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RECOVERY OF UNAUTHORIZED TAXES: A NEW CONSTITUTIONAL RIGHT

Peter W. Hogg*

I. THE LAW BEFORE KINGSTREET

Where a tax has been paid to government under a statute that is subsequently held to be unconstitutional, can the tax be recovered by the taxpayer? It seems obvious that the answer should be yes. The government's right to the tax was destroyed by the holding of unconstitutionality, and the tax should be refunded to the taxpayer. Before 2007 in Canada, neither governments nor courts embraced this simple solution. Governments usually tried to retain taxes paid under an unconstitutional statute, and taxpayers were often unsuccessful in enforcing recovery in the courts. What was the problem?

One problem was the rule of restitution law that payments made under a mistake of law were irrecoverable. That was a barrier to the recovery of unconstitutional taxes. However, that rule was repudiated by the Supreme Court of Canada in 1989,¹ and has now disappeared from the law of restitution, not only for the recovery of illegal taxes, but for restitutionary claims generally. But another problem remained. In *Air Canada v. British Columbia* (1989),² La Forest J. in the Supreme Court of Canada said that there was a special rule of public law applicable only to the recovery of unconstitutional taxes. The special rule was that unconstitutional

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1. *Canadian Pacific Airlines Ltd. v. British Columbia*, [1989] 1 S.C.R. 1133, 59 D.L.R. (4th) 218. Accord, *David Securities v. Commonwealth Bank of Australia* (1992), 175 C.L.R. 353 (H.C.A.); *Kleinwort Benson Ltd. v. Lincoln City Council*, [1999] 2 A.C. 349 (H.L.).
2. [1989] 1 S.C.R. 1161 at pp. 1204-1206, 59 D.L.R. (4th) 161.

taxes were irrecoverable. The reason for the rule was that “fiscal chaos” would otherwise result. This was an *obiter dictum*: recovery was denied in the case because a new valid retroactive tax had replaced the unconstitutional tax. And the special rule was agreed to by only two other judges. Nevertheless, as the considered view of a respected judge, it could not be disregarded, and until the *Kingstreet* decision in 2007,³ which will be the main topic of this article, the court did not repudiate the dictum, which left the state of the law in doubt.

The newly announced special rule of irrecoverability seemed to be inconsistent with the Supreme Court’s earlier decision in *Amax Potash v. Government of Saskatchewan* (1977).⁴ In that case, the court struck down a statute that purported to bar recovery by taxpayers of an unconstitutional tax. To be sure, the court did not decide that the unconstitutional tax was recoverable by the taxpayers, but the decision only made sense on the assumption that the taxes would have been recoverable at common law. Aside from this precedent, the suggested rule was criticized by commentators⁵ on the ground that the rule was opposed to fundamental constitutional principles and sound policy.

II. THE DECISION IN KINGSTREET

The criticisms of the suggested Crown immunity were fully accepted by the Supreme Court of Canada in *Kingstreet Investments v. New Brunswick* (2007).⁶ New Brunswick had for many years been levying a “user charge” on night clubs that were licensed to sell liquor. The night clubs sued the province to recover the charges they had paid, claiming that the charges were unconstitutional. The Supreme Court agreed with the plaintiffs that the charges were unconstitutional, because they were really indirect taxes.⁷ And the court rejected the argument that the plaintiffs should not recover because they had not actually borne the burden of the taxes, having passed it on as part of the price of the drinks that they sold to their customers. Passing-on, the court said, was not a defence to an action to recover unauthorized taxes.⁸

3. *Infra*, footnote 6.

4. [1977] 2 S.C.R. 576, 71 D.L.R. (3d) 1.

5. *E.g.*, P.W. Hogg, *Constitutional Law of Canada*, 4th ed., supplemented (Scarborough: Carswell, 1996) at 55.7.

6. [2007] 1 S.C.R. 3, 276 D.L.R. (4th) 342. Bastarache J. wrote the opinion of the court.

7. *Ibid.*, at para. 4.

8. *Ibid.*, at paras. 42-51. One reason given was that it is impossible to ascertain the

Those rulings made it unavoidable to decide the question whether the plaintiffs were to be defeated by La Forest J.'s suggested Crown immunity. The court did decide the question, emphatically rejecting the immunity rule, and substituting the opposite rule, namely, that unconstitutional taxes were recoverable by the taxpayers who had paid them.

Bastarache J., who wrote the opinion of the court in *Kingstreet*, proceeded from the premise that the governing constitutional principle is that the Crown may not levy a tax without legislative authority. This principle, enshrined in the Bill of Rights of 1688,⁹ 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 in order to raise taxes (and vote supply). This principle would be “undermined” if a tax could be imposed without legislative authority and then could simply be retained by the Crown.¹⁰ An analogous constitutional principle allows the Crown an absolute right to recover expenditures that have been made without legislative authority.¹¹ The spending of money and the raising of money are “two sides of the same coin.” Just as the Crown is entitled to recover unauthorized expenditures, so the Crown should be obliged to repay unauthorized taxes.¹² As for the concern that governmental finances would be disrupted by the return of unauthorized taxes, that was a problem for governments to solve, not the innocent taxpayers. Bastarache J. pointed out that a court striking down an unconstitutional tax could suspend the declaration of invalidity for a period of time to allow the government to address the fiscal problem that the decision would cause.¹³ And he noted that the problem could sometimes be solved by the enactment of a new, valid, retroactive tax, as had occurred

ultimate burden of a tax. Of course, the finding that the taxes were indirect (previous note) entailed a finding that the taxes were likely to be passed on by the taxpayers to their customers: Hogg, *supra*, footnote 5, at 31.2.

9. (U.K.), 1 Will. & Mar., c. 2, s. 4; see also *Bowles v. Bank of England*, [1913] 1 Ch. 57 (resolution of legislative committee, approved by House of Commons, but not by House of Lords and King, cannot authorize levy of tax).
10. *Kingstreet*, *supra*, footnote 6, at paras. 14-15 and 19-22, quoting from the previous edition of Hogg, *supra*, footnote 5.
11. *Auckland Harbour Bd. v. The King*, [1924] A.C. 318 at pp. 326-27 (P.C. (N.Z.)); *The King v. Toronto Terminals Ry. Co.*, [1948] Ex. C.R. 563; *R. v. Breckenridge Speedway Ltd.*, [1970] S.C.R. 175; P.W. Hogg and P.J. Monahan, *Liability of the Crown*, 3rd ed. (Scarborough: Carswell, 2000) at 10.1(c).
12. *Kingstreet*, *supra*, footnote 6, at paras. 23-24.
13. This was done in *Eurig Estate (Re)*, [1998] 2 S.C.R. 565, 165 D.L.R. (4th) 1, where the ruling that Ontario's probate fee was an unconstitutional tax was suspended for six months. The Legislature followed up by enacting a valid “estate administration tax” at the same rate as the probate fees and made it retroactive to

in the *Air Canada* case.¹⁴ (In fact, after the decision in *Kingstreet*, the New Brunswick Legislature enacted a new retroactive direct tax to enable the government to retain the money that had been unconstitutionally levied.)¹⁵

Having decided that taxes levied without valid legislative authority could be recovered, Bastarache J. went on to determine the juridical basis of the recovery. He held that, because of the constitutional principles that govern the levy of taxes, the recovery of unconstitutional taxes is “a matter of constitutional right.”¹⁶ Separate and apart from the private-law cause of action for unjust enrichment, the restitution of taxes is a “public law remedy.”¹⁷ The right of recovery depends solely “on the objective consideration of whether the tax was exacted without proper legal authority.”¹⁸ Moreover, the same right of recovery is available, not only in the case where taxes were levied under an unconstitutional statute (as in this case), but also where taxes were levied without legislative authority in the administrative-law sense.¹⁹ Both situations offend the same constitutional principle that taxes may only be levied by statute.

1950, when the invalid probate fees were introduced: Hogg, *supra*, footnote 5, at 31.8.

14. *Supra*, footnote 2. This also occurred after the *Eurig* decision, *ibid.*, and after the *Kingstreet* case itself.
15. An Act to Amend the Liquor Control Act, S.N.B. 2007, c. 23 (retroactive to March 1, 1998).
16. *Kingstreet*, *supra*, footnote 6, at para. 34. This is generally the position outside Canada: *McKesson Group v. Florida* (1990), 496 U.S. 18 (invoking due process clause of Fourteenth Amendment); *Commr. of State Revenue v. Royal Insurance Australia* (1994), 182 C.L.R. 51; *Woolwich Equitable Building Soc. v. Inland Revenue Comms.*, [1993] A.C. 70 (H.L.); and even in Quebec: *Abel Skiver Farm Corp. v. Ste-Foy*, [1983] 1 S.C.R. 403, 54 N.R. 345; *Willmor Discount Corp. v. Vaudreuil (City)*, [1994] 2 S.C.R. 210, 61 Q.A.C. 141.
17. *Ibid.*, at para. 40. It is not clear what the significance is of treating the recovery of unconstitutional taxes as a special public-law remedy, since the mistaken belief of the taxpayer or the passing on of the tax or the absence of duress would not be defences to a private claim of unjust enrichment.
18. *Ibid.*, at para. 53.
19. *Ibid.*, at paras. 54-58. These passages are not perfectly clear in that they are directed only to the issues of protest and duress. However, the constitutional principle of no taxation without legislative authority is equally violated whether the taxing law is itself invalid (as a matter of constitutional law) or whether the language of a valid statute does not authorize the levy of the tax (as a matter of administrative law). Accord, *Woolwich Equitable Building Soc. v. Inland Revenue Comms.*, *supra*, footnote 16, at p. 172, Lord Goff (applying constitutional principle to permit recovery of administrative-law *ultra vires* taxes).

III. LIMITATION PERIODS

What about limitation periods? Do they restrict the right to recover invalid taxes? It will be recalled that, in the *Amax Potash* case,²⁰ the Supreme Court had struck down a law that purported to bar recovery of an unconstitutional tax. However, in *Kingstreet*, Bastarache J. drew a distinction between a law that was enacted for the purpose of barring the recovery of an unconstitutional tax (*Amax Potash*) and a pre-existing law of general application that imposes limitation periods on causes of action. There was no reason, he said, why a general limitation statute (assuming its terms were apt to apply to the action for recovery of taxes) should not be effective to bar stale claims for recovery of taxes.²¹ In this case, New Brunswick's limitation of actions statute contained a number of specific limitation periods for particular kinds of causes of action and a residuary clause imposing a limitation period of six years on all causes of action not otherwise provided for. That residuary limitation period applied to the plaintiffs' action for recovery of the invalid taxes, and limited the claim to those taxes paid during the six years preceding the commencement of the action. Taxes that had been paid more than six years before the commencement of the action were barred from recovery by the limitation period.

IV. CONCLUSION

Kingstreet decides that taxes levied without statutory authority are recoverable by the taxpayer as a matter of constitutional right. The absence of statutory authority in the case resulted from the taxing statute being unconstitutional (constitutional *ultra vires*). However, it is clear from the reasoning that the same principle would apply to the case where the statute was constitutional but its language did not authorize the tax that was in fact levied (administrative *ultra vires*). The court insisted that the right of recovery was a public-law cause of action that was separate and apart from the private-law right of restitution for unjust enrichment. It is not clear from the reasons what (if any) practical consequences flow from the distinction. The important part of the reasoning was to sweep away La Forest J.'s suggested Crown immunity, and once that was done it seems likely that the law of unjust enrichment, now liberated from its mistake-of-law

20. *Supra*, footnote 4.

21. *Kingstreet*, *supra*, footnote 6, at paras. 59-61.

straitjacket, would also provide a right to recover unauthorized taxes.

The concern about the fiscal consequences to government remains a valid one. However, the application of general limitation periods to the cause of action for recovery will restrict the size of the claims that can be made by taxpayers. And the remedy of a new, valid, retroactive tax will often be available to nullify the liability altogether if the competent legislative body so wishes. Indeed, that was the solution adopted in New Brunswick to overcome the liability imposed by this case.