THE CANADIAN BAR ASSOCIATION
L'ASSOCIATION DU BARREAU CANADIEN

Office of the President
Cabinet du président

November 22, 2022

Via email: nffn@sen.parl.gc.ca

The Honourable Percy Mockler
Chair, Standing Senate Committee on National Finance
Senate of Canada
Ottawa, ON K1A 0A4

Mr. Senator Mockler:

Re: Bill C-32, *Fall Economic Statement Implementation Act* – Proposed Income Tax Amendments Compromise Solicitor-Client Privilege

On behalf of the Canadian Bar Association, I am writing to express our serious concerns about proposed amendments to the *Income Tax Act* (ITA) in Bill C-32, *Fall Economic Statement Implementation Act* that compromise solicitor-client privilege. We would appreciate an opportunity to appear before the Senate Committee on National Finance to discuss our recommendation.

The Canadian Bar Association (CBA) is a national association of over 37,000 lawyers, Québec notaries, law students and law professors. The CBA is the voice of the legal profession and is dedicated to supporting the rule of law and improving the administration of justice in Canada, which includes an independent Bar and respect for solicitor-client privilege.

It is important to state at the outset that we support the objectives of the proposed ITA amendments, namely to effectively counter aggressive tax avoidance, money laundering and other criminal activities. However, changes are required to clarify certain provisions to achieve these objectives and uphold the fundamental principle of solicitor-client privilege.

The CBA has detailed our concerns in previous submissions.[1] These concerns, as well as our recommendations, are summarized below. In short, we believe that the amendments would not withstand constitutional scrutiny, given the jurisprudence from the Supreme Court of Canada.

1 See September 10, 2018 letter to Finance Canada from Joint Committee on Taxation of the Canadian Bar Association and the Chartered Professional Accountants of Canada, explaining why proposed reporting obligations for trusts in the July 2018 draft legislation compromise solicitor-client privilege.

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Importance of Solicitor-Client Privilege

Solicitor-client privilege is a quasi-constitutional right that has been repeatedly affirmed by the Supreme Court of Canada as fundamental to the rule of law, access to justice and the proper administration of justice.

This principle allows clients from all walks of life to communicate freely and in confidence with their lawyers, in a trusted environment, in order to receive the best legal advice possible. Protecting full and frank communication between lawyers and their clients promotes the public interest in the observance of law, and respect for the administration of justice.

New Reporting Obligations for Trust Accounts Compromise Solicitor-Client Privilege

The proposed new rules in Bill C-32, *Fall Economic Statement Implementation Act*, impose new reporting obligations on a broad group of trusts.[2] These trusts would be required to file annual tax returns to report the identity of all trustees, beneficiaries and settlors of the trust, and each person with the ability to exert control over trustee decisions.

Bill C-32 recognizes the importance of solicitor-client privilege and exempts "lawyers' general trust accounts." However, "client-specific trust accounts" are not exempted. As explained below, the absence of a bright-line exemption for client-specific trust accounts is problematic.

The proposed legislation also contains a limited exception for disclosure of information that is subject to solicitor-client privilege. However, this exception (which is ambiguous in scope) is inadequate, impractical and risks placing lawyers in a conflict of interest with their clients.

In some circumstances, the proposed legislation would require a lawyer to disclose, among other things, the name of the client and the amount received from that client. This disclosure would violate the client's reasonable expectation of confidentiality in connection with their dealings with lawyers.

The proposed legislation may also place lawyers and their clients in a conflict of interest. The lawyer's obligation to file a return may conflict with the duty of confidentiality owed to the client, as well as make it difficult to give unbiased advice on the scope of the client's privilege.

In a tax context, the Supreme Court of Canada has strongly criticized attempts to impose penal sanction for non-disclosure of information that places legal advisors in a conflict with their clients (see *Canada (Attorney General) v. Chambre des notaires du Quebec*, 2016 SCC 30 at para 56).

In addition to solicitor-client privilege and conflict of interest concerns, the proposed reporting obligations for client-specific trusts would impose unreasonable and costly reporting burdens on lawyers, with limited benefit to the CRA.

We anticipate that compliance with the proposed legislation will be especially problematic for real estate lawyers. For example, it is common for deposits to be received from hundreds of unit purchasers for a single condominium development. Since provincial legislation requires that lawyer trust accounts be maintained for those deposits, Bill C-32 could require law firms to file tens of thousands of returns per year on account of condo projects alone. This would be financially and administratively onerous and impractical, both for law firms and the CRA. It could ultimately result in higher purchase prices (counter to the government's objective of increasing affordable housing) because of higher costs related to the reporting obligation, with limited benefit to the CRA.

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[2] The Government first announced its intention to impose new filing and reporting obligations for certain trusts in the 2018 federal budget. Draft legislation was released in July 2018, February 2022 and August 2022. Bill C-32 was introduced in the House of Commons on November 4, 2022.

Existing Restrictions on Lawyers' Trust Accounts

Lawyers and notaries are already heavily regulated when holding clients' funds in trust accounts. 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.

Measures to ensure that lawyers 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.

The prospect of lawyers' trust accounts being used in a manner that frustrates the CRA's ability to administer the ITA is extremely remote. Any income earned on amounts held in lawyers' trust accounts is generally subject to T5 reporting, so the CRA is already aware of income earned.

An exception for all lawyers' trust accounts would not impair the CRA's ability to enforce the ITA, and an exception is appropriate in view of the constitutional importance of protecting solicitor-client privilege.

Recommendation:

Amend proposed subsection 150(1.2)(c) to specifically exempt from the filing obligation any trust account maintained by a lawyer or notary in accordance with the rules of professional conduct governing them (which includes trust accounts maintained for particular clients).

Trusts Held by Registered Charities

Proposed subsection 150(1.2)(d) would exempt a trust that is a "registered charity". It is not clear if the new trust reporting rules apply to restricted charitable purpose trusts that are held internally by registered charities, such as endowed funds, building funds or scholarship funds (restricted funds). We wonder if these restricted funds are exempt from separate reporting requirements.

Income and assets from restricted funds are reported to the CRA through a charity's T3010 filing. It is our understanding that the CRA does not currently require separate filings for these funds within a registered charity that are not registered themselves.

If the proposed reporting obligations applied to these restricted charitable purpose trusts, unreasonable and unnecessary reporting burdens would be imposed on charities, most notably on community and public foundations with donor-advised funds and universities with specific scholarship endowment funds. This reporting requires significant additional administrative and accounting work and related financial costs to be borne by charities, without corresponding benefit to the CRA.

Closing comments

We understand and appreciate that authorities require sufficient information to determine taxpayers' tax liabilities to effectively counter aggressive tax avoidance, tax evasion, money laundering and other criminal activities. However, these measures must be balanced with 1) respect for solicitor-client privilege, and 2) allowing lawyers to fulfill their duties to their clients free from any conflict of interest.

The confidentiality of the solicitor-client relationship is essential to the functioning of the justice system and access to justice, as the Supreme Court of Canada reiterated in *Canada (Privacy Commissioner) v. Blood Tribe Department of Health*, [2008] 2 SCR 574:

> Solicitor-client privilege is fundamental to the proper functioning of our legal system. […] Experience shows that people who have a legal problem will often not make a clean breast of the facts to a lawyer without an assurance of confidentiality 'as close to absolute as possible' […]. It is in the public interest that this free flow of legal advice be encouraged. Without it, access to justice and the quality of justice in this country would be severely compromised.

The requirements to disclose information in Bill C-32 are substantially the same as the government's previous attempt to subject lawyers to the FINTRAC regime. In *Canada (Attorney General) v. Federation of Law Societies of Canada*,[3] the Supreme Court of Canada clearly said that was not allowed.

In that case, the Supreme Court of Canada recognized as a principle of fundamental justice that the state cannot impose duties on lawyers that undermine their duty of commitment to their client's cause. The duty is fundamental to the solicitor-client relationship and how the state and the citizen interact in legal matters. The legal professional's duty of commitment to the client's cause is essential to maintaining confidence in the integrity of the administration of justice.

Subject to justification, the state cannot impose obligations on lawyers that undermine their compliance with the duty, either in fact or in the perception of a reasonable person. The proposed legislative changes threaten this bedrock principle.

Lawyers' and notaries' use of trust accounts is already heavily regulated and subject to comprehensive rules of professional conduct imposed and enforced by Canada's law societies. The government should not subject the legal profession to a second regime – especially given the Supreme Court of Canada decision in *Federation of Law Societies of Canada.*

Lawyers' general trust accounts and "client-specific" trust accounts should be treated in the same manner. Not exempting client-specific trust accounts from the filing obligation fails to respect solicitor-client privilege and raises fundamental legal and constitutional issues. Based on the principles in *Chambre des notaires*, it follows that any legislation that could abrogate privilege in this manner would be struck down by a court.

Solicitor-client privilege is a quasi-constitutional right and is fundamental to the rule of law and the proper administration of justice. It will be vigorously defended by the legal profession and the broader justice system stakeholders.

We would appreciate an opportunity to appear before your committee to discuss these important issues and our recommendations.

Yours truly,

(original letter signed by Steeves Bujold)

Steeves Bujold, he/him-il/lui

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[3] [2015] 1 SCR 401