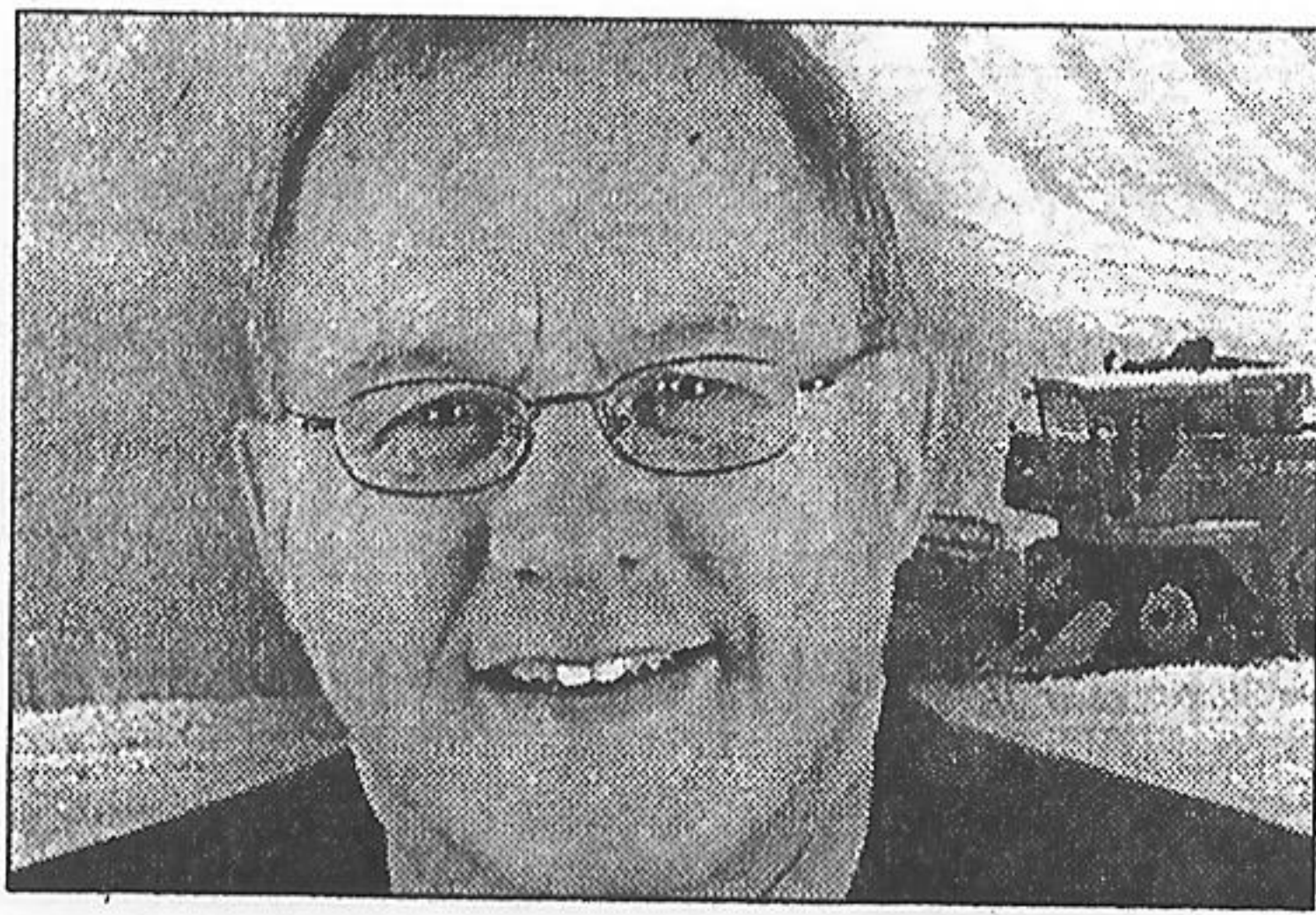


Tax ruling should be warning to gov't

When a tax is unconstitutional, it cannot be kept and must be repaid, says court

Lorne Gunter



In the early 1980s, New Brunswick began levying a surcharge on the liquor served by bar and restaurant owners.

On top of the retail price of the liquor, on top of the provincial sales tax, the excise tax hidden in the retail price and, eventually, the GST, the N.B. government began dinging lounge operators and restaurateurs an addition 11 per cent "user charge."

In 1988, Kingstreet Investments began operating several bars and restaurants in Fredericton and Moncton. So, of course, all its liquor purchases were subject to N.B.'s user charge.

In 2001, Kingstreet decided it had had enough and it took the provincial government to court claiming the user fee was nothing more than an indirect tax that the province lacked the constitutional authority to levy.

It won. Sort of.

The trial judge agreed the 11 per cent charge was an unconstitutional tax, but denied Kingstreet's request to be repaid a sum of nearly \$1 million, which it calculated was the amount it had paid over the year, plus interest.

Kingstreet had passed on the cost to its customers through higher drink prices, the trial judge found, so it wasn't entitled to reimbursement.

It was a lose-lose judgement. Kingstreet lost its claim to be compensated for all the wrongful tax it had paid. Meanwhile, the provincial government lost a lucrative tax. Shortly after Kingstreet's first trial, N.B. killed its user fee.

Kingstreet appealed, and won, but again it was only a partial victory.

The N.B. court of appeal agreed the

regulatory surcharge was just a disguised tax, and one the province lacked the constitutional power to levy.

It also upheld Kingstreet's claim to restitution, but only from the time the company filed its first court application. In other words, since it had not gone to court to fight the tax between 1988 and 2001, it was not entitled to reimbursement for any taxes it paid during those 13 years.

The levy might have been *ultra vires* beyond the province's constitutional authority — yet, since Kingstreet had paid it without complaint for 13 years, it had given the fee its tacit consent.

Therefore, the N.B. treasury only had to pay Kingstreet back those user charges collected from the time they filed their lawsuit in 2001 to the date on which N.B. ended that charge in 2002; a tiny sum.

As the lower court had, the appeal court accepted the "passing-on defence" argued by the province: Kingstreet had passed on the user charge through higher bar prices. As such it had suffered no financial loss. So whether or not the user fee was unconstitutional, Kingstreet had no case for being reimbursed.

But in what John Carpay of the Canadian Constitution Foundation has dubbed a major victory for taxpayers across the country (and not just N.B. bar patrons), the Supreme Court on Thursday overturned the lower courts' rulings against repaying Kingstreet and ordered the province to make financial restitution.

There's just one hitch: The government doesn't have to pay for more than the six years prior to the date on which Kingstreet's claim was filed.

Carpay, whose new legal and constitutional think-tank intervened in the case, says the ruling is surprisingly forceful.

In a rare 9-0 ruling, the justices decided that "illegally collected taxes should be returned to taxpayers," Carpay explained. In contradiction to the two lower courts, the Supreme Court decided

that when a tax is unconstitutional, it cannot be kept — period — and must be returned to those from whom it was wrongfully taken, even if they didn't file a formal protest against it or were able to pass on the amount.

If the basis of a tax is unconstitutional, governments have no right to the money it brings in in the first place. End of argument.

Mr. Justice Michel Bastarache, writing on behalf of the court, said "When the government collects and retains taxes pursuant to *ultra vires* legislation, it undermines the rule of law. To permit the Crown to retain an *ultra vires* tax would condone a breach of this most fundamental constitutional principle."

Carpay also paraphrased other important aspects of the decision.

"All manner of taxes, rates, fees and charges should be extracted only under legal authority, pursuant to constitutional principles. And governments should be required to honour the Constitution, facing penalties or other consequences when they don't."

Governments — both federal and provincial — have for many years now exceeded their constitutional limits, both in taxation and policy making.

I am not talking about the income tax being unconstitutional. There is a powerful conspiracy theory that gains momentum from time to time that contends Ottawa has no authority to tax incomes. It is based on a misreading of the constitution. Regrettably, the income tax is legit — excessive, but legitimate.

I am talking about taxes such as this one, masquerading as a fee to get around the constitution's prohibition against province's imposing indirect taxes.

And I am talking about Ottawa meddling in urban affairs, education and health care, where the constitution gives it no role.

Perhaps this decision will force governments to be more aware of their constitutional limitations, or face the consequences.