# Holding Governments Accountable to Canada's Constitution

Comparing the Canadian Constitution Foundation’s Factum
and the 2007 Supreme Court of Canada’s decision in
*Kingstreet Investments Ltd. v. New Brunswick (Finance)*

# Introduction

In January 2007, the Supreme Court of Canada ruled that governments – like people – should be held accountable for their actions. In *Kingstreet Investments v. New Brunswick*, people earning a living in the hospitality and entertainment industries successfully challenged an 11% provincial "user charge" on alcoholic beverages. Under Canada's Constitution, only the federal government may impose an indirect tax, such as an import duty, paid by one person (e.g., a bar owner) in the expectation that it will be repaid by another (e.g., a bar patron). Provinces may not do so. Handing a significant victory to taxpayers, the Court ordered the New Brunswick government to repay one million dollars of illegally collected taxes to taxpayers. The user charge was an illegal tax, so the Court rightly ordered the government to repay the money.

The B.C., Alberta and Manitoba governments intervened in the Supreme Court of Canada in support of New Brunswick, to argue that governments should not be required to repay illegal taxes that are collected in violation of Canada's Constitution. Before the Supreme Court of Canada, these provinces claimed that having to repay illegal taxes would inflict financial shock and fiscal chaos, forcing governments to reduce services or to raise taxes. This claim is a self-serving justification for illegal activity, and it assumes that there is no waste, mismanagement or inefficiency in the public sector. This claim also assumes that every tax dollar, without exception, is spent to advance the common good. According to the governments, when a court rules that a particular fee or charge is illegal, the court should simply tell the government "stop doing that" – but not order the government to repay the money. The Court rejected these arguments and unanimously accepted the principles put forward by the Canadian Constitution Foundation: that governments must be held accountable to the constitutional principles of federalism, representative democracy, the rule of law, and "no taxation without representation." The *Kingstreet* decision highlights the importance of court challenges to restrain greedy governments from doing whatever they please to feed their never-ending appetite for money.

As an intervener before the Supreme Court of Canada, the Canadian Constitution Foundation submitted the following arguments:

1. The Constitutional principle of "no taxation without representation" should be respected. Taxes collected in breach of constitutional principles should be recoverable.

2. There should be no bars to the recovery of unconstitutional taxes. The "Immunization Rule" should be rejected.

3. The Government's "passing on" defence should also be rejected.

4. Governments should be required to repay unconstitutional taxes regardless of whether or not the taxpayers protested.

5. The legislatures, not the courts, are the best forums for changing unconstitutional laws and dealing with potential 'fiscal chaos.'

| 1. *The Constitutional principle of "no taxation without representation" should be respected. Taxes collected in breach of constitutional principles should be recoverable.* | | | |
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| **Paragraph** | **Canadian Constitution Foundation Factum** | **Paragraph** | **Supreme Court of Canada Decision** |
| **15** | Any tax collected without lawful authority, whether by virtue of begin beyond the constitutional authority of the legislature or by simply being beyond the express authority of the legislation, violates the constitutional principles enunciated in section 53, and there is no basis for the government to retain the tax. | **14** | The Court's central concern must be to guarantee respect for constitutional principles. One such principle is that the Crown may not levy a tax except with authority of the Parliament or the legislature: *Constitution Act, 1867*, ss. 53 and 90. This principle of "no taxation without representation" is central to our conception of democracy and the rule of law. As Hogg and Monahan explain, this principle "ensures not merely that the executive branch is subject to the rule of law, but also that the executive branch must call the legislative branch into session to raise taxes" (P. W. Hogg and P. J. Monahan, *Liability of the Crown* (3rd ed. 2000), at p. 246. See also P. W. Hogg, *Constitutional Law of Canada* (loose-leaf ed.), vol. 2, at pp. 55-16 and 55-17; *Eurig*, at para. 31, *per* Major J.). |
| **19** | The Foundation submits that the right to recover taxes collected without authority flows from the constitutional status of the principle, "no taxation without representation."<br><br>"[T]he constitutional principle that ought to dominate all others in this context is the principle that the Crown may not levy a tax except by the authority of Parliament or the Legislature. This principle...ensures not merely that the executive branch is subject to the rule of law, but also that the executive branch must call the legislative branch into session to | **22** | Professor Hogg has explained that<br><br>"[T]he constitutional principle that ought to dominate all others in this context is the principle that the Crown may not levy a tax except by the authority of Parliament or the Legislature. This principle...ensures not merely that the executive branch is subject to the rule of law, but also that the executive branch must call the legislative branch into session to raise taxes (and vote supply). To permit the Crown to retain a tax that has been levied without a legislative authority is to condone a breach of one of the most |

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| | raise taxes (and vote supply). To permit the Crown to retain a tax that has been levied without a legislative authority is to condone a breach of one of the most fundamental constitutional principles." [emphasis added] | | fundamental constitutional principles." [emphasis added] |
| | | **15** | 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. As a result, a citizen who has made a payment pursuant to *ultra vires* legislation has a right to restitution: P. Birks, "Restitution from the Executive: A Tercentenary Footnote to the Bill of Rights", in P. D. Finn, ed., *Essays on Restitution* (1990), c. 6, at p. 168. |
| **20** | A similar statement may also be found in the dicta of Lord Goff in *Woolwich Equitable Building Society v. Inland Revenue Commissioners*, that:<br><br>. . . the retention by the state of taxes unlawfully exacted is particularly obnoxious, because it is one of the most fundamental principles of our law — enshrined in a famous constitutional document, the *Bill of Rights 1688* — that taxes should not be levied without the authority of Parliament; and full effect can only be given to that principle if the return of taxes exacted under an unlawful demand can be enforced as a matter of right. | **17** | In *Woolwich Equitable Building Society v. Inland Revenue Commissioners*, [1993] A.C. 70, the House of Lords has also recognized a right to restitution for payments made pursuant to *ultra vires* taxes. Without even referring to unjust enrichment, Lord Goff held, at p. 172, that restitution was available as a matter of "common justice":<br><br>. . . the retention by the state of taxes unlawfully exacted is particularly obnoxious, because it is one of the most fundamental principles of our law — enshrined in a famous constitutional document, the *Bill of Rights 1688* — that taxes should not be levied without the authority of Parliament; and full effect can only be given to that principle if the return of taxes exacted under an unlawful demand can be enforced as a matter of right. |

*2. There should be no bars to the recovery of unconstitutional taxes.*
*The "Immunization Rule" should be rejected.*

The "Immunization Rule" was suggested by La Forest J. in *Air Canada, 1989,* to allow governments the right to retain illegally collected taxes due to policy concerns such as "fiscal chaos."

| Paragraph | Canadian Constitution Foundation Factum | Paragraph | Supreme Court of Canada Decision |
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| **35** | The Foundation submits that this Court should reject the so-called "immunization rule" in this appeal, just as it has rejected earlier common law defences to recovery based on the distinction between mistake of fact and mistake of law... Given the supremacy of the Constitution and the democratic underpinnings of Section 53, the so-called "immunization rule" suggested in obiter by a minority of judges in *Air Canada*, *1989*, should not be permitted to take hold as a common law bar to recovery. | **30** | For these reasons, I would not adopt the general immunity rule proposed by La Forest J. [in *Air Canada, 1989*] ... As such, failure to adopt the immunity rule articulated by La Forest J. does not suggest that *within* the law of unjust enrichment policy considerations might not apply to limit the liability of public bodies in certain contexts. Because La Forest J.'s immunity rule was formulated outside of the law of unjust enrichment, its rejection should not have a bearing on the future development of this branch of the law. This being said, as I will now demonstrate, the law of unjust enrichment should not find application in cases for the recovery of illegally imposed taxes. |

*3. The Government's "Passing On" defence should also be rejected.*

The basic premise of the "passing on" defence is that the taxpayer has passed on the burden of the illegal tax payments to others, usually via price increases charged to its customers. According to this theory, the taxpayer has therefore not suffered a deprivation, and the taxpayer would receive a windfall if it were awarded recovery.

| Paragraph | Canadian Constitution Foundation Factum | Paragraph | Supreme Court of Canada Decision |
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| **43** | If this Court is inclined to recognize "passing on," it should at least not be incorporated into the unjust enrichment test, when considering the second element of whether there has been a corresponding "deprivation" of the plaintiff. Rather, whether there has been "passing on" should be considered independently when considering the appropriate remedy. As this Court recognized in *Garland v. Consumers' Gas Co.*, defences to a | **36** | The application of private law principles in the realm of public and constitutional law is not without its difficulties. These difficulties have in the past been resolved by a flexible application of the unjust enrichment principle. McLachlin J. had explained in *Peel* that the three-part formulation of the unjust enrichment principle was capable of going beyond the traditional categories of recovery and of allowing the law to develop in a |

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| | claim for restitution may be considered independently after the three steps for a claim in unjust enrichment have been made out... | | flexible way as required to meet changing perceptions of justice. This restitutionary framework was recently restated and refined in *Garland v. Consumers' Gas Co.*, [2004] 1 S.C.R. 629, 2004 SCC 25. *Garland* established a two-part analysis for determining whether there was a juristic reason for the enrichment that should operate to deny recovery. First, the plaintiff is required to show that no established category of juristic reason for the enrichment exists. If no reason exists, the burden shifts to the defendant to show that there is some other reason why recovery should be denied. At this point of the analysis, the Court explicitly recognized that the juristic reasons for the enrichment had to be considered in light of the reasonable expectation of the parties and certain public policy considerations (para. 46). It is at this second stage of the test that courts would weigh the equities in the particular circumstances of each case. |
| **44** | The Foundation submits that the second element of the unjust enrichment test should simply be whether the immediate plaintiff incurred the tax liability, and made the payments out of its own money to the government. The ability of a business to absorb such losses, directly or indirectly, or to still remain viable, should not be confused with an argument that no loss was suffered due to the burden being "passing on". Examining whether "damages" were incurred at this stage is inconsistent with restitution as an equitable principle, where disgorgement or an accounting of profits is often a common remedy. | **39** | For the above reasons, I would conclude that the ordinary principles of unjust enrichment should not be applied to claims for the recovery of monies paid pursuant to a statute held to be unconstitutional. I do not therefore need to address in any length the distinction between mistake of law and mistake of fact, which used to be of significance in unjust enrichment cases for mistaken payments. Traditionally, although monies paid under mutual mistake of fact were recoverable, monies paid under mutual mistake of law were not. However, this Court has abandoned the distinction between mistake of fact and mistake of law as it applies to the law of unjust enrichment: see *Air Canada*; *Canadian Pacific Air Lines Ltd. v. British Columbia*, [1989] 1 S.C.R. |

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| | | | 1133; and *Pacific National Investments*. There can be no doubt that the ordinary principles of unjust enrichment now apply in cases of payments made pursuant to mutual mistake of law. While this point perhaps needed to be clarified, it is of little moment in this case given that unjust enrichment is an inappropriate framework for restitution. |

*4. Governments should be required to repay unconstitutional taxes regardless of whether or not the taxpayers protested.*

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| **45** | Consistent with its overall position regarding recoverability, the Foundation submits that whether a party paid ultra vires taxes under protest is immaterial. Formal protest should not be required in light of the coercive authority of governments to enforce tax demands. In the alternative, the Foundation submits that if there are legitimate public policy concerns that arise in the evidence at the remedial stage, then the presence or absence of protest may be a relevant factor for a court to take into account when fashioning a remedy for the individual taxpayer who has successfully challenged the collection of a tax without authority. | **53** | In my view, the doctrine of protest and compulsion is simply not applicable to cases such as the present. This flows from the constitutional basis for the right of restitution in this case: that the Crown should not be able to retain taxes that lack legal authority. It therefore matters little whether the taxpayer paid under protest and compulsion. If the law proves to be invalid, then there should be no burden on the taxpayer to prove that they were paying under protest. Such a finding would be inconsistent with the nature of the cause of action in this case. |
| **46** | In any event, the commencement of an action to recover charges which are held to be ultra vires taxes is a sufficient ground, in and of itself, to | **58** | In cases not involving payments made to public authorities pursuant to unconstitutional legislation or the misapplication of an otherwise valid |

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| | obtain recovery. To hold otherwise raises a prohibitive disincentive for citizens to seek to ensure that constitutional principles are respected. | | law, my view is that courts should insist on proof of compulsion in fact. The mere fact that the payment was made in protest should be neither necessary nor sufficient to establish compulsion. Protest may accompany a voluntary payment (in order to protect a hypothetical restitutionary entitlement), and compulsion may occur without any evidence of formal protest. Insisting on compulsion in fact is more principled and ensures that all similarly situated persons will be treated equally, regardless of protest. |

*5. The legislatures, not the courts, are the best forums for changing unconstitutional laws and dealing with potential 'fiscal chaos.'*

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| **54** | Further, courts are ill equipped to determine whether ordering recovery in a particular case will cause "fiscal chaos"... | **25** | Another policy reason given by La Forest J. for the immunity rule was a concern for fiscal inefficiency and fiscal chaos (p. 1207). My view is that concerns regarding potential fiscal chaos are best left to Parliament and the legislatures to address, should they choose to do so. Where the state leads evidence before the court establishing a real concern about fiscal chaos, it is open to the court to suspend the declaration of invalidity to enable government to address the issue.[emphasis added] |
| **36** | In addition to condoning a breach of constitutional principles, an approach that uses a "presumption against recovery, subject to exceptions" will ultimately end up being just as confusing as the mistake of fact/law distinction it replaced. The preferable approach is to recognize a prima facie right to recovery, and to provide the legislature with the opportunity to address the constitutional flaw. [emphasis added] | | |