



**Submission of the
Federation of Law Societies of Canada
to the
Department of Finance**

Draft Income Tax Legislative Proposals

Ottawa, October 19, 2018

Introduction

1. The Federation of Law Societies of Canada (“the Federation”), on behalf of its member law societies, appreciates the opportunity to provide comments in response to the public consultation on draft income tax legislative proposals.
2. The Federation is the coordinating body of the 14 governing bodies of the legal profession in Canada. Our member law societies are statutorily charged by legislation in each province and territory with the responsibility for regulating more than 120,000 lawyers, 3,800 notaries in Quebec and Ontario’s nearly 9,000 licensed paralegals in the public interest. An important role of the Federation is to express the views of the governing bodies of the legal profession on national and international issues relating to the administration of justice and the rule of law. This has resulted in the Federation developing an established history of advocating for robust protection of solicitor-client privilege.

Proposed Reporting on Lawyers’ Trust Accounts

3. The Federation is concerned about the new reporting requirements for trusts contemplated in the proposed legislative changes to the *Income Tax Act*. Specifically, the Federation is of the view that the proposed amendment would require members of the legal profession to report on trust accounts maintained separately for a particular client or clients, thus infringing on solicitor-client privilege.
4. The proposed legislative amendments would require a trust that is resident in Canada, and that is an express trust (or for civil law purposes a trust other than a trust that is established by law or by judgment) to file a tax return notwithstanding that it may meet one of the exceptions to filing a return already listed in subsection 150(1.1) of the existing *Income Tax Act*.¹
5. The proposed legislative amendments list exceptions to the new trust reporting requirements. Key amongst them is an exception for “trusts that are required under the relevant rules of professional conduct or the laws of Canada or a province to hold funds for the purposes of the activity that is regulated under those rules or laws.”² However, this exception also specifies that such trusts are only exempted from reporting requirements “provided the trust is not maintained as a separate trust for a particular client or clients (this provides an exception for legal counsel’s general trust account, but not for specific client accounts).”
6. It is not clear whom is intended to report to the Canada Revenue Agency, but we interpret the proposed legislation to require reporting from lawyers and notaries when they are in control of separate trust accounts on behalf of their clients. If the proposed amendments become law, lawyers and notaries will be obligated to file tax returns containing the names, addresses, and likely other identifying information of the clients

¹ Minister of Finance, Explanatory Notes Relating to the Legislative Proposals Relating to Income Tax and Other Legislation, July 2018 at “Reporting Requirements for Trusts,” paragraph 150(1.1), online:

<https://www.fin.gc.ca/drleg-apl/2018/ita-lir-0718-n-eng.asp>

² *Ibid* at para. 150(2).

for whom they hold money in a separate trust account. This is a clear breach of solicitor-client privilege as it requires legal professionals to report identifying information about their clients to the Canada Revenue Agency.

The Law on Solicitor-Client Privilege in Canada

7. The Supreme Court has held on a number of occasions that solicitor-client privilege is essential to the proper administration of justice and must be as near absolute as possible. The Federation has successfully acted as intervenor before the Supreme Court in its most authoritative cases on the sanctity of solicitor-client privileged materials.³
8. The Supreme Court has emphasized that the compelled disclosure of solicitor-client privileged documents or information constitutes an infringement of the confidentiality between legal counsel and their clients, and such disclosure is all the more serious where there is a possibility of the privileged information being made public or used against the person entitled to the privilege.⁴ The Supreme Court's jurisprudence also establishes that the near-absolute character of solicitor-client privilege means any incursions must minimally impair the right and be justified on the basis of absolute necessity.⁵
9. Solicitor-client privilege encompasses information exchanged for the purpose of giving or receiving legal advice – and this includes basic personal information about clients. It is the Federation's position that the proposed reporting requirements are in direct conflict with the Supreme Court of Canada's recent decision in *Chambre des Notaires*.⁶ At issue in *Chambre des Notaires* was whether the Canada Revenue Agency had the ability to compel information or documents relating to clients of notaries practicing law in Quebec. The Canada Revenue Agency justified their requests under a provision of the *Income Tax Act* that defined solicitor-client privilege as all communications between lawyers and their clients in professional confidence save for the accounting records of lawyers.
10. In a unanimous decision, the Supreme Court held that information protected by professional secrecy "cannot be disclosed by a notary or a lawyer in any regulatory context."⁷ The Supreme Court further held that solicitor-client privilege belongs to the client, and can only be waived by a client; a reporting obligation that is placed solely on legal professionals, under threat of prosecution, puts the lawyer in an "intolerable" situation.⁸ Finally, the Supreme Court affirmed that accounting records are inherently capable of containing information that is protected by professional secrecy. In describing the various types of information contained in accounting records, the Court wrote:

³ See, i.e., *Canada (Privacy Commissioner) v. Blood Tribe Department ("Blood Tribe")*, 2008 SCC 44 (CanLII); *Alberta (Information and Privacy Commissioner) v. University of Calgary ("University of Calgary")*, 206 SCC 53; *Canada (Attorney General) v. Chambre des Notaires ("Chambre des Notaires")*, [2016] 1 S.C.R. 336.

⁴ *Blood Tribe* at paras. 21-22.

⁵ *University of Calgary* at para. 68.

⁶ *Supra* note 3.

⁷ *Ibid* at para. 32

⁸ *Ibid* at paras. 45 and 56.



“...Client’s names may appear in accounting records... In some cases, those names may be privileged, since the fact that a person has consulted a notary or a lawyer may reveal other confidential information about the person’s personal life or legal problems.”⁹

11. *Chambre des Notaires* is unambiguous: any compelled disclosure of information that identifies a lawyer’s client, even if just by name, breaches that client’s right to solicitor-client privilege. Further, the statutory aim behind the Canada Revenue Agency’s regulatory scheme is not sufficient to diminish a client’s expectation of privacy in their confidential relationship with their lawyer or notary. In the view of the Federation, the proposed legislative amendments are clearly inconsistent with the Supreme Court of Canada’s authoritative case law on solicitor-client privilege.

Existing Regulatory Restrictions on Lawyers’ Trust Accounts

12. In holding clients’ funds in trust accounts, lawyers and notaries are heavily regulated. They are subject to comprehensive rules of professional conduct imposed and enforced by Canada’s law societies that prohibit them from engaging in or facilitating unlawful conduct in any way. They are also subject to comprehensive financial and accounting regulations.
13. Law societies take their mandate to regulate the legal profession in the public interest seriously. Measures to ensure that legal professionals maintain appropriate practice management systems and comply with law society regulations include annual reporting obligations, practice reviews and financial audits. Law societies also have extensive investigatory and disciplinary powers that include the ability to impose penalties up to and including disbarment when members fail to abide by law society rules and regulations. Lawyers and notaries who wittingly participate in criminal activity are also subject to criminal charges and sanctions.
14. To ensure that regulation of the flow of money through a legal professional’s practice is as robust and effective as possible, the Federation is in the final stages of a comprehensive review of its anti-money laundering rules. Most notable is a proposed requirement for legal counsel tying the use of trust accounts to the provision of legal services, thus ensuring that lawyers’ and notaries’ trust accounts cannot be used for purely financial transactions.
15. A comparable rule is already in place in a number of jurisdictions, including Ontario and Quebec, which between them regulate approximately 75% of the lawyers in Canada. Adoption and implementation by all law societies across Canada of these new and revised anti-money laundering rules is anticipated by the end of this year. Once adopted, law societies across Canada will uniformly enforce the professional requirement that lawyers and notaries use their trust accounts for the exclusive purpose of providing legal services.

⁹ *Ibid* at para. 74.

16. While the specific legislative intent of the proposed amendments is not clear, we note that Budget 2018 referenced increased reporting requirements to “effectively counter aggressive tax avoidance, tax evasion, money laundering, and other criminal activities.” It is the position of the Federation that, given the extensive regulatory regime described above, and the forthcoming changes to trust accounting rules, there is no evidence that the proposed changes, at least as applied to trust accounts held by legal counsel, meet the test of absolute necessity prescribed by the Supreme Court of Canada.

Conclusion

17. In view of the questionable constitutionality of the proposed legislative amendments, and in light of the considerable oversight exercised over lawyers’ and notaries’ trust accounts, the Federation suggests that all professional trust accounts, including those maintained for specific clients, should be exempted from reporting requirements.
18. We would welcome the opportunity to discuss these matters further and to otherwise assist the Department of Finance in its review of the *Income Tax Act*.

