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THE AMENDED ALBERTA BUSINESS CORPORATIONS ACT – MORE THAN JUST A FRESH COAT OF PAINT

On May 17, 2005, the *Business Corporations Amendment Act, 2005* was proclaimed and became law, enacting sweeping amendments to the *Business Corporations Act* (Alberta) (“ABCA”). Although a variety of important changes are included in the package of amendments, of principal interest to most will be the changes to the way Alberta corporations issue their capital stock and the rules governing ownership of that stock, the changes to the level of financial disclosure and reporting requirements, and the introduction of a “made in Alberta” alternative to the unlimited liability company (“ULC”) otherwise only available in Canada under the *Companies Act* (Nova Scotia) (“NSCA”) (*i.e.*, the NSULC).

Treatment of Capital Stock

- **Series of Shares** – Prior to the amendments, a corporation was unable to issue shares in series without the directors first fixing the number and attributes of those shares and then obtaining articles of amendment designating the series. As amended, the ABCA allows a corporation to provide for a series of shares in its articles and fix both the number and attributes at that time, in which case there is no need to obtain articles of amendment. Alternatively the corporation may leave the details up to the directors, in which case the previous rules will apply and articles of amendment will be necessary.
- **Corporate “Incest”** – Prior to the amendments, a subsidiary corporation was not permitted to hold shares in itself, or acquire and hold more than 1% of the issued shares of each class of shares of its “holding body corporate”. In general terms, a holding body corporate is a corporation that owns enough shares to control the subsidiary either directly or together with other corporations that it controls. This rule is subject to a very narrow exception where the subsidiary corporation previously was incorporated under another statute that permitted the incestuous ownership or where the subsidiary corporation owned shares of the parent before it was acquired by the parent. In that case, the subsidiary is required to sell or otherwise dispose of those shares within five years after it was continued or acquired. Under the amended ABCA, a subsidiary corporation is permitted, from time to time, to hold shares in itself or its parent corporation, without restriction, for a maximum of 30 days, thus significantly expanding upon the exceptions to the corporate incest rules.

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- Stock Dividends - Under the prior rules, if a corporation paid a stock dividend it was required to add to the stated capital account of that class an amount equal to the declared amount of the dividend stated as an amount of money. As a result, there has been serious debate in this province (among others) concerning whether a corporation was permitted to issue “high – low” stock dividends (*i.e.*, shares having a high fair market value and low stated capital).

The amended ABCA now allows the directors of a corporation to add all, or part, of the value of those shares to the stated capital account maintained or to be maintained for the shares of the class or series issued in payment of the dividend. Again, this is a welcome change for the tax planning community.

- Payment for Shares - The ABCA contains the standard restriction that no share shall be issued until the consideration therefor is fully paid in money or in property or past service that is not less in value than the fair equivalent of the money that the corporation would have received if the share had been issued for money. For this purpose, “property” previously excluded a promissory note or promise to pay by the person acquiring the share.

Under the amendments, “property” for this purpose is amended to also exclude promissory notes or promises to pay given by a person “buying” a share or a person who does not deal at “arm’s length” with a person “buying” a share, within the meaning of that expression in the *Income Tax Act* (Canada). This is one of the few “tightening” amendments to the ABCA, and brings the ABCA in line with parallel provisions of many other business corporations statutes in Canada.

Financial Disclosure and Reporting Requirements

- Waiver of Financial Statements – The mandatory, annual preparation of financial statements has long been an irritant to small, private corporations, the only shareholder of which likely is intimately aware of the financial situation of the corporation. Complete relief from this requirement is provided in the amended ABCA in that the shareholders may at any time, by unanimous resolution, waive their right to receive financial statements. This is a change even from previous versions of Bill 16, which provided only limited relief from the production of financial statements for the first incomplete fiscal period of the corporation.
- Replacement of Auditors – Presumably in response to the Enron scandal, the ABCA has been amended to require financial statements to contain the auditors’ comments in various circumstances. In the case of a proposed replacement of an auditor, whether through removal or at the end of the auditor’s term, a corporation now is required to make a statement of the reasons for the proposed replacement. In addition, the proposed replacement auditor may make a statement in which he or she comments on the reasons referred to by the corporation for the replacement.

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The new rules are in addition to the current legislation that already permits the auditor being replaced to make a statement, and which compels the corporation to deliver the statement to its shareholders.

- Whistle Blower Legislation – The amendments to the ABCA now expressly protect a person from civil liability when that person, in good faith, makes an oral or written communication to an auditor as a result of a demand for that information by that auditor. It does not appear to protect, however, a person who volunteers information to an auditor where no demand has been made.

Residence of Directors

The ABCA previously required at least half of the directors of a corporation to be “resident Canadians”, as that expression is defined in the ABCA. The amendments to the ABCA, however, reduce this requirement to one quarter. For those directors wanting to avoid the cold Alberta winters (or summers for that matter), Alberta corporations generally are permitted to hold directors’ meetings anywhere in the world or, as expressly provided under the amendments, entirely by electronic means.

Unlimited Liability Corporations

By way of background, a ULC may be treated as a disregarded entity or partnership for U.S. federal income tax purposes, while retaining status as a corporation for Canadian income tax purposes. Amongst a host of other situations, a ULC could be beneficial where it is anticipated that losses will be realized (*e.g.*, start-up losses) or to facilitate claims for U.S. foreign tax credits for Canadian taxes paid.

Characteristics of an Alberta ULC

Alberta ULCs generally are subject to the same rules in the ABCA as all corporations governed by that statute, including, for example, those relating to amalgamations (including vertical and horizontal short-form amalgamations).

The fundamental characteristic of a ULC is that the shareholders are subject to unlimited liability. The Alberta legislation provides that the liability of each of the shareholders of an Alberta ULC, for any liability, act or default of the ULC, is unlimited in extent, and joint and several in nature. The legislation also provides that any shareholder, including a past shareholder, may be held responsible for the full amount of any claim against the ULC that originated before dissolution, regardless of the amount, if any, received by the shareholder on the distribution of the ULC’s property at dissolution. There is a risk that a creditor of an Alberta ULC could sue its shareholders directly, rather than first suing the ULC and potentially forcing the dissolution of the ULC (which would be inconsistent with the generally accepted view with respect to NSULCs), however, reasonable arguments can be made that a shareholder of an Alberta ULC is not liable unless the ULC has been dissolved. In any event, very serious caution

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should be exercised before considering holding any interest in any ULC (be it an Alberta ULC or an NSULC) without interposing some form of limited liability entity.

Generally, an Alberta ULC will be subject to provincial income tax under the *Alberta Corporate Tax Act* (“ACTA”) (and the federal *Income Tax Act*) if the ULC has a permanent establishment in Alberta in that year. Although a corporation governed by the ABCA generally must maintain books and records at a registered office in Alberta, this registered office likely will not be elevated to the status of a permanent establishment unless it is something more than a mere repository for the books and records of the corporation. Only if a corporation is resident in Canada and does not otherwise have a permanent establishment in Canada would maintaining a registered office in Alberta automatically subject the corporation to the ACTA.

Advantages of Alberta ULCs

The only other Canadian jurisdiction with unlimited liability corporations is Nova Scotia, which has the NSULC. Nova Scotia has dramatically increased the “fees” associated with incorporating or amalgamating an NSULC, to \$4,000, and of maintaining an NSULC, to \$2,000 annually. The fees in respect of Alberta ULCs are expected to be significantly below those currently levied in Nova Scotia.

Continuation of an Extra-Provincial Corporation

Specific rules in the ABCA permit extra-provincial corporations (both NSULCs and limited corporations) to be continued as Alberta ULCs. The rules appear to have been drafted in such a way as to satisfy the particular requirements of the Nova Scotia legislation for continuing an NSULC into Alberta, although a special resolution of the members of the NSULC is required and the Registrar under the NSCA must be satisfied that the continuance will not adversely affect creditors or shareholders of the company. Continuation of a limited corporation into an NSULC typically requires somewhat complex transactions (which could result in U.S. and/or Canadian tax liabilities unless structured very carefully). By comparison, continuation of a limited corporation as an Alberta ULC should be a relatively straightforward process.

Conclusion

The ABCA continues to evolve to better align with the needs of the business community. The recent amendments to the ABCA, as a result, should enhance Alberta’s reputation as a business-friendly province. Indeed, the amendments may even result in Alberta being the “jurisdiction of choice” for tax practitioners, not only with respect to planning that utilizes ULCs, but also for a wide variety of planning techniques involving limited corporations.

The comments in this Tax Note have been prepared for the purpose of providing timely notice regarding changes to the Business Corporations Act (Alberta) and are not intended to constitute a comprehensive summary or legal advice to any reader. The comments should not be relied upon to replace professional advice, including advice from qualified corporate legal counsel.