
As affluent boomers inevitably confront the prospect of their own mortality, estate-planning practices are certain to expand. For practitioners contemplating entry into this field, Frostiak and Poyser provide an excellent explanation of substantive legal rules as well as detailed information on tax returns and filing requirements for trusts.

The book is divided into six parts. Part I offers a concise review of basic estate and trust planning, including a general overview of trust law (chapter 1) and a detailed description of different kinds of trusts—testamentary trusts, inter vivos trusts, spousal trusts, trusts for minor beneficiaries, and alter ego and joint spousal or common-law trusts—and related planning considerations (chapter 2). Part II reviews the taxation of trusts and beneficiaries, with chapters on the taxation of trusts (chapter 3), the taxation of beneficiaries (chapter 4), attributions to contributors under subsection 75(2) of the Income Tax Act¹ (chapter 5), and dispositions of trust property (chapter 6). Part III reviews the filing requirements and administrative practices of the Canada Revenue Agency. Part IV explains the T3 trust income tax and information return. Part V outlines the T3 summary and T3 slips for income allocations and designations to beneficiaries. Part VI is made up of three appendixes listing interpretation bulletins, information circulars, technical interpretations, and marginal tax rates for testamentary and inter vivos trusts.

Although, as the title suggests, the book’s primary readership is likely to be made up of lawyers and accountants whose practices involve trusts and estates, the substantive chapters could serve as useful teaching materials for any course on trusts and estate planning.

D.D.

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¹ RSC 1985, c. 1 (5th Supp.), as amended (herein referred to as “the Act”). Unless otherwise stated, statutory references in this article are to the Act.

This chapter appears in a new volume in the popular “Law Stories” series, which provides an alternative way of teaching traditional legal subjects through an emphasis on specific cases or case studies.2 “Travails in Tax” describes KPMG’s tax-shelter business in the United States—the developing and mass marketing of shelters that led to a Senate subcommittee investigation in the fall of 2003, the replacement of several high-level partners in 2004, and a continuing criminal investigation by the US Justice Department.

After a brief explanation of the changing role of accounting firms in tax practice and the development of retail tax-shelter products in the 1990s, Rostain recounts the story of KPMG’s tax-shelter activities, including its questionable opinion letters on the merits of specific products, its attempts to “fly under the IRS’s radar screen” by disregarding tax-shelter registration rules, its advice to clients to use impermissible reporting methods in their tax returns, and its resisting of IRS enforcement summonses. In the summer of 2002, a young lawyer named Mike Hamersley contacted the government after his superiors instructed him to modify audit information in a manner that he concluded would violate provisions of the Sarbanes-Oxley Act. Following Hamersley’s dismissal and inquiries by the Senate Permanent Subcommittee on Investigations and the US Justice Department, KPMG disbanded its tax-shelter practice, removed or obtained the resignation of many of the partners involved, and agreed to waive claims of solicitor-client privilege in connection with transactions under investigation.

Rostain concludes by asking what lessons can be drawn from this story and from Hamersley’s experience in particular. With respect to legal practice, she suggests, the KPMG story “illustrates the continued importance of the institutions of professionalism.”

Many of the principal players in the firm’s tax practice were lawyers who used their tax expertise outside the confines of traditional lawyer-client relationships. Although precise numbers are hard to come by, a growing number of law graduates are finding it advantageous to renounce law practice in favor of characterizing themselves as consultants or legal experts. In claiming that they are not practicing law, “law specialists” seek to sell their expertise outside the strictures of professional regulation. The KPMG saga signals some of the risks of this strategy. By divesting themselves of a professional persona of a lawyer, law specialists may end up caring less about the law.

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With respect to Hamersley’s experience, Rostain offers some advice to practitioners:

Choosing to work at professional organizations that value dissent and constructive dialogue is a start. KPMG’s hierarchical and highly conformist culture made it difficult for employees to question tax shelter activity and encouraged them to engage in “group think.” Hamersley’s experience is also a reminder that lawyers, no matter how junior, should have faith in their own judgments and not simply defer to more senior lawyers on ethical issues. The fact that “everyone else is doing it” in an organization or particular sphere of practice, is never, of itself, a sufficient justification for engaging in questionable conduct.

Sage advice indeed.

D.D.

Canada Revenue Agency, The Canada Revenue Agency: The First Five Years—Setting the Foundation for Tax and Benefit Administration in the 21st Century (Ottawa: Canada Revenue Agency, 2005), 80 pages

When Revenue Canada became the Canada Customs and Revenue Agency in 1999, the CCRA Act called for a five-year “review and assessment of the provisions and operation” of the legislation by a House of Commons or Senate committee. This account of developments in the past five years is intended to assist with the expected review. Some interesting information is provided: we learn, for example, that the percentage of personal income tax returns filed electronically rose from 31 percent in 2000 to 47 percent in 2004; that the delegation of contracting authority to budget managers went too far in that lower-level managers did not have the expertise to follow prescribed procedures; and that the level of employee satisfaction has increased from 60 percent to 70 percent. However, most of the content is too self-laudatory to be useful. For example, the report cites evidence of increased CRA administration of provincial programs without noting that the achievements fall far short of the goals.

A.M.


Taxes on the transfer of wealth—estate and gift taxes and inheritance taxes—have been abolished in a number of developed countries, including Canada and Australia in the 1970s and 1980s, New Zealand in the 1990s, and the United States in

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3 At 55.
4 At 47.
5 At 51.
2001.\textsuperscript{6} This pattern cannot be attributed solely to conservative electoral victories; in Canada, for example, the Liberal Party abolished estate and gift taxes in 1971. Duff uses historical analysis and political choice theory to explain this trend, arguing that wealth transfer taxes have attracted substantial criticism and have had few supporters. He concludes by suggesting a number of ways in which such taxes could be made politically acceptable. For example, he suggests emphasizing their symbolic and social function (to lessen inequalities and unequal opportunities) rather than the revenue they raise, and taxing living beneficiaries rather than estates. He also argues that wealth transfer taxes should not be levied by provincial governments because the potential for interprovincial tax competition is too great.


Although most health-care costs incurred in hospitals or doctors’ offices are covered by medicare, about 30 percent of health-care expenditures are privately financed.\textsuperscript{7} These expenditures are generally eligible for the medical expense tax credit, and about 15 percent of tax filers with taxable incomes claimed this credit in 2000.\textsuperscript{8} However, Smart and Stabile compare tax data to surveys of personal expenditures and conclude that there is evidence of low takeup rates among high-income individuals: 21 percent of individuals with incomes over $50,000 qualify for the credit, yet only 6 percent actually make the claim.\textsuperscript{9} It appears that collecting and retaining the receipts is cumbersome and deters claims. Despite this, the authors conclude that the effective reduction in the price of health-care services created by the tax credit has the effect of increasing health-care spending, just as more direct point-of-service subsidies have.

A.M.


How, in a democratic society, could a majority of the legislature vote to repeal a tax that applies only to the richest 1 or 2 percent of the population; that encourages charitable gifts; and that reflects the widely accepted principle that people should have an equal opportunity to pursue their economic dreams? Addressing the “political

\textsuperscript{6} In a bizarre use of transitional rules, the abolition of estate and gift taxes in the United States is delayed until 2010, and then the tax is reinstated in 2011.

\textsuperscript{7} At 349.

\textsuperscript{8} At 354.

\textsuperscript{9} At 363.
mystery” behind the demise of US wealth transfer taxes, Graetz and Shapiro have written a fascinating account of contemporary US politics; they document the remarkable success of the Republican anti-tax movement and the consistent failure of Democratic defenders.

The first party of the book (“An American Story”) documents the strategies and growth of the US gift and estate tax repeal movement and the disorganized and ineffective response of the tax’s potential supporters. The second part (“The Battle for Passage”) moves “inside the beltway,” recounting the manner in which Republican strategists translated the repeal movement into legislative action. The third part (“Lessons Learned and Missed”) draws various lessons from the political debate and considers its future implications for tax policy. The authors find that contemporary political debates are won more easily with stories or narratives (at which the repeal movement excelled) than with facts and arguments (on which defenders relied), and that advocates of wealth transfer taxes failed to counter the repeal movement’s moral arguments against the taxes with moral arguments of their own. As anti-tax activists shift their attention to progressive income taxation, the authors conclude, those who wish to defend traditional conceptions of tax justice ignore these lessons at their peril.

D.D.


This report contains statistical data on the contribution of different income groups to federal personal income tax revenue in 1990 and 2002. In 1990, the one-tenth of tax filers with the highest incomes provided 46 percent of revenue; by 2002, this group’s contribution had increased to 53 percent. The increase came about partly because this group had a smaller decrease in its effective tax rate over the period than other tax filers, and partly because its share of income rose from 32 percent to 36 percent.

A.M.


Part of this short monograph is devoted to the criticisms of the concept of “tax freedom day” that one might expect from an advocate of the social value of public expenditures. However, much of the monograph consists of a detailed examination of the calculation methods. One interesting point is that the method of calculation used by the Fraser Institute for Canada is quite different from that used by the Tax Foundation for the United States; hence, the comparisons of “tax freedom days” in the two countries that frequently appear in newspaper reports are largely invalid.

A.M.

The question addressed in this article is whether tax practitioners charge higher fees for preparing tax returns when taxpayers receive tax refunds, and how the level of fees is related to the amount of any tax refund. The authors argue that there is lower taxpayer resistance to high fees when the act of filing a tax return is viewed as a “gain” proposition because the refund exceeds the fee. The evidence, which is from the United States, suggests that there is a positive relationship between fees and refunds; the implication is that ethics rules prohibiting contingent fees for tax compliance services may be only loosely followed.

A.M.


This new textbook on public economics will be of interest to anyone seeking an introduction to the field. Although it is a US publication, it is well worth reading because of its use of interesting anecdotes about real-world situations to illustrate issues and its discussion of empirical findings. An excellent chapter on the empirical tools of public finance emphasizes the distinction between correlation and causal inference, and chapters on particular areas of public economics show how empirical findings supplement theoretical results. For example, the discussion of the tax preferences for housing notes the usual theoretical point that the tax preferences can be justified if there are positive externalities of home ownership. The novelty is that this point is followed by a discussion explaining why the existence of such externalities is so difficult to prove empirically.

A.M.


Common sense suggests that security prices should be affected by investors’ expectations about future tax rates. However, this hypothesis has been difficult to prove because it is so hard to measure expectations. The authors examine the 1992 US presidential campaign, in which there was a clear choice between Bill Clinton’s promise to raise taxes and George H.W. Bush’s pledge, “Read my lips: no new taxes.” The authors measure the likelihood of Clinton being elected by the daily changes that occurred in the Iowa Political Stock Market, in which participants bet money on the outcome of the election. The data show that increased probabilities of Clinton winning the election were associated with decreased returns on tax-exempt
bonds, which is exactly what one would expect if tax rates were thought to be increasing in the future.

A.M.


Corporate income tax revenues are known to be difficult to predict in Canada and many other countries. In the United Kingdom, corporate tax revenues have generally been larger than expected, given the reductions in statutory rates over the past 20 years; yet the increase cannot be fully explained by base broadening. After a detailed review of alternative explanations, the authors conclude that the increase in revenue is due to non-tax causes. In particular, there were sectoral changes in the UK economy, notably an expansion of the financial sector and, partially as a consequence, a rise in the share of corporate profits in national income.

A.M.


Currently, both federal and provincial budget documents report the expected revenue changes associated with key tax changes without disclosing anything about how the estimates are arrived at. Tax expenditure accounts published every summer by the federal government report the revenue cost of key deductions and credits with a little more disclosure, but not much. In this article, the author surveys US and international practices in this area and discusses the arguments for and against greater transparency. One argument in favour of greater transparency is that public and academic discussion of revenue-estimating practices could improve the work of federal and provincial revenue estimators. Also, since financial considerations often drive tax policy decision making, a better understanding of the numbers could allow a more informed public discussion of tax policy.

A.M.

Chris Edwards, “Corporate Tax Reform: Kerry, Bush, and Congress Fall Short” (2004) vol. 105, no. 2 Tax Notes 244-46

This article provides a handy table of statutory corporate tax rates in 69 countries. Although comparisons of corporate tax rates can be misleading because they do not show differences in tax bases and tax credits, the data are nonetheless quite striking. Corporate tax rates have been falling, and in 2004 the average rate in Asia, Europe, and Latin America was 30 percent or less, as compared with 36 percent for Canada and 40 percent for the United States. The common tendency to compare Canada only with the United States may provide incomplete data.

A.M.

In preparing budget documents, governments devote much attention to how the effects of the budget on different income groups are presented. There is seldom, if ever, a desire to present the budget changes as favouring the rich, even if this might be the appropriate goal of tax policy at the time. Zelenak examines the tax cuts enacted by the current US administration and notes that the cuts were always presented in terms of percentage reductions in income tax liabilities of taxpayers at different income levels. He suggests that a fairer approach might be to report percentage increases in after-tax incomes, which would make the cuts appear more regressive.

A.M.


The recent Canadian controversy over civil penalties for tax practitioners has interesting parallels to a similar debate in the United States. The authors argue that the lack of an effective US civil penalty regime has led to the proliferation of abusive tax shelters and government investigation of public accounting firms there. Have the Canadian rules been a factor in the lesser degree of similar problems here?

A.M.


Publications that compare tax systems across countries are both valuable and rare. Thus, it is encouraging that the original 1997 edition of this book has been updated, with Brian J. Arnold joining Hugh J. Ault as a co-editor. The first third of the book consists of nine individual country chapters plus a short note on the European Union; the rest of the book is a comparative analysis of rules for basic income taxation, the taxation of business organizations, and international taxation.

A.M.


Taxation of worldwide income based on residence creates obvious incentives for individuals and corporations to relocate to low-tax jurisdictions in order to reduce
their income taxes. These articles offer an excellent analysis of tax incentives for individual and corporate “expatriation” from the United States as well as the tax and non-tax measures that the US Congress has adopted in response to those incentives. Criticizing the responses as largely symbolic, Kirsch proposes other measures to lessen the incentives for tax-motivated expatriations.

In the first article, Kirsch examines tax-motivated expatriation by individuals. Because the United States taxes worldwide income on the basis of citizenship rather than residence, this can be accomplished only when an individual ceases to be a citizen of the United States—for example, by renouncing citizenship. If one of the principal purposes for the termination of citizenship is the avoidance of federal income taxes, section 877 of the Internal Revenue Code\(^\text{10}\) requires individuals to continue to pay US tax at graduated rates for 10 years, not only on conventional US-source income but also on gains from the disposition of property located in the United States as well as gains from the disposition of shares of debt of US corporations. In practice, however, this rule is difficult to enforce, since US tax authorities are unlikely to know whether a former citizen has sold shares or debt of a US corporation.

Despite numerous proposals to enact a mark-to-market rule for individual expatriations similar to Canada’s deemed disposition rule in subsection 128.1(4) of the Act, the US Congress has resisted substantive tax changes and has adopted only a statutory presumption of tax avoidance based on the net worth and average income tax liability of the individual at the time of expatriation.\(^\text{11}\) At the same time, however, Congress has enacted non-tax legislative sanctions designed to discourage tax-motivated expatriations by publicizing the names of individuals who cease to be citizens of the United States and disallowing the readmission to the United States of individuals who are found to have renounced their citizenship in order to avoid US taxes. The remainder of the article criticizes these non-tax sanctions as both overbroad and ineffective, suggests that tax benefits from individual expatriation should be lessened before non-tax alternatives are pursued, and considers the appropriate place of non-tax sanctions to support these amended tax rules.

In the second article, Kirsch examines corporate expatriations and considers congressional responses to “corporate inversion” transactions in which shareholders exchange shares of a US parent for shares of an offshore sub, which becomes the new parent of a US sub. In the Homeland Security Act of 2002 (HSA), Congress created a non-tax sanction against corporate inversions by preventing expatriated corporations from entering into government contracts with the Department of Homeland Security. In the American Jobs Creation Act of 2004 (AJCA), Congress adopted a tax response to corporate inversions by introducing legislation that treats expatriated corporations as domestic corporations.

\(^{10}\) Internal Revenue Code of 1986, as amended (herein referred to as “IRC”).

\(^{11}\) IRC section 877(a)(2), enacted in 2000.
The author begins by reviewing US tax rules for multinational corporations; he explains residence-based and source-based tax rules and the place-of-incorporation test for corporate residence. Although expatriated corporations continue to be subject to US tax on US-source income, a corporate parent that ceases to be a resident in the United States can avoid the application of controlled foreign corporation (subpart F) rules. The author contends that despite the various rules designed to prevent domestic earnings stripping, expatriated corporations are generally able to reduce taxes on US-source income through offshore debt and transfer pricing. As a result, although corporate inversion transactions generally trigger taxation at the corporate or shareholder level, significant tax incentives encourage taxpayers to engage in these transactions.

The rest of the article reviews congressional responses to corporate expatriations, beginning with the HSA and culminating in the AJCA. After criticizing the HSA as an example of symbolic legislation that purports to address a perceived problem without having much actual effect, the author argues that the AJCA points to a more fundamental problem with the basic place-of-incorporation test for corporate residence. Instead, he concludes, Congress should consider a more substantive test of corporate residence based on day-to-day management and control.

D.D.


Alongside other strategies to encourage economic development in sub-Saharan Africa, it is often suggested that tax treaties can increase trade and investment by reducing double taxation. Canada has entered into tax treaties with 10 sub-Saharan African countries; however, the only such country with which the United States maintains a tax treaty is South Africa. Despite numerous arguments in favour of these treaties and apparent interest on the part of several sub-Saharan countries, the author argues that tax treaties with most less developed countries (LDCs) are

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12 Cameroon, Gabon, Ivory Coast, Kenya, Nigeria, Senegal, South Africa, Tanzania, Zambia, and Zimbabwe. Although signed in 2002, the treaty with Gabon is not yet in force. For a list of Canada’s tax treaties, see the Department of Finance Web site at http://www.fin.gc.ca/treaties/cndtxtreat_e.html.


14 Nigeria, for example, began pursuing a tax treaty with the United States in 1978 after it unilaterally withdrew from coverage under an extension of the 1945 tax treaty between the United States and the United Kingdom. Although negotiated at length, the treaty was never completed.
unlikely to have much impact on taxes paid by multinational enterprises. As a result, she concludes, there is little private sector pressure for these agreements and little probability that they will increase trade and investment, suggesting that alternative approaches should be adopted to promote economic development.

The author begins by reviewing the role of tax treaties in the international tax system and the basic structure of the OECD model treaty\textsuperscript{15} to recognize source taxation of active income and residence taxation of passive investment income. After highlighting the limited scope of most of the treaties (which apply only to income taxation) and contrasting the OECD model treaty with the UN model treaty, the author notes that US tax treaties with LDCs have often relied on provisions and concepts from the UN model treaty, which affords greater taxing jurisdiction to source countries.

The bulk of the article considers a hypothetical tax treaty between the United States and Ghana. The author concludes that such an agreement would not significantly affect the total taxes paid by current or potential investors. Her reasons for this conclusion are fivefold: (1) LDCs rely less on income taxes than on other taxes and levies that are not covered by tax treaties; (2) tax incentives in developing countries, tax deferral by residence countries, and tax avoidance and evasion have enabled multinational enterprises to minimize worldwide income taxes without needing to rely on tax treaties; (3) domestic rates on passive income paid to foreign persons are already equal to or less than the withholding tax rates that might be expected under a US tax treaty with an LDC; (4) tax considerations are less important than non-tax factors in the location decisions of multinational enterprises; and (5) perceptions of security and stability are more likely to be influenced by measures such as investment protection provisions in trade agreements than by the existence of a tax treaty.

These reasons seem plausible in the context of the author’s case study, and they support her conclusion that little private sector pressure is likely to exist for tax treaties between developed countries and LDCs. They also support the author’s conclusion that the expansion of tax treaties between developed countries and LDCs is unlikely to have much impact on trade and investment in the latter.

D.D.


The concept of “harmful tax competition” has been much debated since the OECD Committee on Fiscal Affairs released a detailed report on the subject in 1998.16 These two articles, which appear in a symposium issue of the Michigan Journal of International Law on globalization, law, and development, contribute to this ongoing discussion. Avi-Yonah, a prolific commentator on international tax issues, contends that tax competition deprives both developing countries of revenues necessary to finance human and physical infrastructure and developed countries of revenues necessary to provide essential assistance to developing countries. Emphasizing that tax competition is “a problem of coordination and trust,”17 Avi-Yonah argues that any solution to this problem requires multilateral action—at the very least by the OECD, but preferably by the World Trade Organization or the United Nations through an upgraded version of the Current Ad Hoc Group of Experts on International Cooperation in Tax Matters. In conclusion, he says: “Private market activities that span the globe can only be regulated or taxed by organizations with a similar global reach.”18

In contrast to Avi-Yonah, Littlewood is skeptical about the alleged problem of harmful tax competition, and he is highly critical of the OECD initiative—particularly to the extent that it is directed against so-called harmful preferential tax regimes in developing countries. Challenging both the presumption that tax competition is harmful and the manner in which the OECD has defined and identified tax havens and harmful preferential tax regimes, Littlewood argues that developed countries could respond to other countries’ preferential tax regimes by adopting more comprehensive controlled foreign corporation and foreign investment fund regimes. More generally, he concludes, any coordinated response to international tax competition should come from the United Nations rather than the developed countries in the OECD.

D.D.

17 At 382.
18 At 387.