligible Alberta R & D expenditures plus an incremental 12 percent of the corporation's eligible Alberta R & D expenditures that exceed its "base amount" of expenditures (generally, the corporation's average eligible Alberta R & D expenditures for the two immediately preceding taxation years). The IEG is available on up to $4 million of eligible Alberta R & D expenditures for a corporation, which is subject to a grind if taxable capital employed in Canada exceeds $10 million.

c When R & D is carried on by a partnership, the R & D credit can generally be claimed by corporate partners except in Newfoundland and Labrador, Quebec, and Yukon, where an individual partner can also claim the credit. However, the credit cannot ever be claimed from a partnership that carries on its R & D in other provinces, such as Ontario (except for certain programs).

d British Columbia's refundable R & D tax credit is 10 percent of the lesser of (1) eligible BC R & D expenditures and (2) the federal R & D expenditure limit (to a maximum annual credit of $300,000).

e Manitoba's credit is (1) fully refundable for eligible R & D expenditures incurred in Manitoba by a corporation that has a Manitoba permanent establishment and a contract with a qualifying research institute, and (2) 50 percent refundable for in-house R & D expenditures.

f The Ontario innovation tax credit is available on up to $3 million of expenditures for a corporation that has taxable income under $500,000 and taxable capital under $25 million (to a maximum annual credit of $240,000). A corporation is eligible for a partial credit if its taxable income is over $500,000 but less than $800,000 or its taxable capital is between $25 million and $50 million. All current expenditures are eligible. Taxable income and taxable capital thresholds are set in the previous year on a worldwide associated basis.

g The Ontario business research institute tax credit applies to 20 percent of qualifying payments (up to $20 million annually on an associated basis) to an Ontario eligible research institute (to a maximum annual credit of $4 million).

h For all Quebec R & D tax credits, the following rates and conditions apply:
   1. Quebec Canadian-controlled corporations that have fewer than $50 million in assets can claim the 30 percent rate on up to $3 million of R & D wages and/or eligible R & D expenditures for each credit. If assets held are between $50 million and $75 million, the rate is gradually reduced to 14 percent, which is the rate for all other taxpayers. The rates are higher in certain cases. Asset thresholds are set in the previous year on a worldwide associated basis (consolidated).
   2. The tax credit rate is 14 percent for Quebec corporations controlled by non-residents. Asset thresholds do not apply.
   3. An exclusion threshold is allocated among the Quebec R & D tax credits proportionally to the amount of eligible expenditures of each R & D tax credit. For each R & D tax credit, the eligible R & D expenditures are reduced by the allocated exclusion, which varies depending on the company's assets. The exclusion is
      a. $50,000 for a corporation whose assets are $50 million or less,
      b. an amount that increases linearly between $50,000 and $225,000 for a corporation whose assets are between $50 million and $75 million, and
      c. $225,000 for a corporation whose assets are $75 million or more.

   Asset thresholds are set in the previous year and are not on an associated basis.

(Table 11 is concluded on the next page.)

TABLE 11 Concluded

i A payment may be eligible for the Quebec R & D wage tax credit if the payment was made to (1) an arm's-length subcontractor (up to 50 percent of the payment) or (2) a non-arm's-length subcontractor (100 percent for wages paid and 50 percent of a payment to an arm's-length subcontractor if the payment was made under the non-arm's-length contract).

j Quebec's university R & D tax credit may be available on 80 percent of a payment to an eligible entity such as a university, a public research centre, or a research consortium.

k For the Quebec private partnership pre-competitive tax credit, a qualified expenditure may include (1) wages paid relating to R & D, (2) 80 percent of a payment to an arm's-length subcontractor (generally excluding a university, a public research centre, and a research consortium contract), (3) payment for some materials, or (4) payment for an overhead (or proxy) amount.

l Saskatchewan's total refundable and non-refundable tax credits are capped at $1 million per taxation year.

m Saskatchewan's refundable R & D tax credit is 10 percent of the lesser of (1) eligible Saskatchewan R & D expenditures and (2) $1 million in qualifying expenditures (the maximum annual refundable credit is $100,000).

n Yukon's rate is 20 percent for R & D expenditures made to Yukon College.

Source: Based on table 11 in David Lin, "Survey of Provincial and Territorial Budgets, 2019-20," Finances of the Nation feature (2020) 68:1 *Canadian Tax Journal* 185-250, at 209-11, updated by the author to include changes since 2019.

British Columbia (Table 12)

Tax Highlights

- No changes to corporate or personal income tax rates
- Introduction of residential home-flipping tax

Tax Changes

1. Corporate Income Tax

The 2024 budget amends the regional and distant location tax credit to exclude animation productions from eligibility effective June 1, 2024. The 2024 budget also amends the mining exploration tax credit to exclude oil and gas exploration expenditures from eligibility effective February 23, 2024.

Further, the 2024 budget extends the training tax credit for employers for three years, to the end of 2027, and the shipbuilding and ship repair industry tax credit for two years, to the end of 2026.

2. Personal Income Tax

The 2024 budget introduces the British Columbia family benefit bonus, to be delivered alongside the British Columbia family benefit, which will result in a 25 percent increase to both the annual benefit amounts and the income thresholds used to determine eligibility for the British Columbia family benefit. The bonus is a temporary increase for the 2024-25 benefit year only.

TABLE 12 Projected Revenues and Expenditures, British Columbia, Fiscal Year 2024-25

	February 2024
	millions of dollars
Total revenues	81,523
Total expenditures	(89,434)
Surplus/(deficit)	(7,911)
Revenue sources	
Personal income tax	16,638
Corporate income tax	8,236
Sales tax	10,762
Other taxes	13,578
Total tax revenue	49,214
Federal transfers	14,446
Other revenues	17,863
Total revenues	81,523
Expenditures	
Education	19,479
Health	35,944
Debt servicing	4,105
Other expenditures	29,906
Total expenditures	89,434

Notes: Expenditure figures were estimated by function. Revenue included commercial Crown corporation net income.

Source: British Columbia, Ministry of Finance, 2024 Budget, Budget and Fiscal Plan, 2024/25-2026/27, February 22, 2024.

Further, the 2024 budget extends the training tax credit for individuals for one year, to the end of 2025.

3. Sales Tax

No changes were announced.

4. Excise Taxes

The 2024 budget amends the biomethane credit refund so that it is based solely on the sum of the biomethane credits provided by the qualifying retail dealer in a reporting period.

5. Resource-Related Matters

No changes were announced.

6. Real Estate Taxes

The 2024 budget introduces a new tax targeting home-flipping activities. The tax will apply to income realized on or after January 1, 2025 from the sale of properties with a housing unit and properties zoned for residential use that are held for less than two years. The tax rate is 20 percent for properties sold within 365 days of purchase, and declines on a straightline proportionate basis from 20 percent to 0 percent for properties sold within 366 and 730 days of purchase. The tax also applies to income from the assignment of contracts, but not to land or portions of land used for non-residential purposes. Exemptions are available if certain life circumstances motivated the sale of a residential property within two years. Further, individuals who are selling their primary residence within two years of purchase can exclude up to $20,000 of income from the tax. This tax will be levied on top of any federal or provincial income tax applicable on the sale of the property.

The 2024 budget also increases the exemption threshold for the first-time home buyers' exemption, from $500,000 to $835,000, effective April 1, 2024. The phase-out range is $25,000 above the new threshold, which fully eliminates the exemption on the purchase of a property with a fair market value of $860,000 or more. Properties with a fair market value under $500,000 will be completely exempt from property transfer tax.

Further, the 2024 budget increases the exemption threshold for the newly built home exemption, from $750,000 to $1,100,000, effective April 1, 2024. The phase-out range is $50,000 above the new threshold, which fully eliminates the exemption on the purchase of a qualifying newly built home with a fair market value of $1,150,000 or more.

The 2024 budget also fully eliminates the general property transfer tax for new purpose-built rental buildings, effective for transactions that occur between January 1, 2025 and December 31, 2030.

The average residential class school property tax is increased in 2024 by the province's inflation rate in the previous year, in accordance with longstanding policy, in place since 2003.

Non-residential school property tax rates are increased in 2024 by inflation plus tax on new construction, except for the rate for the industrial property classes, in accordance with longstanding policy, in place since 2005 (except for the 2020 year, when relief was delivered through a reduction in school tax rates for commercial properties, owing to the COVID-19 pandemic). The major industry class tax rate and the light industry class tax rate are to be set at the same rate as the business class tax rate, consistent with the policy announced in the 2008 budget.

The single rural area residential property tax rate is increased in 2024 by the province's inflation rate in the previous year, in accordance with longstanding policy. Similarly, rural area non-residential property tax rates increase by inflation plus the tax on new construction.

Finally, the 2024 budget introduces a new approach to property taxation on Nisga'a lands or the treaty lands of a modern treaty First Nation. Effective for

the 2025 taxation year, British Columbia will no longer impose a requirement for property taxation to apply on Nisga'a lands or the treaty lands of a modern treaty First Nation.

7. Pensions

No changes were announced.

8. Other

The 2024 budget increases the employer health tax exemption threshold from $500,000 to $1 million. The notch rate for remuneration between $1 million and $1.5 million is increased from 2.925 percent to 5.850 percent.

Finally, the 2024 budget introduces a number of technical amendments to various tax acts for clarity and certainty.

Alberta (Table 13)

Tax Highlights

- Introduction of new lowest personal income tax bracket, effective 2026, contingent on a balanced budget
- Introduction of new vaping tax and electric vehicle tax; increased tobacco taxes and land title registration levy

Tax Changes

1. Corporate Income Tax

No changes were announced.

2. Personal Income Tax

The 2024 budget introduces a new lowest personal income tax bracket of 8 percent on the first $60,000 of income, with phased-in implementation. In 2026, this new bracket will be 9 percent on the first $60,000 of income, to be reduced to 8 percent in 2027. The 2024 budget indicates that the implementation schedule for the new bracket "is contingent on the province maintaining sufficient fiscal capacity to introduce the tax cut while maintaining a balanced budget."[18]

The 2024 budget also introduces the "Alberta is calling" moving bonus, which provides a one-time $5,000 refundable tax credit to the first 2,000 individuals who apply. To be eligible, applicants must be adult Canadian citizens or permanent residents working in eligible occupations who move to Alberta between May 1 and December 31, 2024 and reside in the province for at least 12 consecutive months.

18 Alberta, Ministry of Treasury Board and Finance, 2024 Budget, Budget Plan, February 29, 2024, at 123.

TABLE 13 Projected Revenues and Expenditures, Alberta, Fiscal Year 2024-25

	February 2024
	millions of dollars
Total revenues	73,537
Total expenditures	(71,170)
Reserve for contingency for disaster/emergency assistance	(2,000)
Surplus/(deficit)	367
Revenue sources	
Personal income tax	15,604
Corporate income tax	7,028
Sales tax	na
Other taxes	6,013
Total tax revenue	28,645
Federal transfers	12,640
Other revenues	32,252
Total revenues	73,537
Expenditures	
Education	16,957
Health	28,732
Debt servicing	3,365
Other expenditures	22,116
Total expenditures	71,170

na = not applicable.

Note: The budget was presented on a fully consolidated basis, which includes school boards, universities and colleges, health entities, and Alberta Innovates corporations.

Source: Alberta, Ministry of Treasury Board and Finance, 2024 Budget, Budget Plan, February 29, 2024.

3. Sales Tax

No changes were announced with respect to a PST. Alberta does not impose a general tax on retail sales.

4. Excise Taxes

On April 1, 2022, Alberta announced that collection of the 13 cents per litre fuel tax would be temporarily paused until June 30, 2022 and that the government would consider reinstating collection in stages.[19] Alberta's fuel tax relief program provides for fuel tax rates to be adjusted quarterly on the basis of the average price of a barrel

19 Alberta, Ministry of Treasury Board and Finance, "Relief at the Pumps Is Here for Albertans," *News Release*, April 1, 2022 (www.alberta.ca/release.cfm?xID=82260FD28353D-F066-B029-704D25E766253169).

of West Texas Intermediate (WTI) oil, with the average price being based on the 20 trading days of WTI oil price data leading up to the 15th day of the month preceding the start of the next quarter. Fuel taxes in Alberta are suspended when average prices are at or above $90.00 per barrel. A partial fuel tax of 4.5 cents per litre will be applied when average prices are between $85.00 and $89.99. A partial fuel tax of 9 cents per litre will be applied when average prices are between $80.00 and $84.99. The full fuel tax of 13 cents per litre will be applied when average prices fall below $80.00. In addition, fuel tax rates cannot increase by more than 9 cents per litre per quarter when oil prices fall. This fuel tax relief program provided full relief from the fuel tax throughout all of 2023, but on December 19, 2023 Alberta announced that collection and remittance of Alberta fuel tax would resume on January 1, 2024, at a rate of 9 cents per litre, owing to the declining price of WTI oil in the final quarter of 2023.[20]

The 2024 budget introduces a new tax on vaping substances, in keeping with Alberta's participation in the federal-provincial coordinated vaping taxation framework. Starting as early as January 1, 2025, vaping substances sold in Alberta will be subject to a provincial tax of $1 per 2 millilitres or grams for the first 10 millilitres or grams of vaping substances, plus $1 per 10 millilitres or grams for amounts over the first 10 millilitres or grams.

The 2024 budget also increases tobacco taxes effective March 1, 2024. The tax on cigarettes will increase from 27.5 cents per cigarette to 30 cents per cigarette, and the tax on smokeless tobacco will increase from 27.5 cents per gram to 35 cents per gram.

Further, the 2024 budget introduces a $200 annual tax on electric vehicles effective January 1, 2025 to address fairness concerns and challenges owing to declining fuel tax revenue.

5. Resource-Related Matters

No changes were announced.

6. Real Estate Taxes

Education property tax rates were previously frozen at 2019 levels owing to the COVID-19 pandemic, but the 2022 budget increased the education property tax requisition by 1.5 percent, to $2.5 billion, straying from the government's previous long-standing policy of increasing the education property tax requisition by the rate of population growth plus inflation. The 2024 budget further increases the education property tax requisition from $2.5 billion to $2.7 billion. However, owing to increased development, the residential and farmland mill rate used to calculate the tax will remain unchanged, at $2.56 per $1,000 of equalized assessment. The non-residential mill rate also remains unchanged, at $3.76 per $1,000 of equalized assessment.

20 Alberta, Ministry of Treasury Board and Finance, "Fuel Tax Relief: Statement from Minister Horner," *News Release*, December 19, 2023 (www.alberta.ca/release.cfm?xID=89505F92A3BB9-DDCB-F786-54DB624505857EDA).

The 2024 budget also increases the land title registration levy, from $2.00 per $5,000 of property value and $1.50 per $5,000 of mortgage value, to $5.00 per $5,000 of value for both property transfers and mortgage registrations. The change was proclaimed in force as of October 20, 2024 through Alberta Order in Council no. 266/2024.

7. Pensions

No changes were announced.

8. Other

No changes were announced.

Saskatchewan (Table 14)

Tax Highlights

- Delayed implementation of increase to the small business corporate tax rate

Tax Changes

1. Corporate Income Tax

As previously announced in 2020, the temporary reduction in the small business corporate income tax rate was to begin phasing out in 2022, and the small business corporate income tax rate was slated to increase from 0 percent to 1 percent on July 1, 2022. On August 23, 2022, Saskatchewan announced a four-point affordability plan[21] that extended the small business tax rate reduction, retroactive to July 1, 2022, and delayed the restoration of the rate to 2 percent until July 1, 2024. Accordingly, on July 1, 2023, the small business corporate tax rate increases from 0 percent to 1 percent. The 2024 budget delays the restoration of the small business corporate income tax rate until July 1, 2025.

The 2024 budget introduces the Saskatchewan critical mineral innovation incentive, which provides transferable royalty credits of 25 percent for eligible project costs incurred on or after April 1, 2024.

The 2024 budget also introduces the multi-lateral well drilling program, which offers drilling incentives for eligible multi-lateral horizontal oil wells drilled on or after April 1, 2024 through March 31, 2028.

Further, the 2024 budget extends the application period and enhances various industry incentive programs. The Saskatchewan petroleum innovation incentive is extended for five years and the funding cap is increased to a maximum of $100 million in royalty credits. The oil and gas processing investment incentive is extended

21 Saskatchewan, Department of Finance, "Saskatchewan Announces Affordability Plan," *News Release*, August 23, 2022 (www.saskatchewan.ca/government/news-and-media/2022/august/23/saskatchewan-announces-affordability-plan).

TABLE 14 Projected Revenues and Expenditures, Saskatchewan, Fiscal Year 2024-25

	March 2024
	millions of dollars
Total revenues	19,862
Total expenditures	(20,135)
Surplus/(deficit)	(273)
Revenue sources	
Personal income tax	3,295
Corporate income tax	1,209
Sales tax	3,196
Other taxes	2,023
Total tax revenue	9,723
Federal transfers	3,780
Other revenues	6,359
Total revenues	19,862
Expenditures	
Education	4,415
Health	7,640
Debt servicing	912
Other expenditures	7,168
Total expenditures	20,135

Note: Debt servicing is for general debt.

Source: Saskatchewan, Ministry of Finance, 2024 Budget, March 20, 2024.

for five years and the funding cap is increased to a maximum of $500 million in royalty credits. The Saskatchewan commercial innovation incentive is extended for one year to allow for a program review. The Saskatchewan technology startup incentive is extended for one year; the eligibility is expanded to include startups in the clean technology and agricultural technology sectors, and the funding cap is doubled to $7 million of non-refundable tax credits annually.

2. Personal Income Tax

No changes were announced.

3. Sales Tax

No changes were announced.

4. Excise Taxes

No changes were announced.

5. Resource-Related Matters

No changes were announced.

6. Real Estate Taxes

No changes were announced.

7. Pensions

No changes were announced.

8. Other

No changes were announced.

Manitoba (Table 15)

Tax Highlights

- Indexation of basic personal amount with phaseout for higher-income individuals
- Reform of the school tax credit and rebate system

Tax Changes

1. Corporate Income Tax

The 2024 budget introduces a rental housing construction tax credit. The credit provides $8,500 for the construction of new market-rate rental units and $13,500 for units classified and maintained as affordable units for a period of at least 10 years. Eligibility for the credit requires construction to commence on or after January 1, 2024. The credit will be fully refundable for non-profit organizations; for all other businesses, $8,500 per unit will be fully refundable. An additional $5,000 non-refundable credit will be available over 10 years for affordable units.

The 2024 budget eliminates the data-processing investment tax credit, effective for the 2025 taxation year.

Further, the 2024 budget extends the cultural industries printing tax credit for one year, to December 31, 2025.

2. Personal Income Tax

The 2024 budget increases the basic personal amount from $15,000 for the 2023 taxation year to $15,780 for the 2024 taxation year. The 2024 budget also proposes to phase out the basic personal amount for taxpayers whose net income ranges from $200,000 to $400,000.

The 2024 budget increases the renters tax credit from a maximum of $525 to a maximum of $575. The seniors top-up is also increased, from a maximum of $300 to a maximum of $328. These changes are effective for the 2025 taxation year.

Further, the 2024 budget doubles the maximum annual eligible expense under the fertility treatment tax credit from $20,000 to $40,000, effective for the 2024 taxation year.

TABLE 15 Projected Revenues and Expenditures, Manitoba, Fiscal Year 2024-25

	April 2024
	millions of dollars
Total revenues	23,437
Total expenditures	(24,133)
Contingency	(100)
Surplus/(deficit)	(796)
Revenue sources	
Personal income tax	4,670
Corporate income tax	918
Sales tax	2,754
Other taxes	1,982
Total tax revenue	10,324
Federal transfers	8,291
Other revenues	4,822
Total revenues	23,437
Expenditures	
Education	5,787
Health	8,220
Debt servicing	2,264
Other expenditures	7,862
Total expenditures	24,133

Notes: The summary budget's government reporting entity included core government, Crown corporations, government business entities, and public sector organizations. The amount for education includes advanced education, education, and early childhood learning. The amount indicated as the health expenditure is for health, seniors, and long-term care. The 2024 budget includes $100 million of revenue contingency.

Source: Manitoba, Department of Finance, 2024 Budget, April 2, 2024.

3. Sales Taxes

The 2024 budget increases the PST registration threshold from $10,000 to $30,000 of taxable sales, effective January 1, 2024, to be consistent with the federal government's GST/HST registration threshold. Further, sales tax commissions are eliminated for any filing period ending after April 2024.

4. Excise Taxes

The 2024 budget introduces a new tax on vaping products, in keeping with Manitoba's participation in the federal-provincial coordinated vaping taxation framework. With an anticipated start date of January 1, 2025, vaping substances sold in Manitoba will be subject to a provincial tax of $1 per 2 millilitres or grams for the first

10 millilitres or grams of vaping substances, plus $1 per 10 millilitres or grams for amounts over the first 10 millilitres or grams.

In the fall of 2023, Manitoba introduced legislation to temporarily reduce the fuel tax rate to zero cents per litre on gasoline, diesel, and marked gasoline, effective from January 1, 2024 to June 30, 2024.[22] The 2024 budget extends this fuel tax cut to September 30, 2024. After the 2024 budget, Manitoba extended the gas tax cut to December 31, 2024,[23] followed by a permanent reduction in the fuel tax rate from 22.5 cents per litre to 12.5 cents per litre, effective January 1, 2025.[24]

5. Resource-Related Matters

No changes were announced.

6. Real Estate Taxes

The 2024 budget introduces reform to the school tax credit and rebate system. Effective for the 2025 taxation year, the school tax rebate and education property tax credit (and seniors top-up) will be replaced with a homeowners' affordability tax credit of up to $1,500 on principal residences. The school tax rebate for farm properties will remain unchanged, while the school tax rebate for all other commercial properties will be eliminated.

7. Pensions

No changes were announced.

8. Other

The 2024 budget introduces various administrative tax measures, generally to provide technical clarifications of existing tax legislation. A noteworthy change among the various administrative tax measures introduced in the 2024 budget is the elimination of the tax clearance certificate fee and advance ruling fee, effective May 1, 2024.

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22 Manitoba, Department of Finance, "Manitoba Government Introduces Legislation To Make Lives More Affordable for Manitobans by Lowering Fuel Taxes," *News Release*, November 23, 2023 (https://news.gov.mb.ca/news/index.html?item=60899&posted=2023-11-23).

23 Manitoba, Department of Finance, "Manitoba Government To Extend Gas Tax Holiday to December 31," *News Release*, September 25, 2024 (https://news.gov.mb.ca/news/index.html?item=65257&posted=2024-09-25).

24 Manitoba, Department of Finance, "Manitoba Government Introduces Permanent Cut to Provincial Fuel Tax," *News Release*, December 23, 2024 (https://news.gov.mb.ca/news/index.html?item=66897).

Ontario (Table 16)

Tax Highlights

- No changes to personal or corporate income tax rates

Tax Changes

1. Corporate Income Tax

The 2024 budget simplifies the Ontario computer animation and special effects tax credit by removing the tethering of the credit to either the Ontario film and television tax credit or the Ontario production services tax credit. The tethering of the credit is replaced with a new criterion that requires qualifying corporations to incur a minimum of $25,000 in Ontario labour expenditures for each film or television production for which the tax credit is claimed. Certain types of productions, including instructional videos, music videos, and gaming videos, are excluded from eligibility. These new rules are in effect for productions that commence on or after March 26, 2024.

2. Personal Income Tax

No changes were announced.

3. Sales Tax

No changes were announced.

4. Excise Taxes

The 2024 budget extends the temporary reduction in the gasoline tax and fuel tax rates that came into effect on July 1, 2022 for an additional six months, to December 31, 2024.

The 2024 budget also proposes to eliminate the wine basic tax that applies to sales of Ontario wine and wine coolers in on-site winery retail stores, effective April 1, 2024. Further, the 2024 budget indicates that Ontario will conduct a targeted review of taxes and fees on beer, wine, and alcoholic beverages in order to promote a more competitive marketplace for Ontario-based producers and consumers.

5. Resource-Related Matters

No changes were announced.

6. Real Estate Taxes

No changes were announced.

7. Pensions

No changes were announced.

TABLE 16 Projected Revenues and Expenditures, Ontario, Fiscal Year 2024-25

	March 2024
	millions of dollars
Total revenues	205,690
Total expenditures	(214,496)
Contingency	(1,000)
Surplus/(deficit)	(9,806)
Revenue sources	
Personal income tax	51,936
Corporate income tax	24,915
Sales tax	38,832
Other taxes	29,004
Total tax revenue	144,687
Federal transfers	36,252
Other revenues	24,751
Total revenues	205,690
Expenditures	
Education	51,495
Health	84,961
Debt servicing	13,913
Other expenditures	64,127
Total expenditures	214,496

Notes: The figures included amounts for government business enterprises. Expenditures were shown by ministry. Education expenditures include expenditures from the Ministry of Colleges and Universities and the Ministry of Education. Health expenditures include expenditures from the Ministry of Health and the Ministry of Long-Term Care, which were reported separately for the first time in fiscal year 2020-21. Debt servicing is net of interest capitalized during construction of tangible capital assets of $865 million for fiscal year 2024-25.

Source: Ontario, Ministry of Finance, 2024 Budget, March 26, 2024.

8. Other

No changes were announced.

Quebec (Table 17)

Tax Highlights

- No changes to personal or corporate income tax rates
- Changes to various corporate tax credits

Tax Changes

1. Corporate Income Tax

The 2024 budget enhances the refundable tax credit for Quebec film or television productions by increasing the limit for the credit from 50 percent to 65 percent of

TABLE 17 Projected Revenues and Expenditures, Quebec, Fiscal Year 2024-25

	March 2024
	millions of dollars
Total revenues	150,301
Total expenditures	(157,577)
Contingency reserve	(1,500)
Surplus/(deficit)	(8,776)
Revenue sources	
Personal income tax	44,952
Corporate income tax	12,116
Sales tax	27,991
Other taxes	9,980
Total tax revenue	95,039
Federal transfers	29,397
Other revenues	25,865
Total revenues	150,301
Expenditures	
Education	33,424
Health	61,909
Debt servicing	9,762
Other expenditures	52,482
Total expenditures	157,577

Notes: The figures were presented on a consolidated basis, showing general fund plus consolidated entities. The figures shown for expenditures were by department, except for debt servicing. The surplus/(deficit) presented excludes deposits of dedicated revenues in the Generations Fund, a fund dedicated exclusively to repaying Quebec's debt.

Source: Québec, Finances Québec, 2024-2025 Budget, Budget Plan, March 12, 2024.

production costs incurred and directly attributable to the film production, applicable for any Quebec film production for which an application is filed after March 12, 2024.

The 2024 budget increases the refundable tax credit for film production services by increasing the rate of the basic tax credit from 20 percent to 25 percent of the amount of its eligible production costs and amending the legislation to limit eligibility for the credit to 65 percent of the portion of costs of a contract with a service provider for computer-aided special effects and animation. These changes are effective for a qualified production for which an application is filed after March 12, 2024 if work on the production was not sufficiently advanced as of that date, or May 31, 2024 in all other cases.

The 2024 budget introduces changes to the tax credit for the development of e-business by introducing an exclusion threshold per eligible employee and removing the $83,333 limit on the definition of qualified wages for each eligible employee, effective for taxation years beginning after December 31, 2024. Currently, for the 2024 calendar year, the tax credit for the development of e-business provides a 24 percent

refundable tax credit and a 6 percent non-refundable tax credit. Implementation will be phased in over four years; the non-refundable portion of the tax credit will increase by 1 percent each year until it reaches 10 percent, and the refundable portion of the tax credit will be correspondingly reduced until it reaches 20 percent, starting on January 1, 2025, with full implementation achieved by January 1, 2028.

The 2024 budget introduces changes to the tax credit for the production of multimedia titles by introducing an exclusion threshold per eligible employee and removing the $100,000 limit on the definition of qualified labour expenditure for each eligible employee, effective for taxation years beginning after December 31, 2024. Currently, for the 2024 calendar year, the tax credit provides for a refundable tax credit ranging from 26.25 percent to 37.50 percent, depending on the category of multimedia title. The 2024 budget introduces a non-refundable portion of the tax credit valued at 10 percent with a corresponding reduction in the refundable portion of the tax credit. Implementation will be phased in over four years; the non-refundable portion of the tax credit will increase by 2.5 percent each year until it reaches 10 percent, with a corresponding reduction in the refundable portion of the tax credit, starting on January 1, 2025, with full implementation achieved by January 1, 2028.

The 2024 budget also provides for a modification to the definition of government assistance for the purposes of calculating the tax credit for the production of biofuel and the tax credit for the production of pyrolysis oil in Quebec for taxation years beginning after December 31, 2027.

Further, the 2024 budget eliminates the tax credit to foster the retention of experienced workers for amounts paid after March 12, 2024.

2. Personal Income Tax

The 2024 budget introduces changes to two components of the refundable tax credit granting an allowance to families. First, the 2024 budget changes certain assessment parameters for the supplement for handicapped children for applications filed after June 30, 2024. Second, the 2024 budget adds a new situation in which a child will qualify for the first level of the supplement for handicapped children requiring exception care for applications filed after June 30, 2024.

3. Sales Tax

The 2024 budget amends the QST rules to eliminate the application of the estimated value rule for used road vehicles brought into Quebec following their transfer, outside Quebec, between related individuals.

4. Excise Taxes

The 2024 budget introduces a two-phase increase in tobacco taxes. The tax on cigarettes increases from 18.9 cents per cigarette to 19.9 cents per cigarette on March 13, 2024, followed by an increase to 20.9 cents per cigarette on January 6, 2025. The tax on loose tobacco or leaf tobacco increases from 18.9 cents per gram to 19.9 cents per gram on March 13, 2024, followed by an increase to 20.9 cents per

gram on January 6, 2025. The tax on any tobacco other than cigarettes, loose tobacco, leaf tobacco, and cigars increases from 29.07 cents per gram to 30.61 cents per gram on March 13, 2024, followed by an increase to 32.15 cents per gram on January 6, 2025. The tobacco tax on cigars remains unchanged.

5. Resource-Related Matters

No changes were announced.

6. Real Estate Taxes

No changes were announced.

7. Pensions

The 2024 budget eliminates the retirement pension reduction as of January 1, 2025 for seniors with disabilities reaching the age of 65. The 2024 budget also retroactively amends the legislation to protect the pension benefits for recipients of a disability pension between the ages of 60 and 64 to ensure that their benefits are at least as high as what they were prior to the payment of their pension, effective January 1, 2024.

8. Other

No changes were announced.

New Brunswick (Table 18)

Tax Highlights

- No changes to corporate or personal income tax rates

Tax Changes

1. Corporate Income Tax

No changes were announced.

2. Personal Income Tax

The 2024 budget increases the base amount of the low-income seniors' benefit from $400 to $600, beginning with the 2025 benefit year.

The 2024 budget also introduces a new non-refundable personal income tax credit for eligible volunteer firefighters and search and rescue volunteers, effective for the 2024 taxation year. No further details were provided in the 2024 budget.

3. Sales Tax

No changes were announced.

TABLE 18 Projected Revenues and Expenditures, New Brunswick, Fiscal Year 2024-25

	March 2024
	millions of dollars
Total revenues	13,296
Total expenditures	(13,255)
Contingency reserve	nil
Surplus/(deficit)	41
Revenue sources	
Personal income tax	2,440
Corporate income tax	690
Sales tax	2,381
Other taxes	988
Total tax revenue	6,499
Federal transfers	4,896
Other revenues	1,901
Total revenues	13,296
Expenditures	
Education	2,666
Health	3,843
Debt servicing	608
Other expenditures	6,138
Total expenditures	13,255

Notes: Figures were shown on a main estimates basis. Expenditure figures were shown by department. Education and health expenditures exclude special-purpose account and special operating agencies expenses. Education includes both education and early childhood development and post-secondary education, training, and labour.

Source: New Brunswick, Department of Finance and Treasury Board, 2024-25 Budget, March 19, 2024.

4. Excise Taxes

The 2024 budget introduces a new tax on vaping substances, in keeping with New Brunswick's participation in the federal-provincial coordinated vaping taxation framework. With an intended implementation date of January 1, 2025, vaping substances sold in New Brunswick will be subject to a provincial tax of $1 per 2 millilitres or grams for the first 10 millilitres or grams of vaping substances, plus $1 per 10 millilitres or grams for amounts over the first 10 millilitres or grams.

5. Resource-Related Matters

No changes were announced.

6. Real Estate Taxes

No changes were announced.

7. Pensions

No changes were announced.

8. Other

No changes were announced.

Nova Scotia (Table 19)

Tax Highlights

- Introduction of indexation to the provincial personal income tax system starting in 2025

Tax Changes

1. Corporate Income Tax

No changes were announced.

2. Personal Income Tax

The 2024 budget introduces indexation to the personal income tax system for the 2025 and subsequent taxation years. Taxable income brackets and certain non-refundable tax credits will be indexed as of January 1, 2025.

3. Sales Tax

No changes were announced.

4. Excise Taxes

No changes were announced.

5. Resource-Related Matters

No changes were announced.

6. Real Estate Taxes

No changes were announced.

7. Pensions

No changes were announced.

8. Other

No changes were announced.

TABLE 19 Projected Revenues and Expenditures, Nova Scotia, Fiscal Year 2024-25

	February 2024
	millions of dollars
Total revenues	15,844
Total expenditures	(16,519)
Reserve and consolidating adjustments	208
Surplus/(deficit)	(467)
Revenue sources	
Personal income tax	4,174
Corporate income tax	749
Sales tax	2,756
Other taxes	667
Total tax revenue	8,346
Federal transfers	5,313
Other revenues	2,185
Total revenues	15,844
Expenditures	
Education	2,725
Health	6,900
Debt servicing	823
Other expenditures	6,071
Total expenditures	16,519

Notes: Revenue-source figures were for general revenue fund only, with adjustments for consolidation. Expenditure figures were shown by department, general revenue fund. Education expenditures presented are for "education and early childhood development" and "advanced education" departmental expenses. Health expenditures presented are for "health and wellness" and "seniors and long-term care" departmental expenses.

Source: Nova Scotia, Department of Finance and Treasury Board, 2024 Budget, Budget Plan, February 29, 2024.

Prince Edward Island (Table 20)

Tax Highlights

- Continued reform of the personal income tax system effective for 2025

Tax Changes

1. Corporate Income Tax

No changes were announced.

2. Personal Income Tax

The 2023 budget introduced personal tax reform measures by replacing the previous three-bracket system with a five-bracket system for the 2024 taxation year. The 2024

TABLE 20 Projected Revenues and Expenditures, Prince Edward Island, Fiscal Year 2024-25

	February 2024
	millions of dollars
Total revenues	3,147
Total expenditures	(3,232)
Supplementary appropriation	nil
Surplus/(deficit)	(85)
Revenue sources	
Personal income tax	594
Corporate income tax	164
Sales tax	514
Other taxes	285
Total tax revenue	1,557
Federal transfers	1,251
Other revenues	339
Total revenues	3,147
Expenditures	
Education	607
Health	1,126
Debt servicing	168
Other expenditures	1,331
Total expenditures	3,232

Notes: Revenue and expenditure figures were consolidated. Expenditure figures were shown by department. Education expenditures include expenditures for "education and early years" and "workforce, advanced learning, and population" programs.

Source: Prince Edward Island, Department of Finance, 2024 Budget, Budget Plan, February 29, 2024.

budget continues to reform the personal tax system by raising the thresholds of personal tax brackets and lowering the tax rates for the first four brackets for the 2025 taxation year.

The 2024 budget also increases the basic personal tax credit amount from $13,500 for the 2024 taxation year to $14,250 for the 2025 taxation year.

Further, the 2024 budget introduces a PEI child benefit starting in the 2025 taxation year. This benefit supports families by providing a monthly benefit of $30 per child under the age of 18 if family net income is less than $45,000 in the previous year, with the monthly benefit reduced to $20 per child under the age of 18 if family net income is between $45,000 and $80,000 in the previous year.

3. Sales Tax

No changes were announced.

4. Excise Taxes

No changes were announced.

5. Resource-Related Matters

No changes were announced.

6. Real Estate Taxes

No changes were announced.

7. Pensions

No changes were announced.

8. Other

No changes were announced.

Newfoundland and Labrador (Table 21)

Tax Highlights

- Reduction of small business corporate tax rate

Tax Changes

1. Corporate Income Tax

The 2024 budget reduces the small business corporate tax rate from 3 percent to 2.5 percent, effective January 1, 2024.

2. Personal Income Tax

No changes were announced.

3. Sales Tax

No changes were announced.

4. Excise Taxes

No changes were announced.

5. Resource-Related Matters

No changes were announced.

6. Real Estate Taxes

No changes were announced.

7. Pensions

No changes were announced.

TABLE 21 Projected Revenues and Expenditures, Newfoundland and Labrador, Fiscal Year 2024-25

	March 2024
	millions of dollars
Total revenues	10,296
Total expenditures	(10,448)
Contingency reserve	nil
Surplus/(deficit)	(152)
Revenue sources	
Personal income tax	1,816
Corporate income tax	506
Sales tax	1,486
Other taxes	597
Total tax revenue	4,405
Federal transfers	2,412
Other revenues	3,479
Total revenues	10,296
Expenditures	
Education	1,720
Health	4,129
Debt servicing	1,153
Other expenditures	3,446
Total expenditures	10,448

Notes: The figure shown for total revenues includes net income of government business enterprises and partnerships. Expenditures were reported by department, except for debt-related expenses. Health expenditure covers "health and community services." Expenditures were a combination of current and capital account expenditures by department in the government reporting entity on a consolidated basis.

Source: Newfoundland and Labrador, Department of Finance, 2024 Budget, Budget Plan, March 21, 2024.

8. Other

No changes were announced.

YUKON (TABLE 22)

Tax Highlights

- No changes to corporate or personal income tax rates

Tax Changes

1. Corporate Income Tax

No changes were announced.

TABLE 22 Projected Revenues and Expenditures, Yukon, Fiscal Year 2024-25

	March 2024
	millions of dollars
Total revenues	2,046
Total expenditures	(1,877)
Contingency reserve	(50)
Surplus/(deficit)	119
Revenue sources	
Personal income tax	107
Corporate income tax	41
Sales tax	na
Other taxes	42
Total tax revenue	190
Federal transfers	1,429
Other revenues	427
Total revenues	2,046
Expenditures	
Education	282
Health	604
Debt servicing	14
Other expenditures	977
Total expenditures	1,877

Notes: Amounts presented are based on non-consolidated reporting; the consolidated surplus was reported as $154 million. Consolidated reporting includes territorial corporations. The contingency reported represents a $50 million reserve for "anticipated expenses." The health figure includes an amount for social services. The debt-servicing figure shown represents expenditures on loan programs.

The Yukon government signed a devolution agreement with the federal government in 2003 to assume land and resource management responsibilities. Amendments to the resource revenue-sharing arrangement in 2012 ensured that more resource revenue generated in Yukon would be available for use in the territory.

Source: Yukon, Department of Finance, 2024 Budget, Budget Plan, March 7, 2024.

2. Personal Income Tax

No changes were announced.

3. Sales Tax

No changes were announced.

4. Excise Taxes

Tobacco taxes, which are indexed to inflation based on changes in the Whitehorse consumer price index, increase from 32 cents per cigarette to 35 cents per cigarette, effective January 1, 2024.

5. Resource-Related Matters

No changes were announced.

6. Real Estate Taxes

No changes were announced.

7. Pensions

No changes were announced.

8. Other

No changes were announced.

Northwest Territories (Table 23)

Tax Highlights

- No changes to corporate or personal income tax rates

Tax Changes

1. Corporate Income Tax

No changes were announced.

2. Personal Income Tax

No changes were announced.

3. Sales Tax

No changes were announced.

4. Excise Taxes

The 2024 budget increases the carbon tax rate from $65 per tonne of greenhouse gas emissions to $80 per tonne, effective April 1, 2024. The carbon tax rate is to increase annually by $15 per tonne of emissions until it reaches $170 per tonne on April 1, 2030.

Further, the 2024 budget highlights a previously announced vaping tax, introduced in keeping with the territory's participation in the federal-provincial coordinated vaping taxation framework, effective July 1, 2024.

5. Resource-Related Matters

No changes were announced.

TABLE 23 Projected Revenues and Expenditures, Northwest Territories, Fiscal Year 2024-25

	May 2024
	millions of dollars
Total revenues	2,633
Total expenditures	(2,230)
Infrastructure contribution, deferred maintenance, and other reserves	(109)
Surplus/(deficit)	294
Revenue sources	
Personal income tax	128
Corporate income tax	56
Sales tax	na
Other taxes	199
Total tax revenue	383
Federal transfers	2,118
Other revenues	132
Total revenues	2,633
Expenditures	
Education	375
Health	644
Debt servicing	27
Other expenditures	1,184
Total expenditures	2,230

Notes: Figures presented are the health and education expenditures by department; the education figure includes education, culture, and employment, and the health figure includes social services. The stated surplus was on a non-consolidated basis. The debt-servicing amount is assumed to be expenditures classified as "interest" in the summary of expenditures.

On April 1, 2014, the Northwest Territories took responsibility for the management of its land, water, and non-renewable resources. The Northwest Territories started to receive resource revenues under devolution in 2014-15; half is offset against federal territorial formula financing grants, up to 25 percent of the balance will be shared with Indigenous governments, and 25 percent of the balance will be saved in the Heritage Fund. The Northwest Territories and the federal government signed a devolution agreement on March 11, 2013.

Source: Northwest Territories, Department of Finance, 2024 Budget, Budget Plan, May 24, 2024.

6. Real Estate Taxes

The 2024 budget indicates that property tax mill rates will be indexed to inflation, in keeping with past practice.

7. Pensions

No changes were announced.

8. Other

No changes were announced.

Nunavut (Table 24)

Tax Highlights

- No changes to corporate or personal income tax rates

Tax Changes

1. Corporate Income Tax

No changes were announced.

2. Personal Income Tax

No changes were announced.

3. Sales Tax

No changes were announced.

4. Excise Taxes

No changes were announced.

5. Resource-Related Matters

No changes were announced.

6. Real Estate Taxes

No changes were announced.

7. Pensions

No changes were announced.

8. Other

No changes were announced.

TABLE 24 Projected Revenues and Expenditures, Nunavut, Fiscal Year 2024-25

	February 2024
	millions of dollars
Total revenues	2,974
Total expenditures	(2,895)
Supplementary requirements	(100)
Surplus/(deficit)	(21)
Revenue sources	
Personal income tax	40
Corporate income tax	21
Sales tax	na
Other taxes	110
Total tax revenue	171
Federal transfers	2,665
Other revenues	138
Total revenues	2,974
Expenditures	
Education	311
Health	542
Debt servicing	na
Other expenditures	2,042
Total expenditures	2,895

Notes: Main estimates were prepared on a non-consolidated basis. Surplus/(deficit) was shown on a main estimates basis and not the public accounts basis, which funds revenues and expenditures. Expenditure figures appeared to be shown by department and include both operations and maintenance expenditures and capital expenditures. The budget does not present debt-servicing costs separately in the main estimates, and an amount that represents those costs cannot be reasonably determined.

Nunavut, Nunavut Tunngavik Incorporated, and the federal government signed a devolution agreement on January 18, 2024, with an effective transfer date of April 1, 2027. The implementation of the devolution agreement will have an impact on Nunavut's budget in the coming years as the territory works with the federal government to assume responsibility for Nunavut's public lands, natural resources, and rights with respect to water.

Source: Nunavut, Department of Finance, 2024 Budget, Budget Plan, February 26, 2024.

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International Tax Planning

Co-Editors: Ken Buttenham and Ian Bradley*

THE FALLOUT FROM ALTA ENERGY LUXEMBOURG—THE APPLICATION OF GAAR TO TAX TREATIES

*Brian J. Arnold***

This article examines three factors that were influential in the Supreme Court's 2021 decision in *Canada v. Alta Energy Luxembourg SARL* with respect to the potential application of the general anti-avoidance rule to the Canada-Luxembourg tax treaty: (1) the presumption that the contracting states know about each other's domestic income tax system, (2) the dual nature of tax treaties as statutes and treaties, and (3) the theory of economic allegiance. It argues that, irrespective of whether one considers the court's decision to be correct or incorrect, the court did not understand or apply these factors properly.

KEYWORDS: TAX TREATIES ■ GAAR ■ SUPREME COURT OF CANADA ■ INTERPRETATION ■ INCOME TAX CONVENTIONS INTERPRETATION ACT ■ THEORY OF ECONOMIC ALLEGIANCE

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Personal Tax Planning

Co-Editors: Chris Watt Bickley,* Sonia Gandhi,** Dino Infanti,*** and Bessy Triantafyllos****

TAX CONSIDERATIONS WHEN DEPARTING CANADA

*Jeff Paisley and Joel Emond*****

This article explores the tax implications for Canadian residents who are considering emigrating from Canada. It provides a refresher on key tax concepts relevant to departure from Canada and discusses factors to consider in the selection of a new jurisdiction of residence. The article also examines whether to implement pre-departure transactions, the election to defer payment of departure tax, considerations when posting security with the minister of national revenue, and potential pitfalls and planning opportunities for four client profiles: owner-managers, corporate investors, Canadian real estate investors, and high net worth individuals.

KEYWORDS: EMIGRATION ■ DEPARTURE TAXES ■ NON-RESIDENT ■ SECURITY ■ RESIDENCE

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Planification fiscale personnelle

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Considérations fiscales au départ du Canada

*Jeff Paisley et Joel Emond*****

Cet article examine les conséquences fiscales pour les résidents canadiens qui envisagent d'émigrer du Canada. Il rappelle les principaux concepts fiscaux relatifs au départ du Canada et examine les facteurs à prendre en considération dans le choix d'un nouveau pays de résidence. L'article se penche également sur la pertinence d'effectuer des opérations avant le départ, le choix de différer le paiement de l'impôt de départ, les considérations relatives à la fourniture d'une garantie au ministre du Revenu national, ainsi que les pièges potentiels et les possibilités de planification pour quatre profils de clients : les propriétaires exploitants, les investisseurs dans une société, les investisseurs dans l'immobilier canadien et les particuliers fortunés.

MOTS CLÉS : ÉMIGRATION ■ IMPÔT DE DÉPART ■ NON-RÉSIDENT ■ GARANTIE ■ RÉSIDENCE

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Corporate Tax Planning

Co-Editors: Miguel Boissonneault,* Mark Brender,**
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NAVIGATING INTERGENERATIONAL BUSINESS TRANSFERS—SUBSECTIONS 84.1(2.31) AND (2.32)

*Sabrina Jackson-Nazareth and Matthew Wilkins*****

This article explores the complexities of intergenerational business transfers (IBTs) under Canadian income tax law, with particular focus on subsections 84.1(2.31) and (2.32) of the Income Tax Act. It examines the challenges posed by section 84.1, which historically created significant tax disadvantages for family-owned business transfers, and considers legislative changes introduced by Bill C-208 and subsequent amendments in Bill C-59 to provide exceptions for genuine IBTs. The article delves into the mechanics of section 84.1, the criteria for qualifying as an immediate or a gradual intergenerational business transfer, and the conditions that must be met before, during, and after the share disposition. It also addresses practical challenges and planning considerations with regard to valuation, documentation, and family dynamics in navigating these provisions.

KEYWORDS: FAMILY ■ TRANSFER ■ SHARES ■ CHILDREN ■ RULES ■ BUSINESS TAXES

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Current Tax Reading

Co-Editors: David G. Duff, Jinyan Li, Alan Macnaughton, and Michael Veall*

Jason DeBacker, Bradley Heim, Anh Tran, and Alexander Yuskavage, "Seeking Professional Help: How Paid Preparers Decrease Tax Compliance" (2024) 77:2 *National Tax Journal* 229-61

Research from the late 1980s and early 1990s regarding the effects on tax compliance of using a tax practitioner to prepare a personal tax return (as opposed to self-preparation) generally found a two-sided effect: compliance increased for items that have clear and unambiguous reporting requirements but decreased for items with more ambiguity. This article revisits the issue with a much larger dataset, also using US data. The key result is that the use of a professional tax preparer increases the underreporting of taxable income on personal income tax returns by an average of US$3,900 per return.[1] All amounts in the study are inflation-adjusted to 2012 dollars, so this amount would be about US$5,300 in today's dollars (Cdn$7,500).[2] The effects on total revenue are outside the scope of the research, although the article notes that this underreporting is a concern: "With about 60 percent of taxpayers using preparation services, this estimate implies a federal revenue loss of tens of billions of dollars each year due to tax preparers."[3]

The measure of non-compliance in the dataset is the audit adjustment recommended by the IRS agent: "true income" is reported income plus the recommended IRS adjustment (positive or negative). This measure does not account for changes resulting from taxpayers' appeals within the IRS or in court.

The primary data source for the research is the set of randomized audits conducted by the IRS National Research Program (NRP). It includes data collected through this program since 2006, when these audits began to be conducted on an annual basis: waves (samples) from 2006 to 2014 form the dataset. This results in

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1 At 229.

2 All subsequent references to dollar amounts in this review are to 2012 US dollars.

3 At 258.

a sample of just over 100,000 returns, which is a very large sample size compared with samples in past research.

One big advantage of using this dataset rather than all returns audited by the IRS is that NRP audits can range over the whole return. Normal audits look only at selected items, and thus the audit adjustment would be incomplete. Also, the NRP audits are random rather than based on their revenue-generating potential, and thus they are representative of the population of returns (after applying sample weights to correct for stratification criteria, such as the oversampling of high-income returns).

The major methodological issue facing the research is that decisions to use a tax preparer are endogenous and may be related to the taxpayer's demand for non-compliance. In particular, if individuals hiring tax preparers are more non-compliant than self-prepared filers—and would have been equally non-compliant had they prepared their own returns—then the statistical estimate of the effect of the use of a tax preparer would be biased upward. In other words, the impact of tax preparers would be overstated, and the true understatement of income would be lower than estimated.[4]

The authors correct for this endogeneity problem by using an instrumental-variables technique. In a first-stage regression, they estimate the likelihood of a filer using a paid preparer (the dependent variable) as a function of variables that include, most notably, those related to peer influence—that is, the proportion of taxpayers in the filer's zip code and workplace who use a tax preparer. In the second-stage regression, the dependent variable is the filer's audit adjustment, while the independent variables include the likelihood measure from the first regression, an indicator variable regarding whether the taxpayer used a paid preparer, and a series of control variables. The filer's decision to hire a tax preparer in one year is assumed to be independent of their decision in any other year.

As noted above, the main finding of the analysis is that audit adjustments to taxable income are estimated to be about $3,900 higher when a preparer is used to file the tax return than when the return is self-prepared. In terms of tax liability, the average adjustment is $596 for self-prepared returns, but $518 higher when a tax preparer is used—an increase of 87 percent.[5]

Further instrumental-variables statistical analysis investigates the impact of using tax preparers on various items reported on tax returns. The only income source that appears to be affected is sole proprietorship income (form 1040 schedule C), where audit adjustments are about $9,900 higher than for self-prepared returns.[6] A more

4 The endogeneity bias could also go in the other direction. Statistical estimates prepared by using ordinary least squares (rather than using the instrumental-variables technique) indicate that the effect of a preparer on decreasing taxable income would be $884 instead of $3,900 (at 258). The authors interpret this finding as evidence that taxpayers who choose to use paid preparers appear to be those who, if they prepared their own returns, would be unwilling or unable to do so in an aggressive manner.

5 At 242.

6 At 250, table 6.

detailed analysis of schedule C shows that the most significant adjustments are related to expenses, which are overstated by about $6,100 on professionally prepared returns.[7] There is also some evidence that adjustments related to the earned income tax credit are greater for professionally prepared returns. However, the difference ($171) is statistically significant only at a low level (10 percent).[8] Both of these items (schedule C and the earned income tax credit) involve minimal information-return reporting, which makes non-compliance in these areas difficult for the IRS to detect.

Elsewhere in the article, the authors provide estimates of non-compliance for returns prepared under the volunteer income tax assistance (VITA) program. This program's preparers are not subject to the economic incentives of professional preparers. The estimates show that the audit adjustments of VITA-eligible (that is, low-income) filers are much smaller than those of filers who use a paid preparer, and may not be different from those who self-prepare their returns.

The article also investigates how non-compliance varies by gender. While the average audit adjustment for a professionally prepared return is $3,900 overall, the average for single men is about $5,500, as opposed to about $2,500 for single women.[9] This analysis focused on single individuals because married couples may use a joint return for both spouses.

Non-compliance also varies by income. Audit adjustments account for about 4 percent of taxable income for those with adjusted gross income between $15,000 and $35,000, but they account for about 15 percent of taxable income for those with adjusted gross income greater than $150,000.[10]

Finally, non-compliance varies by the type of tax preparer. The level of non-compliance is highest for lawyers, but this estimate is statistically imprecise because lawyers prepare only 0.27 percent of all returns. More precise estimates are available for non-lawyers: enrolled agents and "other" preparers are next to lawyers in their levels of non-compliance, while CPAs and national tax-preparation firms have the lowest levels of non-compliance.[11]

If ordinary least squares (OLS) statistical estimates are used in the analysis instead of the instrumental-variables approach, the estimated effect of using a preparer on decreasing taxable income is $884, rather than $3,900. Thus, taxpayers who use paid preparers appear to be those who, if they prepared their own returns, would be unwilling or unable to be as aggressive as professionals.

The article notes various limitations of the study. One limitation is that some taxpayers may be using tax preparers who do not sign off on the return ("ghost preparers"). In other words, the return appears to be self-prepared but is not. This

7 At 249.

8 At 245 and table 4, at 246.

9 At 251, table 7.

10 At 252.

11 At 254.

practice appears to be most common among low-income filers and the elderly. The direction of the bias that this introduces is unknown.

Another issue is that for the instrumental-variables technique (discussed above) to be effective, two conditions must be met: the variables must be relevant to the taxpayer's decision to use a preparer, and the exclusion restriction must be satisfied. Relevance is not a significant issue. The peer-effects argument described above seems reasonable: taxpayers may be more likely to use a preparer if their neighbours and co-workers do so, and the fact that there is considerable variation in both variables is quite helpful statistically. It is more questionable whether the exclusion restriction is satisfied. For this restriction to hold, these peer effects must influence only the decision to use a tax preparer, without directly affecting compliance behaviour. There are two situations where this condition may not be met, which could result in the upward bias (noted above) in the estimated effect of using a tax preparer on non-compliance. First, areas with a higher share of professionally prepared returns tend to have more preparers who engage in higher rates of non-compliance (perhaps to gain a competitive edge). Second, social networks facilitate the sharing of information not only about methods of tax preparation but also about tax-avoidance strategies. The authors are commendably frank in discussing the problem, and they make efforts to minimize it, but the problem cannot be eliminated with their dataset.

One issue to which the study devotes little attention is the measurement of tax non-compliance based on audit adjustments. The problem is that this measure does not account for subsequent changes in tax liability resulting from taxpayers' responses to these adjustments. Such changes may occur through discussions with the taxpayer (or formal appeals) regarding the applicable law and the specific facts of the case. It would have been helpful if the study had at least indicated how often audit adjustments are revised because of this response—even if the data came from normal operational audits rather than the IRS NRP.

AM

Michael Baker, Derek Messacar, and Mark Stabile, "Effects of Child Tax Benefits on Poverty and Labor Supply: Evidence from the Canada Child Benefit and Universal Child Care Benefit" (2023) 41:4 *Journal of Labor Economics* 1129-82

This article examines two reforms intended to generally increase government financial assistance for the costs of raising children. The first reform is the 2015 expansion of the universal child care benefit (UCCB), a taxable payment. The expansion increased benefits payable for children aged 0 to 5 years and introduced a new benefit for children aged 6 to 17. The second reform is the 2016 replacement of three programs (the UCCB and two others) with a single tax-free benefit, the Canada child benefit (CCB). This program, with some subsequent enhancements, continues to the present day. The 2016 reform provided the largest increase in benefits to families with incomes up to approximately $50,000, but families with household incomes as high as $130,000 also received some increase.

One principal data source is Statistics Canada's Longitudinal Administrative Database (LAD), which is essentially a 20 percent random sample of taxfilers, organized into family groups. The other data source is Statistics Canada's Labour Force Survey, which measures participation in the labour force and usual hours worked. The years studied are 2011 to 2019. The authors link data on each individual across the two datasets, using the individual's social insurance number.

The article uses an event-study, difference-in-differences research design. Families of single and married mothers are examined separately. The primary analysis is of women aged 25 to 54. Women who had at least one child aged 0 to 17 in the calendar year (the treated group) are compared with women who did not have children in this age group in the calendar year (the control group).

One policy outcome examined in the article is the impact on child poverty. This is important, because numerous studies have shown that poverty in childhood is associated with numerous adverse socioeconomic outcomes in adulthood. Poverty is measured by the low-income measure (LIM), which is defined as one-half of the median after-tax income of all households in Canada, adjusted for household size. Individuals whose income is below the LIM are considered to be in poverty. Although the official poverty measure in Canada is the market-based measure (MBM), which is based on the cost of specified qualities and quantities of standard household expenses, the MBM is not as easily comparable across countries and is not available in the LAD.

Before the 2016 introduction of the CCB, the percentage of households living in LIM-measured poverty was about 49 percent for households with single mothers and 11 percent for households with married mothers. Two years after the change, the percentage of households in poverty declined by about 5 percentage points (to about 44 percent) for households with single mothers and 2 percentage points (to about 9 percent) for households with married mothers.[12] These percentages were higher for households of mothers who had less than a post-secondary education. The UCCB change had a more modest effect; for example, it reduced by about 2 percentage points the proportion of households living in poverty in which the mother had less than a post-secondary education.

Of course, the measures above document only some of the effects of these policy changes on after-tax incomes. One effect was to raise the after-tax incomes of households that remained in poverty after the changes; another was to raise the after-tax incomes of households above the poverty line. The article documents these changes as well.

Any program that raises households' after-tax incomes must consider the issue of potential decreases in labour supply—the labour supplied by mothers, in the case of this study. These decreases, if significant, could attenuate the increase in after-tax incomes produced by greater government support. Thus, the article

12 The post-policy-change figures (44 percent and 9 percent) are for illustration of the policy effect and do not consider the effects of rounding.

examines mothers' participation in the labour force and usual hours worked (using data from the Labour Force Survey) and employment income (derived from the LAD). The conclusion, which is perhaps the study's most important finding, is that there is little evidence of such effects. The relevant parameter estimates produced are generally numerically small and statistically insignificant. Where there is such an impact, the amount is both modest and positive.

One qualification noted in the article concerns whether childless women are a suitable control group for measuring the effects of the policy changes. Also, because the LIM threshold of poverty is generally higher than the MBM threshold, the measured impact on poverty might have been smaller if the MBM measure had been used.

AM

Edoardo Rainone, "Tax Evasion Policies and the Demand for Cash"
(June 2023) 76 *Journal of Macroeconomics* 1-16 (https://doi.org/10.1016/j.jmacro.2023.103520)

This article analyzes how the demand for cash in Italy was affected by two policy changes that were strongly connected to tax compliance. First, beginning in 2015, financial intermediaries were required to report to the tax authority the average daily balances in their accounts. The article refers to this policy change as making bank data more visible. This supplemented previous rules for the reporting of (1) deposit balances at the beginning and end of the year and (2) the total value of transactions in the year (both debit and credit). The second policy change, in 2016, raised from €1,000 to €3,000 the maximum amount for a taxable transaction that could be settled in cash. Presumably, the practical burden that the earlier €1,000 cash limit imposed on normal personal and business transactions was considered to be too high, despite the fact that raising the cash limit could lower tax compliance.

To study the two policy changes, the article statistically estimates the parameters of an equation modelling the demand for banknotes of denomination d in month t. Two of the explanatory variables are dichotomous (zero-or-one) indicators, one of which represents the policy change. The first policy change, which makes bank data more visible, is associated with a significant increase in the demand for the highest denomination banknotes (€500 and €200). Thus, it appears that a requirement for increased disclosure of bank account balances drove people to increase cash transactions. The second policy change—increasing the maximum allowable cash transaction—significantly increased cash holdings. Considered together, the two policy changes increased cash holdings by an amount equal to 2 percent of banks' retail deposits.

In a second strand of the analysis, the article explores regional differences in tax evasion across Italy. It finds that increasing the visibility of bank data led to a more significant rise in cash holdings in regions with a higher propensity for tax evasion. By contrast, no such effect is observed following the increase in the cash transaction threshold. The findings suggest—although the paper does not draw this conclusion—that making bank data more visible was a more potent policy instrument in reducing tax evasion than a change in the maximum allowable cash transaction. That

said, an alternative interpretation is that the increase in the maximum allowable cash transaction was not large enough to have much of an effect on tax evasion.

A policy of limiting cash payments has not yet been used in Canada, and therefore it might be helpful to provide some background on the purpose of this policy instrument.[13] In Europe, the biggest spur for action in this area was perhaps the need to combat the financing of terrorist activities, although enforcing tax compliance and uncovering criminal activity (in the form of money laundering) have always been considerations, too.[14] Cash transaction thresholds may be considered a supplement to the elimination of high-denomination notes (in Canada, the $500 and $1,000 bank notes are no longer legal tender).[15]

Thresholds on cash payments are common across the world. In 2017, 16 of 20 member countries of the European Union imposed such limits.[16] In 2024, the European Council decided that, beginning in summer 2027, the highest cash threshold a member country can have is €10,000. For cash transactions between €3,000 and €10,000, the seller must ask the buyer for identification.[17]

AM

Annette Alstadsæter, Niels Johannesen, Ségal Le Guern Herry, and Gabriel Zucman, "Tax Evasion and Tax Avoidance" (February 2022) 206 *Journal of Public Economics* 1-16 (https://doi.org/10.1016/j.jpubeco.2021.104587)

A question often raised about measures to decrease tax evasion among high-income and wealthy taxpayers is whether such taxpayers will simply substitute legal tax avoidance for tax evasion and thus will not actually pay much more tax. This article sheds light on this question by examining approximately 1,500 Norwegian taxpayers who opted to disclose previously unreported foreign assets under a government amnesty program in place from 2008 through 2016. These voluntary disclosures were

13 However, Canada does have a notification requirement: reporting entities (generally financial institutions) are required to report large transactions (generally $10,000 or more) to FINTRAC: Financial Transactions and Reports Analysis Centre of Canada, "FINTRAC's Compliance Guidance: Reporting Large Cash Transactions to FINTRAC" (https://fintrac-canafe.canada.ca/guidance-directives/transaction-operation/lctr-doie/lctr-doie-eng#s2).

14 Peter Sands, Haylea Campbell, Tom Keatinge, and Ben Weisman, *Limiting the Use of Cash for Big Purchases: Assessing the Case for Uniform Cash Thresholds*, M-RCBG Associate Working Paper no. 80 (Cambridge, MA: Harvard Kennedy School, 2017) (www.hks.harvard.edu/sites/default/files/centers/mrcbg/files/80_limiting.cash.pdf), at 13.

15 Bank of Canada, "Bank Note Redemption Service" (www.bankofcanada.ca/banknotes/bank-note-redemption-service/#:~:text=claims%20we%20receive-,Bank%20notes%20that%20are%20no%20longer%20legal%20tender,not%20lost%20their%20face%20value).

16 Oz Shy, "Cash Is Alive: How Economists Explain Holding and Use of Cash" (2023) 61:4 *Journal of Economic Literature* 1465-1520, at 1482,

17 European Consumer Centre (ECC) France, "Paying in Cash: Limits in Europe," November 6, 2024 (www.europe-consommateurs.eu/en/shopping-internet/cash-payment-limitations.html#:~:text=You%20may%20not%20travel%20between,10%20000%20euros%20and%20over).

apparently a response to more stringent enforcement measures such as the conclusion of information exchange agreements with a large number of tax havens.

The main finding is that the taxes paid by these amnesty participants jumped by an average of 30 percent. The increase in their reported taxes, income, and wealth was sustained over time.[18] This increase was not accompanied by an increase in key forms of tax avoidance, such as emigration or investment in tax-favoured asset classes, despite evidence that avoidance opportunities existed for these taxpayers. The key insight for other countries is that combining an amnesty program with increased enforcement seems to make high tax rates a viable policy option despite taxpayers' opportunities for evasion and avoidance.

This research is all the more persuasive because the data used was of particularly high quality. It was possible to examine the amnesty participants' behavioural changes at the individual level, not just in the form of aggregate statistics. Also, the researchers had access to data on the entire adult population of Norway, so they could compare the amnesty participants' behaviour with that of non-participants. All data was de-identified to protect individuals' privacy.

AM

Arjan Lejour and Dirk Schindler, eds., *Research Handbook on the Economics of Tax Havens* (Cheltenham, UK: Edward Elgar, 2024)

This excellent collection of articles by leading researchers, mostly from Europe, deals with five overarching questions about tax havens. None of the articles deals specifically with Canada, but the five questions they address are as relevant here as elsewhere. The questions are the following: (1) What characterizes tax havens, and what drives their behaviour? (2) How do tax havens facilitate profit shifting by multinational corporations and thereby reduce these companies' corporate income tax payments? (3) What is the role of tax havens in the evasion of the personal income tax? (4) What are the different business models and strategies of tax havens? (5) How should tax havens be regulated? An introductory article by the editors[19] reviews these five questions and explains how each of the book's 20 chapters relates to these questions. The chapters are generally literature reviews rather than contributions of original research, but they perform a valuable service by collecting the insights of the burgeoning literature that has accumulated in this field since the 2008-9 financial crisis.

To gain some sense of the contents of the volume, consider the third question above, regarding the role of tax havens in the evasion of the personal income tax. The book's treatment of this question consists of three articles, one of them by

18 At 16.

19 Arjan Lejour and Dirk Schindler, "The Need for (Economic) Research on Tax Havens: An Overview on Where We Are and Where We Go," in Arjan Lejour and Dirk Schindler, eds., *Research Handbook on the Economics of Tax Havens* (Cheltenham, UK: Edward Elgar, 2024), 2-22.

Lisa D. Simone and Bridget Stomberg ("Information Exchange and Tax Havens," pp. 319-47). This article reviews the effectiveness of recent measures intended to increase information sharing among countries, focusing in particular on tax havens. Two early efforts in this regard, which the authors believe to have been largely ineffective, were (1) the publication by the Organisation for Economic Co-operation and Development (OECD), in 2000, of a list of 35 tax havens, along with various measures intended to induce these tax havens to sign tax information exchange agreements (TIEAs) with other countries; and (2) the establishment of the EU savings directive in 2005. In contrast, the authors conclude that two more recent efforts have had larger effects on deterring tax evasion: (1) the passage in 2010 of the US Foreign Account Tax Compliance Act (FATCA); and (2) the creation in 2014, by the OECD and Group of Twenty (G20), of a model agreement for the automatic exchange of information: the common reporting standard (CRS). In considering these four measures, the authors support their conclusions by reviewing the relevant empirical literature. The article ends with a list of specific suggestions for future research and a few suggestions for policy reform. In particular, the article calls for research into how much tax evasion occurs through the use of complex ownership structures and asks whether beneficial ownership registries could further reduce tax evasion.

AM

Michael J. Graetz, *The Power To Destroy: How the Antitax Movement Hijacked America* (Princeton, NJ: Princeton University Press, 2024)

This book is a historical account of how a once-fringe US anti-tax movement moved into the political mainstream over the last 50 years. It covers both interest group activity and actions by political leaders. It is also a critique of this movement, as its title indicates. Readers who want to follow any of the arguments in more detail can delve into the more than 70 pages of footnotes and associated references.

The tax changes discussed in the book began in 1978. A California plebiscite, Proposition 13, created a constitutional limitation on the state's property taxes that both cut back taxes at the time and limited their future growth. Subsequent tax cutting evolved in fits and starts. Under President Ronald Reagan, for example, the Economic Recovery Tax Act of 1981 cut taxes significantly, but concerns over deficits resulted in tax increases in 1982, 1983, and 1984. Similarly, under President George H.W. Bush, taxes were increased in 1990 despite his promise at the 1988 Republican convention: "Read my lips. No new taxes."[20] After that time, tax cuts became more consistent, ranging from the Taxpayer Relief Act of 1997, under President Bill Clinton, to the tax cuts under President George W. Bush in 2001 and 2003, to the Tax Cuts and Jobs Act in 2017 under President Trump. Although Republicans have mostly taken the lead, there has been significant Democratic support for tax cuts as

20 At 134-35.

well. The issue remains alive today, as many of the tax cuts enacted in 2017 expire at the end of 2025.[21]

One important point made by the author is that the effects of tax cuts have been different at the state level than at the federal level. After Proposition 13 was passed, California had a sharp drop in spending on public education, police protection, health care, and welfare. Almost all states have a balanced budget requirement, so tax cuts require cuts in government expenditure.[22] In contrast, tax cuts at the federal level in the United States have tended not to be matched by expenditure decreases, and thus both deficits and debt have grown over time. The author views this pattern as not sustainable.

AM

Adam Kern, "Reports of Pillar 2's Death Are Greatly Exaggerated" (2025) 117:8 *Tax Notes International* 1237-41

On the first day of his second term, President Donald Trump signed an executive order stating that the 2021 global tax deal "has no force or effect in the United States." Since US compliance with pillars 1 and 2 has always required an act of Congress, this statement may be dismissed as a truism.[23] Beyond the rather obvious statement of a legal fact, however, the executive order also signals a broader intent not to support any legislation that might bring the United States into compliance with either pillar.

The issue that this article addresses is whether the global minimum tax (pillar 2) can survive without US participation. According to the author, an assistant professor at the University of San Diego School of Law, this is possible for two reasons. First, so long as the United States retains its global intangible low-taxed income (GILTI) rules, the incentive for a parent entity in a jurisdiction with an income inclusion rule (IIR) to relocate to the United States is likely too small (and too uncertain, given the possibility of future tax changes) to discourage other jurisdictions from adopting an IIR. Second, since jurisdictions adopting an undertaxed profits rule (UTPR) are almost certain to credit GILTI (consistent with OECD administrative guidance released in 2023), the application of another jurisdiction's UTPR to US firms is relatively modest.

The argument is plausible, though somewhat overstated. Although the GILTI rate is close to the global minimum tax rate (and is scheduled to increase in 2026), it is still somewhat lower and applies on a blended basis rather than a country-by-country

21 See Adam Frank, "Approaching the Potential Sunset of Tax Cuts and Jobs Act (TCJA) Provisions," *JP Morgan Wealth Management*, February 13, 2025 (www.jpmorgan.com/insights/wealth-planning/taxes/tax-cuts-and-jobs-act-tcja).

22 See Urban Institute & Brookings Institution, Tax Policy Center, "What Are State Balanced Budget Requirements and How Do They Work?" (https://taxpolicycenter.org/news/unrigging-economy-will-require-enforcing-tax-laws).

23 Mindy Herzfeld, "Trump Executive Orders Bring U.S. Course Change on International Tax" (2025) 117:5 *Tax Notes International* 717-21, at 717.

basis. In addition, even if other jurisdictions' UTPRs credit GILTI, it seems highly unlikely that the Trump administration will not retaliate to the imposition of any UTPR on low-taxed profits of US multinational enterprises. As a result, the more likely short-term outcome, also suggested by the author, is that other countries might modify their IIRs to conform to GILTI rather than abandoning them altogether.

DGD

Shaun Parsons and Afton Titus, "Remote Work and the Taxation of Individuals: A Developing World Perspective and the Argument for Inter-Nation Equity" (2024) 16:2 *World Tax Journal* 325-48 (https://doi.org/10.59403/29w4s8e)

The explosion in remote work with increased digitalization and the COVID-19 pandemic poses a major challenge to traditional source rules for taxing cross-border income from labour, which generally turn on the physical performance of services within a state. In response to these challenges, a growing body of academic literature has begun to consider alternative source rules for taxing labour income in the digital era. Among these alternatives are exclusive source jurisdiction to the state in which the payer is located, exclusive source jurisdiction to the state in which services are physically performed, and exclusive residence jurisdiction.

Although much of this literature bases arguments for one or another alternative on traditional tax policy principles of equity, efficiency, and administrability, the authors propose that these criteria should be supplemented by principles of inter-nation equity that would allocate tax jurisdiction to lower-income countries. Noting that migrant workers have traditionally relocated from low-income countries to higher-income countries, but might remain in place as remote work expands, the authors conclude that inter-nation equity favours exclusive residence taxation of income from remote work.

The article is well researched and well written, and provides a useful contribution to questions about the allocation of tax jurisdiction for income from remote work. Its analysis is limited, however, to the extent that it considers alternatives involving only exclusive tax jurisdiction by a source or residence state, rather than shared jurisdiction among two or more states.

DGD