

Public Beneficial Ownership Registers and Trust Beneficiaries as Beneficial Owners: Canada, the United States and Other Jurisdictions

By Daniel Frajman

As we guide our clients through new legislation relating to beneficial ownership reporting for private company shares, including as regards shareholders that are trusts, it is worthwhile to look at the apparent inconsistencies when comparing government policy at the Canadian federal and provincial levels, at the U.S. federal and state levels and in the U.K., relating to two of the major aspects of the rules: the extent of the public aspect of the reporting, and the manner in which discretionary trust beneficiaries are reported.

This can help promote an understanding of, and perhaps a change for the better, as regards this legislation aimed at increasing transparency.

Public Aspect of the Reporting

The rules for the reporting of beneficial ownership of private company shares go beyond just beneficial ownership, and generally are aimed at looking through all of the holding companies (holding companies are a common tax deferral vehicle in Canada) and trusts in the corporation's structure so as to determine and then report the identity of all physical persons who hold at least 25% of the votes or value of the corporation in question, or who control in fact – have *de facto* control – of the corporation. (For some reason, British Columbia replaces the value criterion with individuals holding 25% of the number of issued shares, which is probably misleading.)

The Canadian division of legislative powers allows corporations to be incorporated provincially or territorially, or at the federal level, and currently all of the jurisdictions (other than Alberta and the territories that have no such legislation, and Quebec, which has a different system) have this beneficial ownership legislation with regard to corporate shares, as part of each jurisdiction's business corporation legislation. In other words, for the most part, this legislation in each Canadian jurisdiction (including in Ontario since January 1, 2023) is limited to corporations incorporated in that jurisdiction.

Quebec is an exception on this latter point, as its rules on this are in Quebec's provincial and extra-provincial corporate and partnership registration legislation, *An Act respecting the legal publicity of enterprises*, with the result that any corporation or partnership (and certain other entities)

formed anywhere in the world, including in the U.S., and with activity in Quebec, would be subject to this reporting on the Quebec register, known as the Enterprise Register, in effect currently making the Quebec register what can perhaps be called Canada's *de facto* national public register for beneficial ownership of corporations and partnerships, including as regards their trust shareholders and unit holders.

Some find it interesting to track the terminology used to describe the physical persons with the requisite ownership or control that must be named on these registers in the various jurisdictions (the physical persons are known as individuals with significant control in Canada federally and in the provinces with legislation other than Quebec and British Columbia, ultimate beneficiaries in Quebec, significant individuals in British Columbia, beneficial owners in the U.S., persons with significant control in the U.K. and ultimate beneficial owners in France, Germany and other EU jurisdictions). The more important issue is whether the establishment of the identity of such true owners and controllers is reported in a publicly accessible register (rather than retaining significant confidentiality by being maintained in the corporation's own records or being submitted to governmental authority subject to restricted access).

In trying to determine whether a North American jurisdiction will require public access, an argument can be made that one looks to the public policy rationale for the register, and that those jurisdictions aiming to use the registers to combat public ills such as tax evasion, abusive tax avoidance, money laundering and terrorist financing, tend to not record this information publicly, with availability of the information to tax, law enforcement and other governmental authorities being seen as sufficient. This is the case when looking at policy statements published by the Canadian government and by most of the provinces going back to a commitment that the federal government published in December 2017.

Another example of this is the following statement made in September 2022 by FinCEN, a division of the U.S. Treasury Department, indicating that the U.S. federal rules under the Corporate Transparency Act (CTA) regarding beneficial ownership would, "enhance US national security by making it more difficult for criminals to exploit

opaque legal structures to launder money[...]and commit serious tax fraud and other crimes.” Not surprisingly in my view, Canadian jurisdictions with legislation on this matter (other than Quebec), and the U.S. federally, currently have legislation that does not publicly register the collected information.

The Quebec rules, in contrast, establish a public register that is freely accessible on the internet (which, for example, can be accessed by searching on the internet the term “Quebec corporate search”). In this regard, it is not surprising, in my view, that the Quebec government has added an additional goal for this legislation beyond combatting tax evasion and the other abovementioned public ills, namely combatting fraud generally among contractual counterparties, so as level the economic playing field by allowing parties to know better who they are dealing with in private transactions, and additionally to allow members of the public accessing the public register to take on a whistle-blower function by reporting perceived falsely declared information.

In a 2019 public consultation on corporate transparency, the Quebec government wrote, “In the fight against *fraud*, tax evasion, tax avoidance, money laundering and the financing of criminal activities[...]the government is examining[...]approaches[...]aimed at improving transparency” [emphasis added].

In further support of this view, to the effect that public beneficial ownership registers arise when there is a desire to create a better private business environment generally, is a statement by the Canadian federal government in March 2023 when it tabled Bill C-42, which provides for amendments to our federal internal registers for individuals with significant control, to make that register a public one (as early as the end of 2023, although the bill appears unlikely to be enacted and to go into effect as early as that), and offers to the provinces and territories, for the similar internal registers for their own provincial and territorial corporations, the ability to individually join a new federal public register that would be scalable. In tabling this bill, the federal government stated that the goal of the proposed public register would be to combat tax evasion and the other public ills, and would also be aimed at, “making sure Canada is an attractive place to conduct business,” and would be meant to “ensure a well-functioning marketplace.”

Similarly, press reports from the time, when the U.K. opened the first publicly available corporate beneficial ownership register in 2016, indicated that one of the goals of the then U.K. government of David Cameron was to also increase the ability of persons to know the identity of their counterparties. (The U.K., which is no longer part of the EU, continues to have a public register, notwithstand-

ing that most EU nations, currently at least, have reversed the public nature of their corporate beneficial ownership registers in response to the November 2022 decision of the European Court of Justice in the case of *WM and Sovim SA v. Luxembourg Business Registers*, to the effect that under the Charter of Fundamental Rights of the European Union, Luxembourg’s public register was a disproportionate interference with privacy rights.)

There is at least one example in the Canadian context where a potential public corporate beneficial ownership register likely will be put into place without a stated government goal to combat fraud and/or to promote commerce generally. This is in British Columbia, where the Business Corporations Act, 2023 enacted in May 2023 calls for the internal BC transparency register relating to corporate beneficial ownership and control to become a public register by 2025. The stated purpose of the BC government with regard to this potential change is to combat “money laundering or other criminal purposes.”

It should be noted that there are two examples of state-level initiatives in the U.S. regarding what can perhaps be seen as private-party contractual concerns being included in the reasoning for public beneficial ownership registers. This is in New York, where the New York State Senate and Assembly have approved the LLC Transparency Act (not yet signed into law by the governor, as of late September 2023), which would require public disclosure of beneficial owners (using the U.S. federal CTA’s definition of beneficial owners) of limited liability companies formed or qualified to do business in New York. This is also in California where a bill (SB 594) (Durazo) would require corporations, LLCs and real estate investment trusts to publicly report information about beneficial owners.

Regarding these initiatives in New York and California, lawmakers have referred to a desire to reduce abuse by residential landlords through public disclosure of their beneficial ownership.

Therefore, as referred to above, there seems to be a fair amount of consistency among the public policy considerations of various governments when deciding whether to create a public register for the reporting of beneficial owners and controllers of private corporations including as regards their trust shareholders. Such consistency should promote certainty and an easier discussion as to potential changes in the rules going forward.

Discretionary Trust Beneficiaries in the Reporting

We now turn to how these registers treat discretionary trust beneficiaries when the trust is a beneficial owner or controller of the private corporation in question, typically arising when the trust in question meets the above-mentioned test of holding on a look-through basis at least 25% of the votes or value of the corporation in question. On this issue, it will be seen, there apparently is less consistency as between jurisdictions, and essentially no discussion of underlying policy, as compared to the above-mentioned issue as to whether the register should be a public one. This is not positive as it creates, for the question of how to treat discretionary trust beneficiaries, uncertainty in interpreting the rules.

Discretionary trusts, when they hold shares in private corporations, usually become shareholders for estate planning and tax purposes, such as in Canada capital gains tax reduction in various circumstances. The trust is discretionary in that the trustees have the discretion to decide who among a list of potential beneficiaries will in fact receive at any time and from time to time a distribution of income or capital from the trust.

If, for example, a trust meets the above-mentioned 25% criterion, generally most jurisdictions, in their beneficial ownership transparency legislation, will require that the trustees be reported as beneficial owners or controllers.

As regards individuals who are the discretionary beneficiaries of such trusts, when are they named as beneficial owners or controllers on the beneficial ownership registers? The question is important because the number of potential discretionary beneficiaries of a trust can be very large and

subject to contingencies, making a list hard to assemble, and the potential penalties for non-compliant reporting are prohibitive. (For example, the Canadian federal rules refer to fines of up to \$CAN200,000 in some circumstances; the U.S. federal rules refer to potential fines of \$500 per day for non-compliance; the Quebec rules refer to the potential striking off of the corporation from the register, which is very disruptive; and in the case of registers that are publicly accessible on the internet, such as Quebec's, incorrect reporting can mislead third parties and potentially can be embarrassing.) Here is how some jurisdictions deal with the question, and in most cases with little or no discussion as to the reason why:

- Under the Canadian federal rules (with most provinces – other than Quebec and BC, which are referred to below, and other than Alberta, which has not legislated in this area – having a similar rule under their own provincial corporations act), which are in the Canada Business Corporations Act, “beneficial owners” with a sufficient (example, 25%) interest are reported as individuals with significant control. This is generally felt to include trust beneficiaries with a fixed (non-discretionary) interest, and to not include discretionary beneficiaries.
- Under the Quebec rules (as mentioned, Quebec has North America's only public register) found in An Act Respecting The Legal Publicity of Enterprises, the statute refers to the term “beneficiary,” without defining the term. In late March 2023, Quebec issued an administrative position apparently indicating that only discretionary beneficiaries who have at some point received a distribution from the trust of income or capital would be named as ultimate



beneficiaries. On a separate but related point, a specific rule in the statute appears to say that for all testamentary trusts, trust beneficiaries are exempt from being ultimate beneficiaries;

- In British Columbia, the Business Corporations Act refers to “beneficial owners,” and the B.C. government has taken the administrative position that as long as the trust is a direct owner of the requisite number of shares in the corporation in question, then all of the discretionary beneficiaries are significant individuals.
- In the U.S., the federal CTA, set to apply as of January 1, 2024, as interpreted by the U.S. Treasury Department’s “final rule” regulations of September 2022, indicates that a trust beneficiary is a beneficial owner if the beneficiary is the sole permissible recipient of income and principal from the trust, or if the beneficiary has the right to demand a distribution of substantially all of the assets of the trust. This appears somewhat limiting; however, at least some legal writers have said that from a conservative point of view, all beneficiaries should be named as beneficial owners;
- In the U.K., the Companies Act 2006 requires the trust beneficiary to hold the right to exercise, or to actually exercise, significant influence or control over the activities of the trust, to be a person with significant control.
- Other analogous laws in Canada dealing with transparency are not helpful on this point, as these other laws also do not deal consistently with the discretionary trust beneficiary, and do not provide material reasoning for the government’s position. For example, beginning with income tax filings for express trusts due in 2024 under the Income Tax Act (Canada) and the Taxation Act (Quebec), all “beneficiaries” must be listed in the trust’s annual tax return. With regard to this, it appears that all beneficiaries must be listed, whether or not they are contingent, and whether they are fixed or discretionary, based on explanatory or administrative statements made by Canada and Quebec. The Canada Revenue Agency indicated this again as late as in June 2023 at the CRA-STEP Canada Roundtable, when the CRA stated that in the context of these Income Tax Act trust tax return rules, very generally a beneficiary of a trust is a person who has the right to compel the trustee to properly enforce the terms of the trust, regardless of whether that person’s right to the income or capital of the trust is immediate, future, contingent, absolute or

conditional on the exercise of the discretion of any person.

- In another example of analogous Canadian laws looking at reporting requirements for discretionary beneficiaries, and very briefly stated, is the anti-money laundering (AML) legislation in Canada, such as the proceeds of crime legislation that requires customer due diligence by, for example, financial institutions; the Canada-U.S. agreement regarding foreign account tax compliance for Canadian accounts of U.S. persons (FATCA); and the common reporting standard (CRS) under the Income Tax Act (Canada) that refers to foreign account tax compliance for persons with a Canadian account but who have a tax residence elsewhere other than the U.S. For all of this legislation, it appears that a trust beneficiary is named if the beneficiary has actually received a trust distribution in the year in question. This is apparently referred to in the CRA’s guide of March 2022 on the Canada-U.S. Enhanced Tax Information Exchange Agreement.

In this brief review of the status of the discretionary trust beneficiary under beneficial ownership transparency legislation, it can be seen that there is significant inconsistency as between jurisdictions, and little discussion of underlying policy. This creates uncertainty in interpreting the rules, uncertainty as to whether interpretations will change in the future, and perceptions that the rules are sometimes arbitrary.

A lesson can be taken here from the policy statements made by governments on the question of whether the beneficial ownership registers should be made public, where the more robust policy discussion reduces uncertainty in interpretation, and likely increases the ability to comply with the rules.

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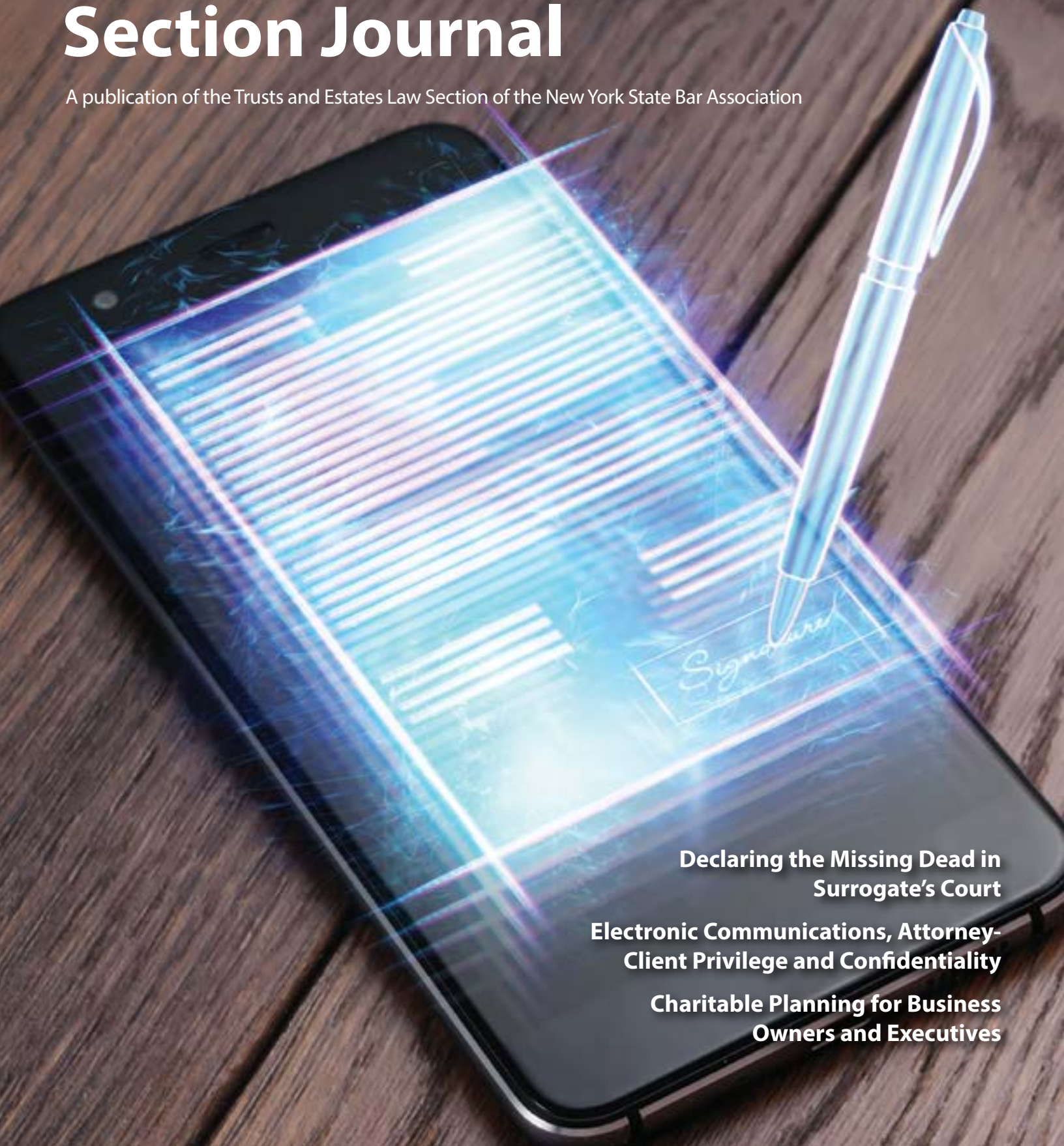
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**Declaring the Missing Dead in
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**Electronic Communications, Attorney-
Client Privilege and Confidentiality**

**Charitable Planning for Business
Owners and Executives**

Message From the Editor-in-Chief

By Avigail Goldglancz

This volume contains articles on issues pertinent to the estate planner, litigator and administration attorney alike. Diane Matero's article focuses on the process of declaring the missing dead; Frank T. Santoro addresses the need to preserve the attorney-client privilege with electronic communications; Kevin Matz discusses the recent court decision *Connelly v. United States*; Daniel Frajman provides a thorough analysis of the beneficial ownership reporting for private company shares, and Gary E. Bashian and Andrew Frisenda detail what is required in order to secure a dismissal of an undue influence objection upon summary judgment.

Additionally, the Charitable Planning Committee has contributed a three-part series examining charitable gifts with assets beyond simple cash and marketable securities. Part II authored by Julia Chu concentrates on adding pre-liquidity charitable options into planning considerations.

Many thanks to those who have contributed to this volume and to the wonderful editors who worked diligently on each volume this year.

We continue to urge Section members to participate in our publication. Our next deadline for submissions is January 8, 2024 for publication in the spring issue. Please consider submitting an article or column for publication in the Journal. CLE credits may be obtained.

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