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William Watson: The Mulroneys Theory of Taxation

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[taxation](#), [Brian Mulroneys](#)

Millions of Canadians would love to delay paying tax on our income until we actually spend it. Lots of economists would like it, too



By William Watson

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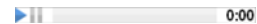
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It's a pity the Internet was only in its infancy back in the 1990s when former prime minister Brian Mulroneys was holding coffee klatches with former — well, what exactly would you call Karlheinz Schreiber? — “businessman,” I suppose, is the usual term. If the Internet had been as ubiquitous as it is today Mr. Mulroneys, who is not unfamiliar with webs, could have availed himself of the Canada Revenue Agency's lovely interactive introduction to the Canadian tax system, featuring two made-up characters named Paul and Omar. (Though the names must have been focus group-tested “Omar” doesn't actually make the top-50 male baby names in the country, according to *Today's Parent* magazine. No doubt the idea is to be inclusive.)

The first and most fundamental principle underlying the Canadian tax system, Paul and Omar learn, is fairness: “The tax system must ensure that all taxpayers share the tax burden equally.” Well, yes, though for some people it appears to be fairer than for others.

How does income taxation work? The overall impression the Web site gives is that Canadians file tax returns mainly so they can benefit from various tax credits and also take advantage of the Taxpayers' Bill of Rights. But after several instructional modules the idea does sift through that if you earn income in a year and your earnings are greater than your deductions, you should pay tax — and if you don't, that's wrong: “Earning income without reporting it is called the underground economy.” If people don't pay on time, the Canada Revenue Agency (“a large and dynamic organization,” it says of itself) will go after the money “in a firm and efficient manner.” It doesn't specify that “firm” sometimes means you'll only have to pay tax on half the income you didn't report and won't face any penalty despite your tardiness in settling your accounts.

The Web site does say that in extraordinary circumstances you may be excused from reporting or paying your taxes on time. Such circumstances include: “a natural or human made disaster, such as a flood or fire; errors in CRA publications; civil disturbances or disruption in services, such as a postal strike; or financial hardship.” It doesn't actually mention the stress that comes from suing the federal government for libelous prosecution. Maybe that's in the hard-copy fine print.

Mr. Mulroneys' case for not immediately paying tax on his retainer is that he didn't spend any of it right away. Millions of Canadians must have had exactly the same reaction: We'd love to delay paying tax on our income until we actually spend it. In fact, lots of economists also subscribe to the Mulroneys Principle of Taxation: they favour the idea of a consumption tax. Don't tax income. Tax what people spend out of income. Taxing income penalizes saving: You pay tax on the income and then again on the income you earn from saving it. How's that fair? Income should only be taxed once — though it really should be taxed that once.

As the godfather of the GST, Mr. Mulroneys did much during the late 1980s to make us all understand the economic virtues of taxing consumption. That he himself seems not to have charged Mr. Schreiber

GST is a corrosive footnote to that history. (That successor Conservatives reduced the rate of goods and services taxation was not necessarily a retrograde step. They also introduced Tax Free Savings Plans that help people shield their savings from tax.)

Unfortunately, it seems the Mulroney Principle hasn't caught on that well. Nanos Research reports this week that 48% of Canadians — and 67% of Ontarians — think Ontario's agreement to harmonize its provincial sales tax with the GST, as Quebec and Atlantic Canada previously did, is a negative thing. This will cause interesting disharmonization in the Flaherty-Elliott household, where federal Conservative Finance Minister Jim Flaherty believes harmonization is good and Ontario Conservative provincial leadership candidate Christine Elliott believes it's bad.

What's worse, when asked whether they thought harmonization would be good for Ontario's economy, 23% of Canadians and 39% of Ontarians said it would instead have a negative effect. By contrast, virtually 100% of economists believe that if you stop taxing business inputs, as Ontario's sales tax currently does, you'll get better economic performance. Respondents in provinces that actually have harmonized with the GST also — though only barely — think economic performance will improve.

That Mr. Mulroney's tax doesn't do better in the polls may have something to do with how Mr. Mulroney would do in the polls these days. That politicians can't persuade ordinary Canadians to support good principles like consumption rather than income taxes and broadly-based rather than narrowly-based consumption taxes may have something to do with how politicians in general are perceived. Fairly or not, that has lots to do with what one of them did while taking "coffee" in hotel rooms a dozen years ago.

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by 66Scorpio
May 22 2009
12:14 AM

The income tax rules for lawyers are something like this:

- 1) You don't tax money clients give you initially as a retainer because it is held in trust: it is still the client's money, not yours.
- 2) As you perform work, you issue a bill and transfer the trust funds to your own account, and that becomes income.
- 3) As you perform work for a client, but before you bill it (know as work-in-progress or WIP ["whip"]), that amount will be counted towards income when you report your professional income on your T1 income tax return.
- 4) A professional can opt out of reporting WIP as income, under certain rules pursuant to the Income Tax Act.

It's not a matter of "spending" the money but of when you take money that you are holding for someone else and make it your own for the work you have performed.

I'm not a tax lawyer. Mulroney is not a tax lawyer. But it is beyond comprehension that he would leave such matters to his own tax lawyer without having a



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