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# THE NEW ACT RESPECTING THE LEGAL PUBLICITY OF ENTERPRISES AND TRUSTS

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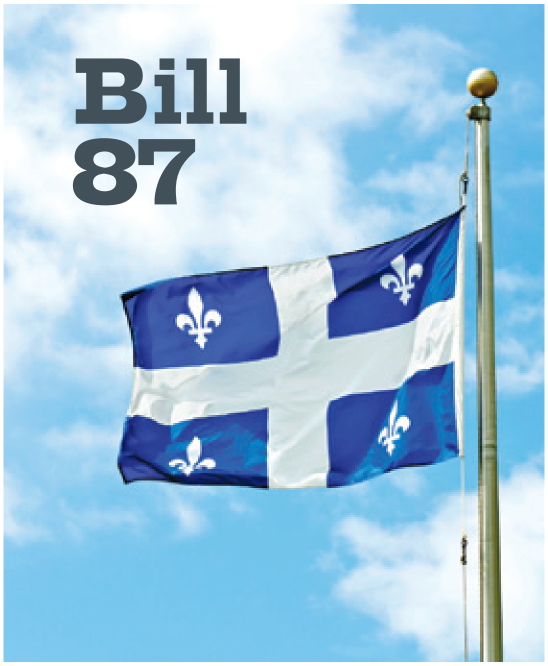
In our June 2010 issue, we discussed the broad outlines of Bill 87 enacting the new *Act respecting the legal publicity of enterprises*, which came into force at the same time as the *Business Corporations Act*, on February 14, 2011. We emphasized, at that time, the fact that Bill 87 did not require trusts to register nor did it permit them to register voluntarily, which seemed incongruous to us, given that many trusts carry on real businesses. Moreover, during the consultations concerning Bill 87, the Québec Bar and the Canadian Bar Association had made specific recommendations on this issue. Indeed, the Québec Bar recommended that the Bill be modified so as to include trusts carrying on a business in the list of registrants required to register themselves. The Canadian Bar Association suggested that the Bill be modified so as to continue to allow all trusts to register voluntarily.




However, the Minister of Revenue paid attention to those recommendations and, by means of an omnibus bill presented on November 10, 2010, accepted the Québec Bar's recommendation and modified Bill 87 so as to require trusts that operate an enterprise in Quebec to register, except for those administered by a registered registrant. However, the Minister of Revenue did not accept the Canadian Bar Association's recommendation, with the result that the *Act respecting the legal publicity of enterprises* that came into force on February 14, 2011, does not permit other kinds of trusts to register voluntarily. As regards trusts that registered voluntarily before that date, section 286 of the *Act respecting the legal publicity of enterprises* provides that they will continue to be registrants until their registrations are cancelled. ◂

# NEW FILING REQUIREMENTS FOR PARTNERSHIPS

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On September 17, 2010, the Canada Revenue Agency ("**CRA**") announced that it would be changing the rules that determine which partnerships are required to file partnership information returns for fiscal periods ending on or after January 1, 2011.

Technically, every member of a partnership that carries on business in Canada, or that is a Canadian partnership or a SIFT partnership, at any time during a fiscal period of the partnership, is required to make and file an information return (T-5013 and Relevé 15). When one partner files such a return it absolves all the other partners from doing so.

The *Income Tax Act* (Canada) provides that the Minister of National Revenue may use his discretionary power to relieve certain partnerships from their obligations to file information returns. The Minister had exercised his discretionary power so as to not require partnerships having fewer than six partners to file information returns.

As of January, 2011, the rules have been modified such that the number of partners is no longer relevant. The criteria have now become either financial, based on the amount of revenues generated by the partnership or the value of the assets and liabilities of the partnership, or based on the nature of the partnership itself.

As of January, 2011, a partnership that carries on business in Canada, or a Canadian partnership with Canadian or foreign operations or investments, is required to file an information return for each fiscal period of the partnership if:

- At the end of the fiscal period, the partnership has an absolute value of revenue plus an absolute value of expenses of more than $2,000,000, or has more than $5,000,000 in assets;
- At any time during the fiscal period, the partnership is a tiered partnership (has another partnership as a partner or is itself a partner in another partnership);
- The partnership has a corporation or a trust as a partner;
- The partnership invested in flow-through shares of a principal business corporation that incurs Canadian resource expenses and renounces those expenses in favour of the partnership; or
- The Minister of National Revenue requests that the partnership file such a return in writing.

Some partnerships that were required to file information returns may no longer be required to do so and some others that were not required to do so may continue to be relieved of that obligation. Does that mean these partnerships should not file information returns? We believe that not filing information returns would be a mistake because under subsections 152(1.3) and 152(1.7) of the *Income Tax Act* (Canada) it could be argued that prescription is never acquired by a taxpayer with respect to his portion of the income or loss arising from a partnership if an information return is not filed.

So, whether a partnership has never been required to file information returns in the past or is no longer required to do so, we believe that it would be prudent to file such returns because doing so precludes the tax authorities from assessing partnership income and losses beyond the normal reassessment period in situations where there has been no misrepresentation that is attributable to neglect, carelessness or willful default. ◄

# REQUESTS FOR PRODUCTION OF DOCUMENTS BY THE TAX AUTHORITIES

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In previous issues of RATIO, we discussed the management of tax related documents[1] and the lawyer-client privilege.[2] This article completes the series by tackling the subject of requests made by tax authorities to taxpayers for the production of documents.

Despite the very extensive powers conferred on the tax authorities concerning requests for documents, those powers are subject to two important limitations:

- The request must be made in the context of an audit or a real and serious investigation relating to the affairs of an identifiable taxpayer; and
- The documents requested must be related to such audit or investigation.

These two conditions do not offer taxpayers real possibilities to contest a request for production of documents since it is usually difficult for them to know the motives and the context of such a request. However, the limitations on the tax authorities' powers can, for example, enable a taxpayer to refuse to produce documents requested from him for statistical or other purposes not directly related to the application of one or more tax laws.

Similarly, the tax authorities generally cannot go on a "fishing expedition" in relation to unidentified taxpayers. For example, they cannot ask a stockbroker to produce documents relating to all his clients having a particular investor profile.

The tax laws do, however, provide for an exception permitting the authorities to go on such a fishing expedition to the extent that they obtain prior court authorization.

In addition, the Supreme Court of Canada has twice stated that the authorities cannot use their powers to ask a taxpayer to produce documents to the extent that the request is made in the context of an investigation having as its main purpose to establish the penal or criminal responsibility of a taxpayer. Documents obtained contrary to that principle would not be admissible as evidence in the context of a penal or criminal prosecution of the taxpayer. It may, however, be difficult to determine at what time an audit ceases to be of a fiscal nature and becomes penal or criminal.

Lastly, as discussed in a previous article, taxpayers may use procedures generally provided for in the tax laws to invoke the lawyer-client privilege and refuse to hand over certain documents to the tax authorities. Even in cases of doubt as to whether the privilege applies to certain documents, taxpayers are better off to invoke such privilege in order to make sure that their rights in the matter are determined with impartiality.

Despite the applicable limitations, there is no denying that the powers conferred on the authorities with respect to the production of documents by a taxpayer in the context of a tax audit are quite extensive. However, taxpayers have the right to know the motives for such a request as well as the context in which it is being made before complying with it, if it is necessary to do so. The tax laws and courts provide taxpayers with certain rights and it is to their advantage to assert them judiciously.

1 *Words vanish: documents must be managed properly.* Ratio, number 6, December 2009, lavery.ca/publications, select Ratio/Luc Pariseau.

2 *Speech is silver, silence is golden... what about secrecy?* Ratio, number 9, September 2009, lavery.ca/publications, select Ratio/Luc Pariseau.

# YOU'RE FIRED!: THE IMPACT ON THE EXERCISE OF STOCK OPTIONS

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By offering their employees options to purchase shares in the capital of their business, commonly referred to as "stock options", employers hope to encourage them to participate in the company's growth. When the employment relationship is threatened, employees may wish to take advantage of the favourable terms of their stock options. However, the exercise of options in the context of a dismissal merits a more detailed analysis.

The right to stock options, per se, is generally found in the employment contract, while the specific terms and conditions of this right are set out in a separate plan. When the holder of stock options wishes to exercise them, he must consult the text of the stock option plan to determine the terms and conditions for doing so. Employees are entitled to know what these terms and conditions are, so it is important for employers to systematically provide them with a copy of the provisions governing the plan, and to retain proof that they were sent to them.

The right to exercise options may vary depending upon how the dismissal is characterized. The plan may provide that the employee's options have no effect upon the termination of his employment if the employee is dismissed for serious grounds (insubordination, fraud, etc.), or simply upon termination of employment, regardless of the reason. If the plan is clear on this issue, the employee will be able to exercise his options only following the termination of his employment in accordance with the time limit set by the plan.

Where a dismissal is made "without good and sufficient cause", a line of reasoning developed in the other Canadian provinces provides that if the plan simply indicates that the right to exercise the options terminates upon dismissal, without specifying what happens in case of a dismissal without cause, the right survives for the entire period of reasonable notice to which the employee is entitled. This may therefore enable the employee to exercise his options for a longer period of time than anticipated by the employer, which could have a significant financial impact. Although this argument for extending the time period for exercising options carries little weight according to the doctrine in Quebec, one should be aware of it when drafting the provisions of the plan. A clause dealing with the time period for exercising options which does not indicate what would happen in the event of a dismissal without cause could be viewed as ambiguous and open to interpretation. A simple and effective solution to avoid this situation is to specifically provide in the plan for what will happen in the event of a dismissal, with or without cause.

It is sometimes surprising to see the problems that a request to exercise options can raise, precisely because this perk is often governed by both the employment contract and the employer's stock option plan. To avoid any confusion, it is useful to specify in the employment contract whether the text of the plan takes precedence over the contract or vice versa. Since the context of a dismissal is already a tangle just from the standpoint of human resources, the careful drafting of conditions for exercise of stock options neatly links both contracts and can spare you a lot of worry. ◄

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