UNIFORM LAW CONFERENCE OF CANADA

CIVIL LAW SECTION

THE *UNIFORM INCOME TRUSTS ACT*: CLOSING THE GAP BETWEEN TRADITIONAL TRUST LAW AND CURRENT GOVERNANCE EXPECTATIONS

Report of the Uniform Income Trusts Act Working Group to the Uniform Law Conference of Canada, Civil Law Section

Readers are cautioned that the ideas or conclusions set forth in this paper, including any proposed statutory language and any comments or recommendations, have not been adopted by the Uniform Law Conference of Canada. They do not necessarily reflect the views of the Conference and its Delegates.

Edmonton, Alberta

August, 2006

TABLE OF CONTENTS

Report of the Uniform Income Trusts Act Working Group[*] to the Uniform Law Conference of Canada, Civil Law Section

I. Introduction

[1.] The ***Report on Forms of Business Associations in Canada***[1] delivered at the August, 2005 conference of the Uniform Law Conference of Canada (ULCC) suggested that income trust legislation should be placed at the top of the list of possible ULCC projects in the area of business associations. The ULCC agreed and requested a report on proposed income trust legislation that could be uniformly adopted by the provinces and territories (collectively, Provinces).

[2.] Subsequently, a working group was struck to consider the possible content of what we tentatively call the "***Uniform Income Trusts Act***" (interchangeably, UITA or Act).

[3.] Income trusts involve a complex amalgam of various legal disciplines, including: tax; securities; trusts; contracts; and corporate or partnership law, depending on the nature of the entities chosen to underlie the publicly-traded income trust. Reflecting the inter-disciplinary nature of the subject, a working group was assembled that included both leading specialists in the field and those who specialize in related areas. The working group consists of practitioners, regulatory lawyers and legal academics who work in the area.

[4.] What follows, therefore, is the report of the working group on the possible content of the UITA. While the recommendations set out in this report reflect the consensus of the working group, this is not to suggest that each recommendation necessarily has the support of every member of the working group. In addition to setting out the content of the UITA, this report addresses subjects the working group thinks, for various reasons, should be excluded from the UITA - at least for the time being. As stated, the focus of the report is on income trusts. However, at various points, the report will suggest that parallel amendments to the other type of flow-through entity used in Canadian capital markets, namely, the limited partnership (LP), also be considered.

II. What is an Income Trust?

[5.] To set the stage for the report to follow, it is important to lay out a brief overview of the income trust, including when, how and why it is used.

[6.] Historically, use of the income trust was largely confined to the acquisition and holding of certain steady, income-producing, capital-intensive assets. For many years, trusts have been used to own income-producing assets such as real estate (REITs) and oil and gas royalty-generating properties.[2] However, the last decade has seen a tremendous expansion both in the market share of the trust sector and in the use of trusts beyond their historical niches, as the income trust has expanded into operating businesses.[3] For example, income trusts have recently been used in various industries that traditionally were the exclusive domain of corporations.[4] These include consumer products, energy services, industrial manufacturing, media, raw materials, restaurants, retail distribution, equipment rental, investment banking and transportation.

[7.] Investors pool their funds in a trust that, in most cases, indirectly through a purchasing entity, acquires a reliable income-producing asset or business. The operating entity typically consists of a corporation or an LP – mainly because the trust cannot, for tax reasons, carry on an active business. One effect of this structure is that the business risks inherent in the operations are isolated at that level, thus minimizing the liability exposure of both the investors at the trust level and the trustees. An ideal candidate for an income trust is an asset or business that generates reasonably stable distributable cash-flows and has modest or predictable capital expenditure requirements.[5]

[8.] The type of trust that is the focal point of this report is an ***inter vivos*** trust created under the law of a Province through a declaration of trust (DOT) that is qualified as a mutual fund trust for tax purposes under the ***Income Tax Act*** (Canada) (ITA)[6] and that is a reporting issuer under the securities laws of one or more Provinces. The DOT provides for the appointment of individual trustees or a corporate trustee (generally formed under federal or provincial trust company legislation). The trust sells units to the public through a prospectus filed with applicable Provincial securities commissions. Investors in the trust are known as "unitholders". With the subscription proceeds, the trustees acquire and hold legal ownership of all of the assets of the trust, including, directly or indirectly, typically shares in the corporation or units in the LP carrying on the operating business so that the income trust does not carry on the business directly. The legal relationship between the trustees and the unitholders is that of trustee-beneficiary and is governed almost entirely by the written DOT superimposed on a body of largely uncodified trust law and codified securities laws of general application. Management of the operating entity can be either internal (the trust's operating entity being managed by officers of that operating entity) or external (the trust's operating entity generally entering into a management agreement with a third party management service provider). Both types of management structure are prevalent in income trust structures - although the latter is increasingly less common.

[9.] Many income trust structures also include a subsidiary trust as the operating entity or the intermediate entity through which shares in the operating corporation or units in the LP are held.[7] Subsidiary trusts are primarily used for technical tax reasons. Any legislation dealing with income trusts needs to factor in the continued use of LPs and subsidiary trusts in complex income trust structures.

[10.] The income trust structure has found favour with investors due to both its favourable tax attributes when compared with corporations and its high payment ratio relative to dividend-paying corporations.[8]

III. Background

1. Types of Reporting Issuers

[11.] A "reporting issuer" under the securities law of those Provinces that recognize the concept is generally an entity that issues securities under a prospectus, has filed a prospectus or the securities of which are or were listed and posting for trading on the Toronto Stock Exchange (TSX) or the TSX Venture Exchange or are traded over-the-counter on the Canadian Trading and Quotation System (CNQ). Reporting issuers generally take one of three legal forms:

(a) Corporations;

(b) Trusts; and

(c) LPs.

[12.] Corporations are by far the most prevalent form whether measured by number of entities or market capitalization.

[13.] Given the historical dominance of corporations in the commercial marketplace, legislative attention has historically been placed on corporate law and the regulation of the rights, interests and duties of the various actors in corporations, namely: shareholders; directors; officers; employees; auditors; indenture trustees; registrars and transfer agents; liquidators; receivers; bondholders; and other creditors. Flow-through vehicles (trusts and LPs) have received much less legislative and judicial attention than corporations. As a result, some of the laws governing trusts and LPs are, as will be elaborated in this report, underdeveloped.

2. Advantages of Flow-Through Vehicles

[14.] Canadian tax laws treat corporations, trusts and LPs differently. It is not the purpose of this report to discuss whether or how tax laws should continue to provide for differential treatment between corporations and flow-through vehicles. Those issues are the domain of tax policy. This report assumes that there will continue to be differences between the taxation of corporations and flow-through entities significant enough to justify the continued use of all three entities in the public marketplace.

(a) Income Trusts

[15.] One of the current advantages of an income trust is that the trust is allowed a deduction in calculating its income for tax purposes for all income paid or payable in the year to a beneficiary.[9] Income paid or payable is included in the beneficiary's income. However, if the beneficiary holds the units as part of an RRSP, RRIF, RESP, pension plan or other tax-deferred investment vehicle, then the recipient beneficiary does not pay any immediate tax on the income received or receivable from the income trust but instead can defer tax on the income receipt, and any further income accrued on the income receipt, until the amount is distributed by the tax-deferred vehicle to its beneficiary.[10] Distributions of capital out of the income trust to its beneficiaries are generally not taxable in the beneficiary's hands.

[16.] By contrast, corporations cannot deduct dividends paid to shareholders. In the months before the January 23, 2006 federal election, the previous Liberal government[11] announced amendments to the ITA that, at the federal level, would eliminate the element of double taxation that results when income is earned by a public corporation and then passed-through to shareholders by way of dividend. Despite this pending change, tax parity between corporations and trusts assumes that unitholders of an income trust are fully taxable on the distributions received from the trust, which is often not the case. Even if a dividend is paid to a person who holds the shares in a tax-deferred plan, tax will still have been paid at the corporate level. Within an income trust structure, the operating corporation's taxes can generally be reduced to almost nil. So, there will still be a tax advantage for an income trust.

[17.] Second, the tax character of capital and income to the income trust (for example, capital distributions, taxable dividends, capital dividends, interest and capital gains) is retained when flowed out to beneficiaries of an income trust.[12] By contrast, various income receipts of a corporation lose their character when paid to shareholders as a dividend.

[18.] Third, unlike corporations, business trusts are not subject to Provincial corporations capital tax (PCT)[13] or federal large corporations tax (LCT).[14] Avoiding PCT and LCT can give trusts a further incremental advantage.[15]

[19.] To maintain its status as a mutual fund trust for tax purposes, a trust must satisfy several tests relating to its investments and the distribution of its units.[16] These tests may be summarized as follows:

[20.] A trust is defined as a "mutual fund trust" if:[17]

(i) it is a "unit trust" resident in Canada;

(ii) its only undertaking is investing its funds in property (other than real property), acquiring, holding, maintaining, improving, leasing, or managing capital real property, or any combination of the foregoing; and

(iii) it complies with prescribed conditions relating to the number of unitholders, dispersal of ownership and public trading of its units.[18]

[21.] As well, an income trust cannot be established or maintained primarily for the benefit of non-resident persons.[19]

[22.] To qualify as a "unit trust", the trust must be an ***inter vivos*** trust, the interest of each beneficiary under which is described by reference to units of the trust, and either:[20]

(i) the units of the trust include units having conditions requiring the trust to accept retraction of the units by the holder at prices determined in accordance with such conditions and the fair market value (FMV) of such units is not less than 95% of the FMV of all the issued units of the trust; or

(ii) each of the following conditions is satisfied:

(A) throughout the taxation year, the trust was resident in Canada;

(B) the trust's only undertaking was investing funds in property (other than real property), acquiring, holding, maintaining, improving, leasing, or managing any capital real property, or any combination of the foregoing;

(C) at least 80% of the trust's property consists of any combination of shares, property convertible or exchangeable into shares, cash, debt instruments, marketable securities, real property in Canada, and rights or interests in any rental or royalty relating to petroleum or natural gas, an oil or gas well, or a mineral resource, in each case located in Canada;

(D) not less than 95% of its income for the current year was derived from, or from the disposition of, investments described in (ii) (C) above;

(E) not more than 10% of its property consists of bonds, shares or securities of any one corporation or debtor, other than a Canadian federal, provincial, or municipal government entity; and

(F) in the case of a REIT, the units are listed on a prescribed stock exchange in Canada.

[23.] With respect to the dispersal of ownership requirements:

(i) a class of units of the mutual fund trust:

(A) must be qualified for distribution to the public; or

(B) must have been lawfully distributed to the public where a prospectus, registration statement, or similar document was not required to be filed in respect of the distribution; and

(ii) in respect of any one class of units, there must be not fewer than 150 beneficiaries, each holding not less than one "block of units" of the class having an aggregate FMV of not less than $500.[21]

[24.] A corporation is not generally penalized if it fails to distribute its income to shareholders. Indeed, for certain types of corporations and sources of income, the ITA creates disincentives to the distribution of corporate income – particularly where the distribution would result in an element of double taxation or loss of a tax deferral.[22]

(b) Limited Partnerships

[25.] In contrast to corporations and income trusts, LPs are not taxpayers as such. Rather, the partners of an LP must file their own tax returns. Income, losses, taxable capital gains and allowable capital losses are calculated at the partnership level for tax purposes and then allocated to the partners. PCT and LCT are not applicable to LPs as such. However, to the extent that a corporation is a partner of an LP, its partnership interest will be taken into account in computing the corporation's liability for PCT and LCT. Unlike corporations and income trusts, losses of an LP can generally be flowed out to partners.[23]

3. Extent of Existing Statutory Treatment

[26.] Leaving aside the tax treatment of income trusts, currently there are three types of legislation that explicitly address income trusts. First and most importantly, income trusts, like other types of reporting issuers, are intensively regulated under Provincial securities laws and policies. Securities laws and policies provide for the largely uniform treatment of reporting issuers. An income trust is a species of reporting issuer. Some of the explicit recognition of income trusts in Provincial securities regulation is recent and is in direct response to the explosive growth of income trusts in the public marketplace.

[27.] Second, five common law provinces have explicitly addressed the narrow issue of unitholder immunity from civil liability. Quebec has gone beyond reporting issuers and has limited the liability of beneficiaries of trusts generally in the ***Quebec Civil Code*** (CCQ).[24] Limiting unitholder liability is addressed at Part V.6 below.

[28.] Finally, income trusts, themselves, as opposed to their underlying entities, may soon be subject to insolvency legislation. Indeed, these developments are still pending. Since preparation of the ULCC Business Associations Report in the Spring of 2005, Bill C-55[25] was passed by the former Liberal government that, if brought into force, would expressly extend the ***Bankruptcy and Insolvency Act*** (BIA)[26] and ***Companies' Creditors Arrangement Act*** (CCAA)[27] to income trusts even though, in the latter case, the trust is a non-corporate vehicle. It is important to have legislation in place in case some income trusts may have to be restructured in a manner similar to what is now possible for distressed corporations (particularly for REITs, which may not employ underlying entities).

[29.] Despite the general applicability of securities laws and the recent gap-filling efforts with respect to unitholder liability and insolvency laws, there is still a considerable lacunae in the law - at least in common law Canada. There is no comprehensive income trust legislation in Canada, except in Quebec which in the CCQ has codified its law applicable to trusts in that Province. By way of contrast, many U.S. states have adopted comprehensive statutes governing business or statutory trusts which, in the U.S., are extensively used in the real estate industry.[28] For example, most U.S. REITs are reportedly formed under Maryland business trust legislation.[29]

4. CBCA as Comparator

[30.] In considering the gaps that might exist in the regulation of income trusts and how those gaps might be addressed, it is useful to consider, as a basis for comparison, the provisions of the ***Canada Business Corporations Act*** (CBCA).[30] The CBCA provides a useful frame of reference for three main reasons.

[31.] First, it is a federal statute and, therefore, the logical alternative to incorporation under the general corporate legislation of each Province. Second, the CBCA has served as the ***de facto*** model corporate statute for many Provinces, particularly Alberta, Saskatchewan, Manitoba, Ontario, New Brunswick, Newfoundland and Labrador, the Yukon Territory, Nunavut and the Northwest Territories (as well as certain foreign countries such as New Zealand). It also served as the model for the separate statutes governing banks and federally-incorporated insurance companies, trust and loan companies and, with necessary variations, co-operatives. It has even served as the model for Bill C-21, the ***Canada Not-For-Profit Corporations Act*** which, if enacted and brought into force, will govern federal non-share corporations.[31] Almost 50% of the 200 largest non-financial corporations in Canada are formed under the CBCA.[32]

[32.] Third, using the CBCA as a frame of reference also facilitates uniformity. If a Provincial corporate statute were used as a model, the remaining Provinces may be more inclined to customize their income trust statute to their own corporate statute. Fragmentation of income trust legislation would undermine the goal of uniformity, which is particularly important in capital markets.

[33.] Diversity in corporate statutes prevails in Canada. Thus, the question that might be asked is whether diversity should also be encouraged in the legislative treatment of income trusts by the Provinces.

[34.] There are several responses. Corporate statutes cover both corporate reporting issuers and privately-held companies. Almost 99.7% of all corporations (whether incorporated at the federal level or under the laws of the Provinces) are privately-held.[33] In public markets, it is arguably more important that investors, many of whom are, directly or indirectly, pensioners and retail investors, know the nature of their rights and liabilities with respect to a particular issuer. Nor should acquiring such knowledge entail tremendous effort or transaction cost. Second, the number of income trusts in absolute terms is still very small. There are only about 237 income trusts in the whole country.[34] By contrast, there are approximately 6,677 corporate reporting issuers in Canada.[35] There are approximately 2.15 million corporations in Canada, exclusive of those that have been dissolved but including those that may be inactive.[36] Due to the wide variety in size and character of corporations, far more diversity must be accommodated in corporate statutes than is warranted in the numerically smaller and characteristically more homogeneous realm of income trusts.

5. Summary of Guiding Principles

[35.] The working group feels that the advantages of uniform income trust legislation at this time outweigh the marginal advantages (if any) that might be obtained in diversity and that, therefore, the UITA should be implemented on a substantially uniform basis throughout the country even in those Provinces in which few, if any, income trusts are likely to be established. The main reasons for uniformity are to achieve fair and balanced treatment for the main actors in the income trust sector, ***viz***. unitholders, creditors, trustees and management, in a manner consistent with their commercial expectations.

For unitholders, this primarily translates into immunity from liability and into rights and remedies broadly consistent with those available to shareholders. For creditors, this translates into clear rights and remedies directly against the assets of the trust. For trustees, it means liabilities comparable to those imposed on corporate directors. And for management, it means flexibility in arrangements for the management of income trusts and their operating businesses or assets. All Provinces will have residents who fall into one or more of these categories. Likewise, the operations of income trusts will touch all Provinces.

6. Preserving the Tax Characterization of Income Trusts – An Imperative

(a) Domestic Characterization of Domestic and Foreign Entities

[36.] As stated, the ITA provides separate tax regimes for corporations, trusts and partnerships. However, the ITA does not make a meaningful attempt to define these entities, relying instead mainly on Provincial law for entity classification.

[37.] Corporations are formed under a statute, are separate legal persons, separate management from ownership and, with rare exceptions, insulate shareholders from liability.[37] Even in Quebec, partnerships in Canada are generally not considered separate legal entities – although there have long been specific statutory exceptions to this general rule.[38] A partnership (including an LP) merely describes the relationship that subsists between two or more persons carrying on business in common with a view to profit.[39] LPs require registration. General partnerships that do not use a name other than those of its partners do not require registration.[40] General partnerships that use a name other than those of its partners as well as the recent advent, limited liability partnerships (LLPs), require registration under Provincial legislation regulating the use of business names[41] but otherwise do not require registration as a condition of formation.

[38.] Trusts have been much more various than corporations and partnerships. Historically, well-recognized forms of trusts have included the charitable use trust, business trust, investment trust, pension trust, securitization trust and many others. Over the centuries, various types of trusts have been created or recognized by courts to serve the function at hand.

[39.] Domestically, there have been reasonably clear lines of demarcation among these entities. As a result, the issue of entity classification of domestic entities has not been fully developed in this country. The issue has, however, arisen in connection with the tax classification of foreign entities. Briefly, whether a foreign entity will be classified as a corporation under Canadian tax law turns primarily on whether the foreign entity is recognized, under the foreign law, as a separate legal person.[42] A second, but subordinate criterion, is whether the owners of the foreign entity enjoy limited liability.[43]

[40.] If, however, the commercial legal rules relating to income trusts were altered so that the rules applicable to corporations were extended to income trusts, the tax status of the income trust in Canada could be jeopardized, putting it at risk of becoming taxed domestically as a corporation. Taxing income trusts as corporations would defeat the purpose of allowing investment through income trusts as an efficient and attractive alternative to the use of corporations. Arguably, the greater the similarity in the legal rules applicable to trusts and corporations, the greater the risk that what was intended as a trust will instead become taxed as a corporation. The aggregate of all legislative changes made to income trusts should not, therefore, be such that they adversely affect the classification of income trusts for tax purposes, resulting in their re-characterization as corporations. While no one factor might push trusts over the line and turn them into corporations for tax purposes, the combination of all factors might have that unintended effect. For that reason, the working group felt that, at this time, restraint should be exercised in the extent to which corporate rules are superimposed onto income trusts. Instead, a balance must be struck between superimposing corporate law rules onto income trusts in the interests of investor protection while, at the same time, preserving the flow-through tax status of the trust for the ultimate benefit of those same investors.

(b) Foreign Characterization of Canadian Income Trusts

[41.] The same issue of entity classification also arises in some foreign jurisdictions. While some U.S. states provide that statutory business trusts are separate legal persons and that unitholders enjoy immunity from liability equivalent to that enjoyed by shareholders,[44] the tax classification of Canadian income trusts could be an issue under other foreign jurisdictions that are significant to Canadian capital markets. A survey of these jurisdictions, however, was beyond the scope of this report.

IV. Regulatory Approaches

1. Constitutional Dimensions

[42.] In contrast to corporations, non-corporate forms of business associations such as LPs and income trusts cannot be formed under federal law. Provinces have exclusive jurisdiction to legislate in respect of property and civil rights under s. 92(13) of the ***Constitution Act, 1867***,[45] and the proposed UITA falls squarely within the legislative jurisdiction of the Provinces. As noted at Part III.3 above, the federal government has the power to legislate in certain areas that are germane to the income trust sector – particularly with respect to income tax and insolvency law.

2. Mandatory Rules

[43.] There are two types of provisions that could be developed to govern income trusts: mandatory rules and optional provisions. Mandatory provisions would override any contrary provisions of a DOT. Parties are unable to contract out of mandatory rules.

[44.] Mandatory provisions can be used to set a minimum level of investor protection and, therefore, reinforce investor expectations. With respect to business and investment vehicles, there is generally nothing to prevent parties from imposing rules or standards that are more strict than the minimum mandatory standards provided for in a statute. Unless otherwise stated, any rules recommended for adoption in this report are mandatory.

[45.] In some cases, the effect on existing DOTs must also be considered. The issue here is whether the mandatory provision should override an existing DOT or whether the contrary provisions of a DOT should be grandfathered so that the new mandatory rule will only apply to DOTs created after the implementation date of the UITA. The issue of grandfathering existing DOT provisions will be considered in this report on a case-by-case basis. Schedule A to this report summarizes the effect that adoption of the recommendations set out in this report is expected to have on existing DOT provisions.

3. Optional Provisions

[46.] In some cases, where a mandatory rule is not recommended in this report, consideration is then given to the adoption of an optional (or model) provision. There are three types of optional provisions: opt-in; opt-out; and default. An opt-in provision means that the provision in the statute can be adopted in a DOT but, unless expressly adopted, is excluded. A DOT has the flexibility to adopt a model provision in whole or in part or to exclude its application. Examples of opt-in provisions under the CBCA include cumulative voting[46] and pre-emptive rights on share issues.[47]

[47.] An opt-out provision means that a statutory provision applies unless the DOT excludes it. Before an opt-out provision is imposed on existing income trusts, consideration must be given to its impact on the business bargain reflected in the existing DOT for that trust. Opt-out provisions that are subsequently imposed on an income trust may have the effect of altering the bargain among the parties, unless an amendment is made to exclude the application of the provision. In any case, an opt-out provision imposes upon the parties the burden of amending their DOT just to maintain the ***status quo*** and may inadvertently shift the balance of power amongst the unitholders of an income trust. For example, if an amendment to exclude a provision of the UITA requires the support of not less than 2/3rds of votes cast by unitholders, then power shifts from the majority (who purchased units on the basis of the DOT) to the minority (who, if holding more than 1/3rd of the votes, can veto the amendment designed to preserve the ***status quo***). Thus, where this report refers to an optional provision, it is, unless otherwise stated, an opt-in provision. Examples of opt-out rules under the CBCA include the ability of shareholders of a non-distributing corporation to waive the audit requirement,[48] adopt a unanimous shareholder agreement[49] or shorten the notice requirement for meetings of shareholders.[50]

[48.] A default rule applies where the constating document is silent. Examples of default rules under the CBCA are the rights of shareholders to exercise one vote ***per*** share at meetings, to be paid any dividends and to receive residual assets on liquidation.[51] Further examples are the quorum rules for meetings of shareholders and the board.[52] The advantages of a default rule are to fill gaps and to reduce the length of constating documents and by-laws.

4. Cons and Pros of Optional Provisions

[49.] Optional provisions have certain potential draw-backs. Where optional provisions exist but are never used, they merely serve to clutter the statute. Even if they are adopted by the parties, they result in the business bargain being partly covered in the DOT and partly in the statute. It may be easier for retail investors to have the entire bargain set out in one instrument. More pragmatic concerns may also exist. To date, for example, there has been considerable variance between provisions that are used in Alberta DOTs and those that are used in Ontario DOTs. Provisions also vary from law firm to law firm. In some cases, it might be a challenge to draft model provisions in a statute that would actually be used in preference to those that are drafted by the law firm representing the trust issuer.

[50.] By way of analogy, model articles of association (Table A Articles) are still set out in a table to the Nova Scotia ***Companies Act*** (NSCA).[53] Originally, these were modeled after the English legislation from which the NSCA was derived. Table A Articles facilitated the incorporation of companies. In the days before computers, applicants for incorporation did not have to pay a stenographer to type a lengthy set of customized articles. Instead, the incorporators could form the company by adopting Table A Articles - subject to whatever individualized changes the incorporators sought to make.

[51.] However, Table A Articles in the NSCA have fallen into disuse. Generally, each law firm in Nova Scotia has long had its own standard articles of association and prefers to use it rather than the statutory model.

[52.] On the other hand, model provisions could still be useful in certain circumstances as an alternative to mandatory rules. Some examples appear later in the report. Also, model provisions could help in standardizing certain provisions and could also serve as a point of reference for purposes of prospectus disclosure.

V. Content of the UITA

1. Scope of the Statute

[53.] As stated, the primary focus of the UITA should be mutual fund trusts that are reporting issuers in Canada other than mutual funds in which investors are entitled to receive, after demand, an amount calculated by reference to a proportionate interest in the net assets of the fund (in this report, these latter trusts are referred to as "ordinary mutual funds"). With certain exceptions for subsidiary trusts and ordinary mutual funds, other types of trusts, in particular other types of private ***inter vivos*** trusts should not be addressed in the UITA. Each type of trust has its own unique functions and attributes. Consideration of trusts that are not reporting issuers or subsidiary trusts falls outside the scope of this report.

[54.] Subsidiary trusts, as the name implies, are ***inter vivos*** trusts that are, directly or indirectly, owned by the reporting issuer (or more accurately by the trustees of the reporting issuer). As further described at Part II above, subsidiary trusts are part of a larger income trust structure. Income trust structures often involve a combination of entities that include a mutual fund reporting issuer at the top and, beneath that, layers of subsidiary trusts, LPs and/or corporations.[54] The underlying business is actually owned and operated by one or more of these subsidiary entities, "subsidiary entity" being used in this report to mean a body corporate, partnership, trust, joint venture or unincorporated association or organization that is, directly or indirectly, controlled by the income trust. Since trustees of the subsidiary trust are also capital markets participants and since trustees of the top-level income trust are often also trustees of the subsidiary trust, it is important that the liability regime that is adopted for the trustees of an income trust also apply to the trustees of any underlying or subsidiary trust. Otherwise, whatever liability regime may be established for trustees of the income trust will be incomplete.

> **Recommendation 1: Subject to the exceptions set out in recommendations 3 and 4 below, the Act only apply to: (a) trusts that are reporting issuers in Canada (the "income trust"); and (b) any trust a majority of whose units are, directly or indirectly, owned by or for the benefit of the income trust (the "subsidiary trust"). For purposes of the Act, reference to a trust would mean either an income trust or a subsidiary trust but not an ordinary mutual fund, as described more fully in recommendation 3 below.**

[55.] The securities laws of Prince Edward Island and all three territories do not define the term "reporting issuer". For these Provinces, the Act needs a default definition.

> **Recommendation 2: Where the securities legislation of a Province does not contain a definition of "reporting issuer", "reporting issuer" will mean a trust (a) that has filed a final prospectus for which a receipt has been issued under Provincial securities legislation or (b) any of whose securities are listed and posted for trading on any exchange in Canada.**

2. Exclusion of Ordinary Mutual Fund Trusts

[56.] With the sole exceptions of the unitholder liability shield discussed at Part V.6 below and the conflict of laws rules discussed at Part V.12 below, the Act should not cover ordinary mutual funds. An ordinary mutual fund is a mutual fund in which investors are entitled to receive, on demand or within a specified period after demand, an amount computed by reference to a proportionate interest in the whole or part of the net asset value (NAV) of the fund.[55] Ordinary mutual funds fall outside the scope of this report. However, because this report recommends at Part V.6 below that the UITA subsume the unitholder liability shield currently embodied in the legislation of some Provinces and those statutes currently cover investors in all trusts that are reporting issuers under declarations of trusts governed by those Provinces, the liability shield in the UITA should continue to extend protection to the unitholders of all trusts that are reporting issuers whether income trusts or ordinary mutual funds. Likewise, the conflict of laws rules are needed to identify which Provincial statute governs an ordinary mutual fund.

> **Recommendation 3: Except with respect to recommendations 7, 8, 9, 36 and 37 below, the Act not apply to a trust in which investors are entitled to receive, on demand or within a specified period after demand, an amount computed by reference to the value of a proportionate interest in the whole or part of the net assets of the fund.**

3. Exclusion of Foreign Trusts

[57.] As stated at Part II above, the Act is only intended to capture certain types of publicly-traded mutual fund trusts recognized as such under the ITA. In particular, the Act is not meant to apply to foreign trusts and care must be taken to ensure that the Act does not inadvertently capture foreign trusts. Accordingly, the Act should not apply if the income trust is a "non-resident" of Canada for the purposes of the ITA. Adopting the ITA residency criterion suggests itself because, as discussed at Part III.2 above, it is already part of the tax definition of a "mutual fund trust".

> **Recommendation 4: The Act not apply to a trust that is a non-resident of Canada for the purposes of the *Income Tax Act* (Canada).**

4. Statement of Statutory Purposes

[58.] We recommend that the UITA contain a brief statement of the purposes of the Act modelled on s. 4 of the CBCA, which sets out the overarching purposes the CBCA is designed to achieve. In the UITA, these purposes would include placing the law applicable to income trusts on a firm legal footing and advancing the cause of uniformity of income trust law in Canada.

> **Recommendation 5: The Act contain a declaration that its purposes are to clarify and modify certain laws applicable to income trusts and subsidiary trusts and to advance the cause of harmonizing the law applicable to these trusts with the laws in other Provinces.**

5. Legal Status

[59.] To assist with the tax characterization issues referred to at Part III.6 above, the UITA should expressly state that an income trust is not a separate legal person and is not a corporation. Anything that could alter the tax status of the income trust or risk it becoming taxed as a corporation would be self-defeating. Thus, regardless of whether statutory trusts are treated as separate legal persons in the U.S., they cannot be recognized as separate legal persons in Canada at the present time, in the absence of changes to tax laws.

> **Recommendation 6: The Act state that, except to the extent otherwise provided in any other statute of the Province, an income trust or subsidiary trust is not a legal person and that nothing in the Act shall be construed as making an income trust a body corporate.**

6. Unitholder Liability

(a) Investor Immunity

[60.] Limiting the liability of investors to the amounts that they contribute to an entity is critical to capital formation. Equity investors in publicly-traded corporations are shielded from personal liability even if they play a role in the direction or management of the corporation. Likewise, investors in income trusts and ordinary mutual funds should not face the possibility of personal liability.

[61.] Any uncertainty as to whether an investor could be exposed to loss beyond the amount invested, or committed for investment, poses a significant barrier to capital formation, particularly for risk-averse investors such as financial institutions and pension funds. Before the adoption of specific legislation shielding trust unitholders from liability, financial institutions and pension funds were in fact generally too risk-averse to invest in income trusts. What this demonstrates is that different kinds of investors are willing to accept different levels of risk.

[62.] In addition to the arguments that justify limited liability for shareholders in corporations, further arguments apply in the case of trusts. First, while there was some residual doubt in the law because of the paucity of jurisprudence, the overwhelming consensus was that the risk of liability for unitholders of income trusts was extremely remote.[56] However, analysis of the issue entailed significant transaction costs in the form of expensive legal opinions. Investors rarely understood the degree of risk they were incurring. Thus, specific legislation shielding investors likely does not change the law but rather merely simplifies the analysis, reducing transaction expense and encouraging capital formation.[57]

[63.] Investors in publicly-traded issuers should enjoy comparable immunity from personal liability regardless of the legal form of the underlying issuer: corporation; income trust; ordinary mutual fund; or LP. This is already the case with respect to trusts that are reporting issuers and governed by the laws of British Columbia, Alberta, Saskatchewan, Manitoba or Ontario and with respect to Quebec trusts generally. Under the CCQ, a beneficiary/investor is not liable for the acts of the trustees in the absence of fraud.[58]

(b) Liability Shield

[64.] The UITA should, therefore, contain the same liability shield as is provided for in corporate legislation such as the CBCA, ***Business Corporations Act*** (Ontario) (OBCA)[59] and ***Business Corporations Act*** (Alberta) (ABCA).[60] The CBCA provides as follows:

> The shareholders of a corporation are not, as shareholders, liable for any liability, act or default of the corporation except under [various provisions are listed that require shareholders to disgorge cash or other property received while the corporation is insolvent or that impose liability on shareholders under a unanimous shareholder agreement].[61]

[65.] The UITA should subsume the liability regime currently set out in separate statutes such as the ***Trust Beneficiaries Liability Act, 2004*** (TBLA or Ontario Act),[62] the ***Income Trust Liability Act*** (the Alberta Act),[63] ***The Investment Trust Unitholders' Protection Act*** (the Manitoba Act),[64] ***The Income Trust Liability Act*** (the Saskatchewan Act)[65] and the ***Income Trust Liability Act*** (the BC Act).[66] Explicit immunity from liability gives considerable comfort to investors in the marketplace. Also, courts would likely find the statutory language of the TBLA, BC Act, Alberta Act, Saskatchewan Act, Manitoba Act or Ontario Act (collectively Income Trust Liability Acts) persuasive in that it parallels the immunity from liability granted to shareholders.[67] While arguments could be made that each statute adds little to the common law, a Herculean effort was made to pass the Income Trusts Liability Acts in order to promote investor confidence in trusts that are reporting issuers. It would be a retrograde step to repeal the statutes outright. Rather, the UITA should subsume and standardize the unitholder liability shield so that the same unitholder liability regime applies on a uniform basis throughout the country. Investors would then have the same confidence investing in an income trust or ordinary mutual fund that they now enjoy investing in a CBCA, OBCA, ABCA or almost any corporation (other than an unlimited company in Nova Scotia or an unlimited liability corporation in Alberta).

(c) Immunity Formulation

[66.] To achieve uniformity under the UITA, a choice must be made among the immunity formulations: (i) in the Ontario Act; (ii) common to the Alberta Act, Saskatchewan Act and Manitoba Act; and (iii) in the BC Act.[68] A majority of the working group is of the view that the limitation of liability formulation in the Ontario Act is to be preferred to that found in the earlier Alberta Act (which was subsequently replicated in the Manitoba and the Saskatchewan Acts). While the Alberta, Saskatchewan and Manitoba Acts only immunize unitholders from the liabilities of the "trustee", the Ontario Act immunizes unitholders from the liabilities of "the trust or any of its trustees". Even though the intent and likely effect of the Income Trust Liability Acts are the same, the Ontario Act is clearer, more certain and more comprehensive than the Alberta, Saskatchewan or Manitoba Acts. And while the language negating any liability of the beneficiaries for liabilities of the trust perhaps implies that the trust is a separate legal person when it generally is not, the additional language may extend further protection to the investing public. For example, the ***Securities Act*** (Ontario)[69] and the ***Securities Act*** (Alberta)[70] include trusts within the definition of "person" for purposes of such legislation, meaning that the trust is subject to the various liabilities imposed on issuers. Likewise the CBCA, OBCA and ABCA include trusts in the definition of "person" and, therefore, could impose liabilities arising under those statutes against trusts ***per se***, rather than against trustees.

Recommendation 7: The Act subsume any stand-alone Provincial statute providing a liability shield in favour of unitholders of trusts that are reporting issuers and adopt the immunity formulation found in the Ontario Act, making it apply on a

uniform basis in all Provinces. The liability shield would extend to unitholders of income trusts, subsidiary trusts and ordinary mutual funds.

(d) Retroactivity

[67.] The BC Act, which received third reading on March 30, 2006, contains an important innovation on the earlier Uniform Trust Liability Acts. The new BC Act, which is otherwise modelled on the Alberta Act, expressly declares that it has retroactive effect, in effect confirming the consensus view of the common law and the pragmatic effect of the income trust structures that have been put in place. We agree that the BC Act makes a useful contribution.

Recommendation 8: Like the *Income Trust Liability Act* (British Columbia), the unitholder immunity rule in the Act apply with retroactive effect.

(e) Negating Partnership and Agency Characterizations

[68.] To forestall an argument that trustees could be carrying on a business as agents for unitholders as principals and that the relationship amongst the unitholders is that of partnership, it is desirable to amend Provincial partnership legislation to add a provision akin to that stating that the relationship among shareholders of a corporation is not that of partnership.[71]

Recommendation 9: The partnership legislation be amended to stipulate that the relationship among unitholders in an income trust, a subsidiary trust or an ordinary mutual fund is not a partnership.

[69.] While we considered going further to add a provision that unitholders cannot be liable on some other agency theory, we do not recommend that the UITA include such a provision. It is theoretically possible, although highly unlikely, that trustees could be found to be agents acting for unitholders as principals.[72] However, the same theoretical possibility exists under corporate law.[73] In appropriate cases, courts can use agency concepts to pierce the corporate veil.[74] In our view, it would be going overboard to create a special rule for unitholders that does not exist for shareholders. The UITA should leave open the possibility that, in some remote or extreme set of circumstances involving egregious unitholder behaviour, courts could pierce the unitholder liability shield.[75]

(f) LPs

[70.] Analogous arguments can be made that limited partners should enjoy immunity from liability similar to that accorded shareholders under corporate law or unitholders under the UITA. LPs are most often, but not exclusively, used as investment vehicles.

Different formulations of the liability shield across the country are arguably not conducive to promoting use of the LP as a vehicle for investment. However, the liability shield for LPs in general is beyond the scope of this report, and we have not exhaustively considered the pros and cons of various formulations of the LP liability shield. As well, since this ULCC working group on income trusts was struck, a separate ULCC working group under the chair of Professor Heather Heavin was formed to report on general partnerships and LPs. We, therefore, defer to the working group studying partnership law the broader question of whether investors in LPs should enjoy a stronger liability shield than that which generally prevails under Provincial law. Having said that, at least with respect to LPs that are subsidiary or underlying entities of income trusts and that, therefore, are part of the income trust structure, our view is that limited partners should enjoy a full liability shield comparable to that available to shareholders under corporate law or to unitholders under the Income Trust Liability Acts, or that would be available to unitholders under the UITA. As in the case of investing in these other vehicles, the shield should not automatically be lost just because the limited partner controls or participates in managing the business of the LP. It was also our tentative view that, at least with respect to LPs that are themselves reporting issuers, limited partners should enjoy a full liability shield comparable to that available to shareholders and that the shield not be lost merely because the limited partner participates in, or controls, the management of the business of the LP. Uniformity in the liability shield for investors in corporations, income trusts, ordinary mutual funds and LPs would be conducive to capital formation and remove an important bias in the commercial law.

7. Unitholder Rights and Remedies

(a) Unit Equality

[71.] The principle of equality among all shares within the same class is deeply enshrined in Canadian corporate law.[76] Thus, for example, provisions in articles or by-laws that purport to reduce the voting power of the shareholder who is a transferee[77] or on the basis of the total number of voting shares held[78] have been struck down by our courts as invalid. The only exceptions to the principle of the equality of share classes are where different classes or series of shares are created (each with different rights, privileges, restrictions and conditions attached) or where the shares are held by a subsidiary in its parent corporation. A subsidiary cannot vote any shares that it beneficially holds in its parent.[79]

[72.] DOTs often provide that units held by affiliates, not just subsidiaries, cannot be voted. The potential disenfranchisement of unitholders is at variance with accepted norms and expectations. Disenfranchisement may also adversely affect the market for corporate control and serve to entrench inefficient management. Accordingly, we recommend that the Act override provisions of a DOT that would discriminate against unitholders on the basis of who holds the units. As in the case of corporations, however, controlled subsidiary entities would not be permitted to vote units held in the income trust.

> **Recommendation 10: The Act provide that all units of the same class or series are equal in all respects but that a controlled subsidiary entity not be permitted to vote any units that it holds in its parent income trust.**

(b) Election and Replacement of Trustees

[73.] Provision for the election of trustees is a standard feature of all income trusts. However, the Act should enshrine flexibility in the election or appointment of trustees by permitting designated unitholders such as sponsors to continue to elect or appoint one or more trustees in accordance with the terms of the DOT. As well, between annual meetings, trustees should be empowered to appoint replacement trustees to fill vacancies and, as under corporate law, expand the number of trustees by up to 1/3rd the number of trustees elected at the last annual meeting where the DOT so provides. The right to increase the number of trustees is useful where, between annual meetings, the income trust expands through acquisition or other unexpected opportunities arise. Before the first annual meeting, even greater flexibility is warranted. Often trustees are added after the preliminary prospectus but before the first annual meeting.

> **Recommendation 11: The Act provide that trustees of an income trust may be elected or appointed at unitholder meetings by the unitholders or subset of unitholders entitled to vote thereon in accordance with the declaration of trust. Before the first annual meeting, trustees in office shall have the right to appoint additional trustees in accordance with the DOT. Between annual meetings, trustees in office shall have the right to appoint replacement trustees to fill any vacancies and, if the DOT so provides, appoint up to 1/3rd the number of trustees elected at the last annual meeting. Unitholders entitled to elect any particular subset of the trustees would have the exclusive right to fill any vacancies within that subset**.

[74.] According to a survey[80] conducted by Goodmans LLP for Industry Canada (Goodmans Survey), 76% of the DOTs surveyed permitted unitholders to remove trustees by a majority vote and 22% provided that only a super-majority of 2/3rds of units voted could remove trustees.[81] To place unitholders in substantially the same position as shareholders of a corporation, no more that a simple majority of votes cast by unitholders entitled to vote on the election of the trustees, or the subset of trustees affected, should be needed to remove the trustees, or the members of the subset, elected by those unitholders.

To clarify, public unitholders would not be given the power to remove trustees who are not subject to election by those unitholders. One issue that required a close examination was whether a new uniform rule on removal of trustees should be imposed on existing trusts whose DOTs provide super-majority approval, removal for cause or some higher or other removal threshold. Alternatively, should existing DOTs be grandfathered? In support of the uniform rule are arguments based on uniformity of fundamental investor rights in publicly traded vehicles and avoiding the bifurcation that would otherwise take place between grandfathered and post-grandfathered income trusts. The counterveiling argument posits that legislators should avoid doing violence to existing consensual arrangements found acceptable to the parties. On balance, the working group felt that, in this instance, the fundamental nature of the investor rights and the advantages to investors in having largely uniform expectations outweighed the arguments in favour of grandfathering.

> **Recommendation 12: The Act provide that, notwithstanding any contrary provision in a declaration of trust, trustees who are elected or appointed by holders of publicly traded units may be removed or replaced by a simple majority vote (*i.e.* a majority of votes cast) of those entitled to vote thereon.**

(c) Unitholder Proposals

[75.] Corporate legislation such as the CBCA, OBCA and ABCA provides shareholders with machinery to enable them, at the expense of the corporation, to communicate with the corporation and their fellow shareholders on matters of common concern. However, according to the Goodmans Survey, only one out of 54 income trusts surveyed (2% of the sample survey) provided a unitholder proposal regime similar to that found in corporate legislation such as the CBCA.[82]

[76.] In the absence of an express provision in a DOT, trustees are under no obligation to make reference to any views other than their own in any notice of meeting or management information circular nor to include in any notice of meeting any proposals other than their own. While some might dismiss the shareholder proposal as a device whereby shareholders can harass or abuse management, Parliament and our Provincial legislatures have recognized the shareholder proposal as a legitimate mechanism for encouraging shareholder voice in the affairs of corporations, particularly those that are publicly-traded.[83] In general terms, therefore, the UITA should contain a similar mandatory provision whereby registered or beneficial unitholders of an income trust can submit written proposals for circulation in advance of an annual meeting. A unitholder proposal regime would be an important vehicle for dialogue between management and unitholders of an income trust, the real point of the proposal regime.[84] The unitholder proposal regime should be loosely modelled on the equivalent shareholder proposal provisions of the CBCA.[85]

[77.] As checks against potential abuse, for example, some of the anti-harassment devices found in the CBCA should also be included in the UITA. These include the right to reject any proposal that is not received at least 90 days before the anniversary date of notice of the previous annual meeting,[86] any proposal whose primary purpose is to enforce a personal claim or redress a personal grievance,[87] any proposal that is being used to secure publicity[88] or any proposal that does not relate in a significant way to the property or affairs of the income trust.[89] Other counterweights to making the proposal mechanism available to unitholders include placing a 500-word limitation on the proposal and any supporting statement,[90] requiring minimum levels of support and timeframes before similar proposals may be resubmitted[91] and temporarily suspending the proposal submission rights of any unitholder who submits a proposal but then fails to present it at the ensuing meeting.[92]

[78.] As is the case under corporate law, we are not recommending that unitholder proposals necessarily be given any binding effect. The legal effect of a resolution will depend on the DOT and the nature of the resolution proposed. The proposal regime is primarily a means to give unitholders voice in the affairs of their income trust. We observe too that, in many cases, the unitholder proposal will relate to the underlying operating entity rather than to the income trust itself.

> **Recommendation 13: The Act contain a provision whereby registered or beneficial voting unitholders of an income trust are entitled to submit a written proposal for circulation in advance of an annual meeting. The provision would be loosely modelled on the shareholder proposal regime set out in the CBCA. This includes proof of beneficial status, timeliness of the submission, grounds upon which to reject the circulation of proposals (including the requirement that the proposal "relate in a significant way to the property or affairs of the income trust"), word-count and resubmission restrictions and the temporary blacklisting of those who submit, but fail to present, a proposal at the ensuing meeting of unitholders.**

(d) Requisitioning Meetings of Unitholders

[79.] Under the CBCA, OBCA and ABCA, the holders of not less than 5% of the issued shares of a corporation that carry the right to vote at a meeting may requisition directors to call a meeting of shareholders for the purposes stated in the requisition.[93] While not frequently invoked in practice,[94] the existence of a shareholder requisition constitutes an important disciplinary check on management, posing the possibility that, at any time between annual meetings, shareholders could remove a board they feel is either untrustworthy or simply underperforming.

[80.] Again, there is no compelling reason to deny unitholders of income trusts the right to requisition unitholder meetings. One observation from the Goodmans Survey is that, although all DOTs included in the survey provided for the requisition of unitholder meetings, the threshold at which unitholders can invoke the provision varied widely.[95] Instead of the uniform rule under corporate legislation, only 37% of DOTs prescribed the 5% threshold for calling a meeting, while 48% had a 10% threshold, 4% had a 15% threshold and 11% had a 20% threshold. It is also possible for DOTs to exclude unitholder requisitions completely, although none of those included in the Goodmans Survey had done so.

[81.] Despite economic efficiency arguments supporting freedom of contract, it is difficult to justify allowing different thresholds depending on whether the reporting issuer is a corporation or an income trust. Investors in corporations and income trusts would benefit from having a uniform threshold equal to that found in corporate statutes. Since Parliament and Provincial legislatures have generally set the threshold at 5%, it would be more democratic to make uniform the lower corporate threshold rather than one of the higher thresholds currently found in DOTs. Also, grandfathering existing DOTs created before the UITA goes into effect would create an awkward and confusing bifurcation between publicly traded issuers subject to the 5% threshold and the grandfathered income trusts that would continue to be subject to a higher threshold.

> **Recommendation 14: The Act provide that, notwithstanding any contrary provision in a declaration of trust, registered or beneficial unitholders of an income trust holding not less than 5% of the voting units may requisition a meeting of unitholders.**

(e) Investigations

[82.] As the ***Hollinger***[96] saga and, before that, the ***Principal Trust***[97] debacle in Alberta demonstrated, statutory investigations can prove extremely useful in getting to the bottom of complex commercial wrong-doings. Part XIX of the CBCA sets out what has become the accepted statutory model. Although a few DOTs contain contractual investigatory powers, these contractual provisions are narrower than the statutory investigations that are available under corporate law. Corporate investigations are conducted by an inspector under court supervision and, as a result, have certain legal protections, powers of compulsion and evidentiary privileges not otherwise available. Even though they may be used infrequently, it is important that the power to investigate frauds and other wrong-doings in complex settings be extended to income trusts – in part as a prophylactic against abuse and in part for its intrinsic utility.

Recommendation 15: The Act set out an investigation regime for income trusts that is similar to Part XIX of the CBCA.

(f) Oppression Remedy

[83.] According to the Goodmans Survey, none of the DOTs surveyed provided unitholders with an equivalent of the statutory oppression remedy available under corporate law to shareholders, holders of debt obligations and other complainants.[98] Since the oppression remedy is statute-based, infrequent provision of an oppression remedy in DOTs may reflect the lack of a statutory underpinning.[99] The oppression remedy requires an application to court and vests the court with broad remedial jurisdiction.

[84.] While the oppression remedy has undoubtedly been very useful to minority shareholders of closely-held private companies, the working group had reservations on the usefulness of the oppression remedy with respect to widely-held public corporations. Judging by reported cases, the oppression remedy has not been used in the public company context frequently or with much recent success.[100] On the other hand, it is perhaps unfair to measure the usefulness of the oppression remedy by reported cases alone. The true value of the oppression remedy is perhaps more ***in terrorem*, *viz.*** as an omnipresent warning to management and controlling shareholders that all corporate conduct is subject to scrutiny and possible remedial action by a court under a broad fairness standard. Even though unitholders of an income trust might (subject to the terms of the DOT, perhaps) have an alternative action in equity for breach of duty by the trustees,[101] such an action is untested.

[85.] On balance, our recommendation at this point is that the oppression remedy not be extended as a mandatory rule applicable to income trusts in the absence of a definitive analysis of its costs ***versus*** benefits to widely-held public corporations. As well, as a practical matter, income trusts pay out most or all of their taxable income, which, in practice, severely limits the discretion available to management and makes management highly dependent on the markets to raise expansion capital. Finally, to qualify as a mutual fund trust, unitholders are usually given the right, subject to limitations, to retract at close to trading value. Even though this right has been rarely exercised in practice, it is something usually given to unitholders for which there is rarely a counterpart in corporate law outside the realm of mutual fund corporations or retractable preferred shares issued by other types of corporations.

[86.] Accordingly, this may be an area where an optional provision is warranted. Underwriters and, ultimately, purchasers of units could decide for themselves the relative advantages and disadvantages of the oppression remedy with respect to their particular income trust. An opt-in provision would at least allow unitholders of those trusts choosing it to have access to the courts in the same way that shareholders of a corporation have access to the courts to rectify oppressive or unfairly prejudicial conduct. Indeed, the recent Royal Utilities Income Fund offering evidences that there may well be a place for the oppression remedy in the panoply of rights extended to unitholders. At least, the Act could create the statutory framework for the remedy, leaving it to the marketplace to decide whether adopting it was value-enhancing or value-reducing.

> **Recommendation 16: The Act provide a counterpart to the corporate oppression remedy modelled on s. 241 of the CBCA, except that the oppression remedy would apply only if the applicable declaration of trust opts-in to the remedy. The remedy would apply to conduct at the level of the income trust or at the level of any controlled subsidiary entity.**

(g) Derivative Action

[87.] There are two types of derivative actions at corporate law. The most common type of derivative action is where a shareholder (or other complainant) brings or continues an action on behalf of a corporation to enforce a corporate right. The decision on whether to pursue an action against a third party would normally be a management decision of the directors or officers of the corporation. If the directors or officers chose not to expend corporate resources on either an action against the directors or officers for breach of their fiduciary duties or an action against a third party (***e.g***. an action for breach of contract or in tort), a shareholder can seek leave to enforce the corporation's rights, the fruits of which generally accrue to the indirect benefit of the shareholders. The less common type of derivative action is where the shareholder (or other complainant) defends an action brought against the corporation. In both cases, the shareholder (or other complainant) is not enforcing a personal right or defending a personal obligation but is instead enforcing a corporate right or defending against an alleged corporate obligation.

[88.] The derivative action was introduced into corporate law[102] to overcome some of the obstacles imposed by the infamous rule in ***Foss v. Harbottle.***[103] Since a corporation is a separate legal entity, actions to enforce rights or remedies belonging to, or defend actions against, a corporation could only be brought, or defended, by the corporation itself. The authority to commence, or defend, an action resided with the board, or ultimately with shareholders as a general body. At common law, the possibility of ratification by the majority would be enough to stop a derivative action, except in limited circumstances such as where those in control of the corporation were perpetrating a fraud on the minority.[104] A derivative action is particularly useful where the alleged wrong-doers are in control of the corporation and, therefore, cannot be expected to authorize a corporate action against themselves. It is rare for a shareholder to be given leave to bring or continue an action against a third party where the exercise of business judgment by directors is untainted by self-interest.

[89.] These obstacles and issues are not precisely the same in the case of trusts. Since a trust is not a separate legal entity, there is no separate person whose interests can be pursued or defended by an investor in the trust.

[90.] Consider actions against trustees and third parties in a trust context. If trustees have committed a breach of trust, there may be no need for the beneficiaries to bring a derivative action. The duties are owed by the trustees directly to the beneficiaries. Any right of action belongs to the beneficiaries and not an artificial person that they own. The trustees are defendants. They cannot sue themselves on behalf of the beneficiaries. Where there are many beneficiaries who have been harmed by the breach of trust, the action might best be brought as a class proceeding under Provincial legislation or rules of court.[105]

[91.] Where trustees have an action against a third person on the basis, for example, of breach of contract entered into in the administration of the trust or a tort arising in the context of the trust administration, but fail to bring it, one or more of the beneficiaries might sue the trustees alleging that their decision not to bring such an action was a breach of trust (and such an action by multiple beneficiaries might be pursued as a class proceeding). The trustees might then join the third person.

[92.] Derivative actions and shareholder personal actions in representative form existed at common law but were found wanting. The statutory derivative action supplanted the common law regime and brought some certainty for investors. Likewise, a derivative action for investors in an income trust may prove salutary. It would give unitholders a straightforward, well-recognized method of enforcing rights of the income trust and any subsidiary entities. It would enable the court to impose filters on the derivative action such as the requirements for advance notice of intent to bring the action, the ***bona fides*** of the applicant and the ***prima facie*** apparent best interests of the unitholders. Again, for reasons similar to those discussed in connection with the oppression remedy, we recommend that, at this time, the derivative action be available on an opt-in basis, leaving it for unitholders to decide for themselves whether the advantages of the derivative action outstrip any perceived disadvantages. Again, the Royal Utilities Income Fund affords a recent example of an attempt to replicate the corporate derivative action in a DOT.

Recommendation 17: The Act provide a counterpart to the corporate derivative action modelled on ss. 239 and 240 of the CBCA, except that an applicant would only have the right to apply for leave to bring a derivative action if the applicable declaration of trust opts-in to the statutory provision. Leave could be granted to bring an action on behalf of the trustees or on behalf of any controlled subsidiary entity.

(h) Dissent and Appraisal Right

[93.] According to the Goodmans Survey, unitholder dissent and appraisal rights were provided in only one out of 54 funds surveyed (or about 2% of the sample survey).[106] Even then, the DOT of that fund provided that unitholders had a dissent and appraisal right analogous to that available to shareholders of a corporation - without addressing the absence of statutory triggering events for income trusts.[107]

[94.] There may be a number of reasons for this departure from the corporate norm. There are market remedies that may be considered adequate substitutes for the appraisal right, particularly where a reporting issuer's securities are liquid. In the corporate sphere, the appraisal right has generally fallen into some disuse except where shares are thinly traded or in connection with mergers or going-private transactions. In these circumstances, the appraisal right provides liquidity where there would otherwise not be enough liquidity for the shareholder to exit the investment. Also, income trusts typically distribute most of their cash-flow. Finally, to qualify as a mutual fund trust, the DOT usually includes the right to retract at a price equal to not less than 95% of the FMV of all issued units of the trust.

[95.] The dissent and appraisal right is an expensive remedy for a shareholder to invoke, particularly where there are adequate market substitutes.[108] Thus, the dissent and appraisal right may be illusory to investors in certain types of widely-held or highly-liquid reporting issuers. On the other hand, the existence of the dissent and appraisal right may serve to limit the flexibility of certain fundamental changes that would trigger the right, such as continuances, amalgamations and certain recapitalizations.[109]

[96.] Thus, before extending the dissent and appraisal right to unitholders in income trusts on a mandatory basis, perhaps it is time to re-examine more closely where the dissent and appraisal remedy has proven useful and where it might be counter-productive. In Delaware and most other U.S. states, the dissent and appraisal right is not available to shareholders of publicly-traded corporations. Similarly, it could be argued that the conscious failure to provide an analogue of the appraisal remedy in most DOTs reflects an assessment that the remedy is value-reducing for those trusts. The remedy would be value-reducing if it constitutes an obstacle to legitimate transactions without any meaningful offsetting protections for investors.[110] Is this one instance where experience with income trusts serves to inform corporate law rather than the reverse? A final, serious difficulty is deciding what triggering events should give rise to the dissent and appraisal right. Triggering events under corporate law such as amalgamating two or more corporations, changing the restrictions on what businesses may be carried on, imposing or removing restrictions on share transfers, carrying-out going private transactions or carrying-out squeeze-out transactions may have limited analogues for income trusts and even under corporate law sometimes are counter-intuitive. Arguably, a change of governing law should only give rise to a dissent and appraisal right if it adversely affects unitholders in a substantive way – something that would be avoided if the Act were uniformly adopted.

[97.] As in the case of the oppression remedy and the derivative action, the best option, for the time being, is probably not to adopt the dissent and appraisal remedy as a universal, mandatory rule. However, if the unitholders of an income trust decide for themselves that the dissent and appraisal remedy would add value to their trust, they should be free to adopt it either on formation of the trust or by amending the DOT. Indeed, as in the case of the oppression remedy and the derivative action, demand for the dissent and appraisal right may be starting to develop in the marketplace. Consistent with this customized approach, the DOT is the place to specify the appropriate triggering events. In addition, as under corporate arrangements, the court should, as discussed further at Part V.11(a) below, have the power to extend the statutory dissent and appraisal remedy to dissenting unitholders.

[98.] If the dissent and appraisal remedy is available in the Act, trustees might choose to have it apply on a transaction-specific basis. For example, OSC Rule 61-501 (***Insider Bids, Issuer Bids, Business Combinations and Related Party Transactions***) provides an exemption from the majority-of-the-minority approval requirements for business combinations and related-party transactions where a statutory or contractual appraisal remedy is available and certain other criteria are met.

> **Recommendation 18: The Act include a general dissent and appraisal right, modelled on s. 190 of the CBCA, except that the right would apply only: (a) to the extent, and upon the triggering events, specified in the applicable declaration of trust, or, where the declaration of trust so provides, to specific transactions designated by the trustees; or (b) where specifically ordered by a court as part of a statutory arrangement.**

8. Powers and Duties of Trustees

(a) Powers of Trustees

[99.] According to the CBCA, OBCA and ABCA, the function of directors of a corporation is to manage, or supervise the management of, the business and affairs of the corporation.[111] In the case of publicly-listed corporations, the ***de facto*** emphasis is on the supervisory function.[112]

[100.] Trustee functions, duties, liabilities and immunities are critical subject matters for the UITA. It is as important for maximizing enterprise value that income trusts attract committed, honest and capable trustees as it is that corporations attract and retain committed, honest and capable directors.

[101.] As a general principle, the Act should seek parity for trustees with the functions, duties, liabilities and immunities of corporate directors. The investment community would benefit through consistency and ease of understanding. Boards and trustees would benefit from having substantially the same or similar roles and obligations, the same exposure to liability and the same indemnification rights. If parity were achieved, income trusts would be in the same position in recruiting and retaining trustees as corporations are with respect to recruiting and retaining directors.

[102.] On the other hand, the liability and immunity regime for trustees should not be designed to go further, protecting trustees beyond the level of protection afforded corporate directors. The objective should be to level the playing field between trusts and corporations, not to tilt the balance in favour of trustees. Thus, for example, the UITA should not permit DOTs to cap the liability of trustees for misfeasance, unless Canadian corporate legislation begins to allow corporate charters to so cap the liability of directors of publicly traded corporations.[113]

[103.] Unlike most publicly traded corporations, most income trusts are not direct operating entities. Rather, the typical income trust merely holds property consisting of shares, debt obligations, real estate, intellectual property or other assets that generate income from property. Akin to directors, therefore, trustees should have power to manage, or supervise the management of, the property (not the business) and affairs of the trust. A similar formulation has, in the corporate realm, accommodated the widest conceivable variety of board-management configurations and extent of board delegation to management – a flexibility that is needed as much for income trusts as it is for publicly traded corporations.

(b) Power of Unitholders to Bind Trustees

[104.] Under the CBCA, directors have the power to manage, or supervise the management of, the business and affairs of the corporation.[114] Thus, under corporate law, directors, not shareholders, are entrusted with managing or supervising the management of the business and affairs of the corporation. Shareholders cannot generally pass resolutions that bind the board.[115] The remedy of shareholders is to replace the directors.

[105.] By contrast, at least until recently, many DOTs provided that unitholders have the power, in certain cases, to bind trustees. In some cases, for example, unitholders have been given the explicit power to direct trustees to sell all or substantially all of the assets of the underlying entity or to direct trustees how to vote the securities in the underlying operating entity. Such a division of powers arguably creates an anomalous split in the authority-responsibility chain. Trustees are legally responsible for administration of the trust but lack authority to the extent they must act in accordance with a unitholder directive. Unitholders have, to this extent, authority to act but no legal responsibility to consider any factors other than their own interests.

[106.] One view is that the division of powers between trustees and unitholders should parallel that in corporations. Such a division would be consistent with the expectations of the marketplace. The opposing view is that the division of powers between unitholders and trustees is fundamentally an issue of freedom of contract as expressed in the DOT for that trust.

[107.] It appears that, given recent experiences, new trusts are less likely than in the past to be created to give unitholders the power to bind trustees.

[108.] If a rule were adopted requiring DOTs to conform to the corporate model, many current trusts would be non-compliant. Further, a rule requiring conformity to the corporate model would take away the rights of unitholders, thereby undermining unitholder autonomy.

[109.] On balance, the UITA should not lightly override or alter existing unitholder rights (particularly to take away possible unitholder rights) or force the amendment of DOTs. Instead, the recommended solution is to provide mandatory rules to the effect that trustees have the power to manage, or supervise the management of, the property and affairs of the trust, but that unitholders cannot direct or mandate action by trustees. While unitholders may have the power to approve certain transactions (such as a sale of all or substantially all of the property of the trust), they could no longer direct or compel trustees to act. These mandatory rules would not apply to income trusts formed in the

Province before the effective date of Act. Grandfathered trusts would of course be free to opt-in to the rules through DOT amendment.

> **Recommendation 19: The Act set out mandatory rules whereby trustees of an income trust have the power to manage, or supervise the management of, the property and affairs of the income trust and, similarly, trustees of a subsidiary trust have the power to manage, or supervise the management of, the property and affairs of the subsidiary trust. In addition, unitholders would no longer have the power to direct or compel the trustees to take particular actions. These provisions would not apply to trusts formed in the Province before the Act goes into effect.**

(c) Delegation of Powers

[110.] As a general rule, the CBCA gives broad authority to directors of a corporation to delegate their powers to a managing director or a committee of directors.[116] There are various exceptions to the general power to delegate that are peculiar to corporations, including the authority to submit questions to shareholders, fill a vacancy in the board, issue shares in series, declare dividends, purchase or redeem shares and adopt, amend or repeal by-laws.[117]

[111.] The power to delegate is also important in the case of income trusts. As stated more fully at Part II above, trustees may delegate their powers to internal management, to committees of trustees or to external, or third party, managers. In the latter case, trustees enter into a management agreement setting out the rights and obligations of the parties, including the compensation of the external manager. There tends to be a much greater variety of management arrangements in the case of income trusts than prevail in the case of publicly traded corporations. For example, as at the date of the Goodmans Survey, more than 90% of power and pipeline income trusts had external management while most other income trusts have internal management.[118] Management arrangements are generally settled before the trust acquires assets or offers units to public investors.[119] Thus, management arrangements tend to be highly customized to fit the circumstances of the particular trust, and the timing of the management arrangements necessarily meets the expectations of initial and subsequent investors who buy into the trust.

[112.] The UITA should codify the power of trustees to delegate their powers to internal management, a committee of trustees or an external manager. However, given the significant variance among trusts in their management arrangements, there should be few exceptions to the general power to delegate. The exceptions ought to be analogous to the non-delegable powers of a CBCA corporate board. However, unlike a corporate board, trustees should be able to delegate the power to issue or repurchase units (shares in the case of a corporation). A rule prohibiting the right to issue or repurchase units would make many existing DOTs non-compliant.

> **Recommendation 20: The Act codify the power of trustees of an income trust or a subsidiary trust to delegate any part of their authority to internal (including a committee of trustees) or external management. There will be certain non-delegable powers, *viz.*: submitting questions for the approval of unitholders; appointing or removing trustees except to fill vacancies or as otherwise provided in the Act; appointing or removing an auditor; approving management information circulars; and approving audited financial statements. Trustees would be able to delegate the power to issue or repurchase units in the trust. These rules will not apply retroactively to income trusts or subsidiary trusts that were formed before the Act goes into effect.**

[113.] It is anticipated that securities laws will continue to require that the prospectus for an income trust disclose the material terms of external management agreements, thus informing investors and prospective investors.

(d) Duties of Loyalty and Care

[114.] The CBCA provides that:

> Every director and officer of a corporation in exercising their powers and discharging their duties shall: (a) act honestly and in good faith with a view to the best interests of the corporation; and (b) exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.[120]

[115.] The first duty is commonly referred to as the "statutory duty of loyalty". The second is commonly referred to as the "duty of care".

[116.] Recently, the Supreme Court of Canada held that, while the duty of loyalty of a director of a CBCA corporation is owed exclusively to the corporation (and not directly to other stakeholders such as shareholders and creditors), the duty of care is owed not only to the corporation but also to creditors and possibly other stakeholders.[121] We note that this decision has been widely criticized, however.[122] According to the Goodmans Survey, all DOTs surveyed adopted substantially the same duties of loyalty and care for trustees as those set out for directors and officers in the CBCA.[123]

[117.] In addition to stating that the duty of care is owed to the corporation, its creditors and, possibly, shareholders and other stakeholders, the Supreme Court also held that the standard of care of directors and officers is an objective standard analogous to the standard applicable to professionals such as lawyers, accountants, architects and surgeons.[124] We propose to adopt the subjective-objective test that applied before ***Peoples*** rather than the objective standard that the ***Peoples*** ruling now appears to impose.

[118.] A corporation is a separate legal person, while an income trust is not. Trustees of an income trust should, therefore, owe their duty of care directly to unitholders as a whole – the position both at common law and under the CCQ. Since there seems to be no compelling reason to extend the duty of care of trustees to creditors, we do not recommend that the UITA state that trustees owe a duty of care to creditors or other stakeholders.

[119.] Nor is it possible to map the fiduciary duties of trustees of an income trust onto that of corporate directors. A corporation is a separate legal person. As stated, directors owe their fiduciary duties exclusively to the corporation and not to shareholders or any other stakeholders. However, income trusts are not separate legal persons. Trustees must owe their duties of loyalty directly to unitholders as a general body. Thus, the UITA should state that the duty of loyalty and duty of care of trustees is owed exclusively to unitholders as a whole.

[120.] It is recognized that there may be theoretical differences between the duties of loyalty and care imposed on trustees at common law and the statutory duties of loyalty and care imposed on corporate directors and officers.[125] ***Prima facie***, the duties imposed on trustees may be higher than the duties imposed on directors and officers. However, the duties imposed on trustees may be varied in the DOT, whereas the CBCA (and corporate statutes modelled on the CBCA) generally prevent any lowering of the standards imposed on directors and officers.[126] For example, according to the Goodmans Survey, DOTs generally adopt CBCA standards for the duties of loyalty and care, not the stricter common law standards imposed on trustees. The implicit assumption here is that the corporate standards are more appropriate to an environment where, like corporate directors, trustees of an income trust are intended to take commercial risks, not merely to preserve the ***corpus*** of the trust. Moreover, in fashioning a special set of rules for the trustees of an income trust, we reiterate that our intention is to not derogate in any way from the duties imposed on trustees of other types of trusts.

> **Recommendation 21: The Act state that trustees of an income trust owe their fiduciary duties exclusively to unitholders as a general body and that trustees of a subsidiary trust owe their fiduciary duties exclusively to beneficiaries of the subsidiary trust as a general body.**

> **Recommendation 22: The Act also state that trustees of an income trust owe their respective duties of care exclusively to unitholders as a general body, that trustees of a subsidiary trust owe their respective duties of care to beneficiaries of the**

subsidiary trust as a general body and that, in both cases, the standard of care be to exercise the care, diligence and skill of a reasonably prudent person with comparable skills and experience.

(e) No Exculpation

[121.] The CBCA states that no provision of the articles, by-laws or unanimous shareholder agreement of a corporation or any other contract may relieve a director or officer from the requirement to act in accordance with the CBCA or the CBCR or relieve the director or officer from liability for a breach of such legislation.[127] The UITA should include a similar provision. Ensuring that the standards for trustees set out in the UITA are minimum standards that cannot be further lessened in a DOT seems a fair trade-off for importing into the UITA corporate law standards such as the duties of loyalty and care and the corporate law conflict of interest regime. It is recognized that adoption of these corporate law standards may result in a theoretical reduction in the standards that would apply to trustees in the absence of a contrary provision in the DOT.

Recommendation 23: The Act state that no provision in a declaration of trust, contract or a resolution relieves a trustee from the duty to act in accordance with the Act or relieves the trustee from liability for breach of the Act.

(f) Conflicts of Interest

[122.] Corporate legislation, such as the CBCA, OBCA and ABCA, contains a code governing conflicts of interest for directors and officers.[128] For example, the CBCA specifies that directors and officers must disclose material conflicts of interest, to whom and when the disclosure must be made, the circumstances in which directors can vote or must abstain from voting for the approval of contracts or transactions in which they are interested and what level of shareholder approval is required to approve an interested contract or transaction.[129] If all conditions are satisfied, the contract or transaction is not void or voidable, and the director or officer has no liability to account for any profit that he or she may make as a result of the contract or transaction.[130] The regime also imposes the overriding criterion that the contract or transaction be reasonable and fair to the corporation at the time that it is made.[131]

[123.] The statutory code sets out a mandatory, minimum standard. It does not preclude the corporation from adopting higher standards in its by-laws, corporate codes of conduct, executive employment agreements or management contracts.

[124.] The default conflict of interest rule that applies to trustees at common law is certainly higher than the statutory minimum standard set out in the CBCA. At common law, trustees are held to a strict duty of utmost good faith such that trustees cannot allow their own interests to conflict with the interests of beneficiaries. For example, in the ***locus classicus***, ***Keech v. Sandford,***[132] a trustee was not permitted to renew a lease in his own favour even though the lease was no longer available to him in his capacity as trustee. Trustees have been rendered liable to account for profits made even though no beneficiary suffers damages from the loss of a trust asset.[133] However, in practice, it is possible to modify the strictness of the default common law rule through exculpatory provisions in the trust instrument.

[125.] Historically, corporate law also held directors and officers to a strict standard.[134] The CBCA conflict of interest regime substitutes for a strict common law prohibition a more permissive regime with checks and balances designed to ensure that transactions in which directors and officers are conflicted simulate arm's length transactions.

[126.] According to the Goodmans Survey, all DOTs surveyed addressed conflicts of interest. However, there is a significant lack of uniformity in the versions that were adopted: 61% required trustees to disclose conflicts and abstain from voting on interested contracts; 7.5% required trustees to disclose and abstain from voting but provided limited exceptions; and 31.5% contained regimes that were otherwise less onerous than the corporate minimum.[135] Thus, more than 30% of the DOTs surveyed either had no provision comparable to s. 120 of the CBCA or contained provisions that fell below the minimum standard set out in s. 120. In the interests of uniform investor protection, the UITA should contain minimum standards comparable to those set out s. 120 of the CBCA.

[127.] If the corporate law standards applied, trustees would either have to avoid material conflicts of interest or ensure that these conflicts of interest are fully disclosed, are reasonable and fair to unitholders and receive approval either from a majority of disinterested trustees or from not less than 2/3rds of the votes cast by unitholders. Again, it is a fair trade-off to make the new regime a mandatory, minimum standard so that it is not further lowered in the DOT.

> **Recommendation 24: The Act contain a minimum conflict of interest code modelled on s. 120 of the CBCA providing that material conflicts of interest must be disclosed at the earliest moment, that, except in limited circumstances, trustees abstain from voting for the approval of contracts or transactions in which they are interested, that a majority of the disinterested trustees or not less than 2/3rds of the votes cast by voting unitholders approve the interested contract or transaction and that the contract or transaction must be reasonable and fair to the unitholders at the time that it is made. If these conditions are satisfied, the contract or transaction is not void or voidable, and the trustees have no liability to account for any profit they may make as a result of the contract or transaction. However, trustees should be**

expressly permitted to vote on their own compensation as trustees, contracts of indemnity or insurance in their own favour and contracts or transactions involving subsidiary or affiliated entities.

(g) Corporate Trustees

[128.] Under the CBCA, only individuals (***i.e.*** not corporations) can be directors.[136] Income trusts, however, have both corporate and individual trustees.[137] There appears to be no compelling reason to mandate that income trusts jettison corporate trustees in favour of individual trustees. More particularly, if an income trust chooses a corporate trustee, it should continue to have the power to choose between a corporation formed under federal or Provincial trust company legislation or, if the Provincial securities commission provides an exemption, an ordinary business corporation. The subsidiary trust should be able to have a corporate trustee that is a trust company formed under federal or Provincial trust company legislation or, provided its securities are not held by the public, that is a general business corporation. Again, in the case of a subsidiary trust, Provincial securities commissions can likely intercede to prevent a particular trustee from acting as such. Specific exemption applications to securities regulators would be required if the income trust is to have a corporate trustee other than a federally-licenced or Provincially-licenced trust company.

[129.] In effect, the corporate trustee of an income trust would have to be a trust company unless the Provincial securities commission specifically allows an ordinary business corporation to act, while a corporate trustee of a subsidiary trust could be an ordinary business corporation unless the Provincial securities commission, acting in the public interest, orders otherwise. The trustees of the parent income trust would still have to exercise care in selecting the trustee of any subsidiary trust, thereby protecting the interests of public unitholders. To facilitate flexibility in the appointment of corporate trustees for income trusts and subsidiary trusts, Provincial trust company legislation may have to be amended to expressly allow ordinary business corporations to act as trustees of income trusts or subsidiary trusts.[138] The UITA is only enabling legislation. It would not override Provincial laws regulating the operation of corporations offering their services to the public as trustees.

Recommendation 25: The Act confirm that trustees of an income trust or a subsidiary trust can consist of individuals or corporations. An income trust may have a corporate trustee that is a trust company or, if the Provincial securities regulator grants a specific exemption, an ordinary business corporation. The corporate trustee of a subsidiary trust may, provided its securities are not held by the public and the Provincial securities regulator does not order otherwise, be any

corporation formed under the laws of Canada or any Province, not necessarily a licenced trust company.

9. Trustee Liability and Indemnification

(a) Statutory and Contractual Liability

[130.] Trustee liability is another important subject for the UITA. Again, for reasons stated at Part V.8(a) above, the UITA should seek to establish parity between the liability regimes applicable to trustees and corporate directors.

[131.] Under corporate law, directors are generally not liable for the debts and obligations of the corporation, which, again, is a separate legal person. Despite the general rule, there is a large body of federal and provincial statute law (often criticized as being too onerous)[139] that imposes liabilities (and frequently strict liabilities) on directors of corporations in a wide variety of circumstances. In these instances, while the corporation is primarily liable for the underlying claim, directors have secondary liability. All directors can be sued with respect to the corporation's obligation, but the directors generally have a right of indemnification from the primary obligant, the corporation, and a right of contribution from the other directors. Examples of statutory liabilities imposed on directors include: (i) unpaid wages and other debts owing to employees;[140] and (ii) withholding taxes under the ITA,[141] unpaid contributions under the ***Canada Pension Plan,***[142] unpaid employment insurance premiums under the ***Employment Insurance Act,***[143] unpaid GST remittances under the ***Excise Tax Act***[144] and unpaid remittances under some provincial sales tax regimes.[145] Unlike U.S. securities laws, Canadian securities laws are arguably unclear as to whether trustees are in fact the issuer, which is a matter that should also be rectified.[146]

[132.] To place trustees in approximately the same position as directors, the general liability of trustees should be limited to the trust assets, and trustees should have a right of indemnification out of those assets, subject to very limited qualifications. So, for example, if trustees enter into a contract on behalf of the trust, then, even in the absence of language in the contract limiting the liability of trustees, their liability should be limited to the assets of the trust.

[133.] Except in instances where directors would be personally liable (such as for unpaid employee wages and source deductions), trustees should not incur liability beyond the assets of the trust. Trustees should continue to have direct liability for unpaid employee wages and source deductions, as there is no other primary obligant. In these instances, the trustees would have a right of indemnification out of the trust assets, but their liability could not be limited to those assets without making trustees better off than unindemnified directors.

> **Recommendation 26: Unless the debt instrument or other contract expressly states otherwise, the liability of trustees of an income trust or a subsidiary trust under any debt instrument or other contract expressly entered into in their capacity as trustees be limited to the *corpus* of the trust. This rule does not apply retroactively to debt instruments or other contracts entered into by trustees in their capacity as such. Nor does it derogate from an exclusion or limitation of liability contained in any debt instrument or other contract whether entered into before or after the Act becomes effective.**

[134.] While, in theory, the proposed default rule would constitute a change in the law, the change is not significant in practice, as it is consistent with prevailing practices in which trustees of income trusts generally limit their liability by contract to the ***corpus*** of the trust.

(b) Tort Liability

[135.] The liability of directors, officers and employees for tortious conduct engaged in by them while acting on behalf of a corporation is in a state of confusion. A line of authority had held that, for such liability to attach, the plaintiff had to establish a degree and kind of personal involvement by the director, officer or employee that made the wrongful conduct the employee's own.[147] Other courts have required employees to have acted outside their corporate character for liability to attach.[148] Still other courts have required that the conduct constitute a tort separate and apart from the employee's duties to the corporation.[149] In ***ADGA Systems International Ltd. v. Valcom Ltd***.,[150] the Ontario Court of Appeal held that any director, officer or employee is personally liable for tortious conduct that he or she engages in even where that conduct is carried out solely for the benefit of the corporation and pursuant to that individual's employment with the corporation.

[136.] In the two most recent Supreme Court of Canada decisions, ***London Drugs Ltd. v. Kuehne & Nagel International Ltd***.[151] and ***Edgeworth Construction Ltd. v. N.D. Lea & Associates Ltd***.,[152] the Court appears to support a broader principle of employee or agent immunity from liability.[153] In ***London Drugs***, a limitation of liability clause in the corporate defendant's contract with its customer was extended to implicitly protect the employees of the corporate defendant. In ***Edgeworth***, individual engineers of the negligent corporate employer were held not to owe a separate duty of care, as individuals, to the plaintiff. What appears to be underlying these Supreme Court decisions is a principle that, where third parties voluntarily deal with an entity such as a corporation, these parties should not have recourse against individual employees or other agents of the entity in the case of mere negligence. Analogously, the law has long held that a party who contracts with a corporation can have no claim for inducing breach of contract against corporate officers or agents who cause their corporation to breach its contract.[154] Even though it may take time for the courts to clarify the law on the liability of directors, officers and employees for tortious conduct engaged in by them while acting for their corporation, in principle, trustees should be put in as a similar position to directors as possible.

> **Recommendation 27: Trustees of an income trust or subsidiary trust be placed in a similar position as directors insofar as it relates to their liabilities in tort. Recourse against trustees for claims sounding in tort would be limited to the *corpus* of the trust if, in the same circumstances, a director would not be personally liable for the tort committed. Conversely, the liability of trustees would not be limited to the *corpus* of the trust if, in the same circumstances, a director would be personally liable for the tort. These rules would not apply retroactively and would not apply to statutory liability such as for breach of the duties of loyalty or care set out in the Act or for misrepresentation under securities legislation.**

[137.] The foregoing rules would roughly level the playing field between trustees/directors, on the one hand, and unitholders/shareholders, on the other. Unitholders would continue to be protected by fiduciary duties and the duty of care applicable to trustees and by other relevant legislation (such as liability for prospectus and continuous disclosure misrepresentation in securities legislation).[155] In addition, recourse against trustees would not be limited to the assets of the trust where, in analogous circumstances, a director would be held personally liable as a tortfeasor.[156]

(c) Indemnification

[138.] As stated at Part V.8(a) above, trustees should have a general right of indemnification out of trust assets. Indemnification should be unavailable only if the trustee was not acting honestly and in good faith with the view to the best interests of the unitholders as a whole or, in the case of a criminal or administrative proceeding enforced by a monetary penalty, the trustee had no reasonable grounds for believing that his or her conduct was lawful.[157] Indemnification should not depend on whether the trustee complied with the DOT. Rather, like directors under the CBCA, trustees should have a right to indemnification if they do not run afoul of the foregoing conditions and are not adjudged, by a court or other competent authority, to have committed any fault or omitted to do anything that they ought to have done.[158]

[139.] Adoption of such a rule would place trustees in approximately the same position as directors. Indemnification of trustees will not, in practice, amount to a significant departure in the law or enrich trustees at the expense of unitholders. Nevertheless, indemnification is particularly important in the case of trustees to the extent that their liability is primary, not secondary. Indemnification is also important to ensure that income trusts continue to attract the best trustees available.

> **Recommendation 28: Trustees of an income trust or a subsidiary trust have rights of indemnification out of trust assets similar to those available to directors under the CBCA, provided that the trustees comply with their fiduciary duties and, in the case of criminal or administrative proceedings enforced by a monetary penalty, have reasonable grounds to believe that their conduct is lawful. If these conditions are satisfied, a trustee would have the right to be indemnified so long as the trustee was not found by a court, or other competent authority, to have committed any fault or omitted to do anything that he or she ought to have done. The right to indemnification would not be lost solely because the trustee failed to comply with the declaration of trust. Trustees would also be entitled to the advance of defence costs but would have to repay the advance if subsequently found to have not satisfied the conditions for indemnification.**

(d) Insurance

[140.] The CBCA has removed any limitations on the insurance that a corporation can purchase on behalf of its directors and officers, leaving it to the insurance marketplace to regulate the scope of permitted coverage.[159] Likewise, the UITA should permit trusts to acquire insurance for trustees free of any statutory restrictions. Like directors, trustees should be permitted to vote on the approval of insurance even though it clearly involves a conflict of interest.[160] Insurance is part of the matrix of protection designed to attract the best trustees available.

> **Recommendation 29: The Act expressly permit trustees of income trusts or subsidiary trusts to approve the purchase of liability insurance out of trust monies and to vote thereon despite the conflict of interest.**

(e) Resignation

[141.] Corporate directors are free to resign at any time.[161] Finding replacement directors is a problem for the remaining directors or shareholders, not for the director who resigns.

[142.] Trustees are not generally able to resign until a replacement trustee is appointed – generally concurrently. The inability to resign could pose a significant problem should a trust be on the verge of insolvency. The incumbent trustees would want to resign in order to minimize their personal liability for statutory obligations such as wage payments to employees, withholding taxes and environmental claims. However, at that point, no responsible person could be expected to step into the shoes of the resigning trustee. Nor is it fair to allow some trustees to jump a sinking ship at the expense of the last trustee on board. Accordingly, the last trustee should be permitted to resign in favour of the prior or concurrent appointment of a trustee in bankruptcy, receiver or receiver-manager of the trust estate.

> **Recommendation 30: The Act provide that trustees are free to resign at any time provided that at least one trustee remains. The last trustee of an income trust or subsidiary trust be permitted to resign at any time if: (a) approved by the court; or (b) on or after the appointment of a trustee in bankruptcy, receiver, receiver-manager or interim receiver to administer the whole, or substantially the whole, of the assets of the trust.**

[143.] Provincial ***Trustee Acts*** may contain provisions applicable where a trustee wishes to resign and there are difficulties appointing a successor trustee.[162]

10. Unsecured Creditors and Claimants

[144.] Currently, the status at common law of the claims of unsecured trade creditors, other unsecured creditors and claimants with unliquidated claims against a trust is unclear.[163] The unsecured creditor or claimant appears to have no claim against the trust assets ***per se*** because, again, the trust is not a separate legal person. According to this theory, an unsecured creditor or claimant only has a claim against the trustees.[164] Creditors and claimants may have an indirect claim against trust assets through the doctrines of subrogation or specific performance or other legal theories.[165] There remains much uncertainty in Canadian common law on these points, however.

[145.] The UITA should resolve these issues in a manner consistent with the legitimate expectations of creditors and other claimants that have business dealings directly with an income trust or subsidiary trust. The Act should also meet the legitimate expectations of trustees and unitholders. Thus, unsecured creditors and claimants should be able to look directly to the assets of the trust, should have no right to recover from unitholders directly and should only have recourse against assets of trustees outside the ***corpus*** of the trust in circumstances analogous to those in which a creditor can look to directors personally. These circumstances include fraud, breach of warranty of authority or personal commission of an independent tort (such as a negligent misstatement made outside the scope of his or her duties) but not a duty of loyalty to creditors or a breach of contract claim between the creditor and the trust. Clarifying that third parties have recourse directly against trust assets is the reverse-side of the proposals regarding liability of trustees and trustee indemnification out of trust assets. Secured creditors, ***ex hypothesei***, will have protected themselves by taking security in the trust assets.

> **Recommendation 31: The Act declare that unsecured creditors, including unsecured trade creditors and persons with unliquidated claims, of an income trust or a subsidiary trust have a direct unsecured claim against the *corpus* of the trust subject to the terms of their claim.**

[146.] We add a caveat to the above recommendation. We would want to revisit the recommendation if a plausible argument is made that the recommendation, if implemented, might adversely affect the tax characterization of income trusts.

11. Statutory Mergers

(a) Arrangements

[147.] It is clear that OSC Rule 61-501 and Quebec's Q-27 apply equally to corporations and trusts that are reporting issuers in these Provinces. However, these pieces of subordinate legislation have two fundamental limitations. First, they are limited to reporting issuers in these Provinces and, therefore, do not provide ***de jure*** national coverage. Second, they are limited by type of underlying transaction. For example, OSC Rule 61-501 only applies to related party transactions, business combinations, insider bids and issuer bids.

[148.] It would be useful for trusts to enjoy a statutory arrangement provision similar to s. 192 of the CBCA. Section 192 allows a court to approve arrangements involving CBCA corporations. Among other things, statutory plans of arrangement have been extremely useful in implementing mergers involving publicly-traded target corporations. Notably, statutory arrangements have also been useful in converting corporations into trusts.

[149.] Currently, however, there is no analogous statutory regime applicable to trusts ***per se***. Rather, efforts are sometimes made to shoe-horn trusts into statutory corporate arrangements by involving subsidiary corporations. Adoption of a statutory arrangement provision for trusts would facilitate transactions while, simultaneously, ensuring court protection of the interests of minority or dissenting unitholders. Arrangements are useful in complex transactions, such as tax-driven transactions or transactions where exemptions are needed under U.S. securities laws. As in the case of corporations, the court would have the power to make interim and final orders, appoint independent counsel, convene meetings of unitholders, approve arrangements that receive the necessary approvals and are fair and reasonable, and exercise discretion to make the appraisal remedy available to dissenting unitholders.[166]

Recommendation 32: The Act include a statutory arrangement provision modelled on s. 192 of the CBCA empowering the court to approve arrangements that effect fundamental changes in the affairs of an income trust provided that the arrangement satisfies the statutory conditions and the fair and reasonable test. A trust arrangement would become effective in accordance with the terms of the court order.

[150.] Unlike corporate arrangements, trust arrangements would not involve the filing of articles of arrangement in any public office. Accordingly, a trust arrangement would have to become effective in accordance with the terms of the court order (which may call for a filing with the court on behalf of the trust to effect the underlying transaction). The trustees should be given discretion not to close the underlying transaction if unexpected problems arise. Also, the CBCA (and some Provincial corporate statutes modelled on the CBCA) automatically disqualify a corporation from effecting a statutory arrangement if the corporation is insolvent. However, this requirement is now routinely circumvented by forming a solvent corporate applicant to effect an arrangement involving an insolvent corporation and, is, therefore, not an obstacle to be duplicated in the UITA.

(b) Reorganizations

[151.] Another CBCA provision that, in recent years, has proven to be a useful tool for certain transactions is s. 191, the statutory reorganization provision. Section 191 is commonly used in insolvency contexts as a companion or supplement to a plan of arrangement under the CCAA or a commercial proposal under the BIA. In particular, s. 191 has been used to extinguish shares that have become worthless or consolidate shares that have little residual value.

Recommendation 33: The Act include a statutory reorganization provision modelled on s. 191 of the CBCA empowering the court to amend declarations of trust, authorize the issue of debt obligations or appoint additional or replacement trustees where the court has made an order in respect of the income trust under the *Bankruptcy and Insolvency Act* (Canada) or the *Companies' Creditors Arrangement Act* (Canada). Again, the reorganization would become effective in accordance with the terms of the court order.

(c) Compulsory Acquisitions

[152.] Under corporate law, a compulsory purchase is a transaction in which, following a successful take-over bid of 90% or more of the minority-held shares of a target corporation, the successful bidder may expropriate the dissenting minority interest.[167] Compulsory purchases are provided for under Part XVII of the CBCA and Part XV of the OBCA. A mechanism to cash-out the interests of dissenting shareholders is important in striking a balance between the interests of the majority and the interests of the minority. Apart from transactions to which OSC Rule 61-501 and Q-27 apply, securities laws do not provide a mechanism to cash-out the interests of dissenting unitholders.

[153.] In practice, compulsory purchases are not used frequently, particularly in light of OSC Rule 61-501 (and its immediate predecessor, OSC Policy Statement 9.1) and, in the case of corporations, the statutory arrangement mechanism.

[154.] Compulsory acquisitions following a take-over bid are generally addressed in DOTs – typically as an analogue of s. 206 of the CBCA. Also, if a statutory arrangement provision is provided for trusts, the need for a compulsory acquisition regime to effect friendly take-overs diminishes. However, a compulsory acquisition must still be used to eliminate the minority in the case of a hostile take-over bid. Also, some DOTs contain compulsory acquisition mechanisms that have been unworkable,[168] and most DOTs do not allow a dissenting unitholder to seek fair value in court. Hence, to provide uniformity of treatment, to ensure that all trusts have workable compulsory acquisition provisions particularly in hostile bid situations and to reduce the length of DOTs, a compulsory acquisition regime patterned after s. 206 of the CBCA should be included in the UITA. Any dissenting offeree would also be entitled to challenge the fair value of the buyout price.

> **Recommendation 34: The Act include a compulsory acquisition provision to facilitate take-over bids for all units of income trusts patterned after s. 206 of the CBCA. A dissenting offeree would be entitled to challenge the fair value of the offeror's buyout price.**

(d) Compelled Acquisitions

[155.] Under corporate law, a compelled purchase is the countervail of a compulsory purchase.[169] In a compelled purchase, a shareholder whose interest was not acquired as part of the successful bid for 90% or more of the shares may force the bidder to acquire the shareholder's interest.[170] Again, while minority shareholders do not appear to invoke the compelled purchase provision often, the true measure of its value may be in its disciplining effect. To ensure that unitholders enjoy at least the same level of protection as minority shareholders of publicly traded corporations, the UITA should contain a provision similar to s. 206.1 of the CBCA. Section 206.1, which was only introduced as part of the reform of the CBCA that took place in late 2001, provides that a dissenting offeree has the right to compel the offeror under a take-over bid to acquire his or her minority interest. As under the CBCA, once the take-over bid receives 90% acceptance (excluding shares held by the bidder or affiliates or associates of the bidder), the unitholder triggering the forced purchase should only be able to do so on the terms of the successful take-over bid.[171] The unitholder should not have the right to contest price where arm's length unitholders representing 90% or more of the relevant units have accepted that price. Finally, like the CBCA but unlike the OBCA, only in an issuer bid would the target trust be required to purchase the units of the minority. In other circumstances, the minority could force the third party offeror (rather than the target trust) to purchase the units.

> **Recommendation 35: To protect minority unitholders in a change of control transaction, the Act contain a compelled acquisition provision patterned after s. 206.1 of the CBCA.**

12. Conflict of Laws

(a) Choice of Governing Law

[156.] It is important that the UITA provide a simple, clear, certain conflict of laws rule so that investors know what law applies to their particular trust. In the case of corporations, the rule is clear in that a corporation must be incorporated under a particular corporate statute. However, as discussed as Part VI.1 below, it is not proposed here that the UITA provide for registration of a DOT with any governmental agency or that any governmental agency (other than Canada Revenue Agency under the ITA) formally recognize the existence of the trust. As a reporting issuer, a trust is already recognized and required to make initial, periodic and other continuous disclosure filings with the Provincial securities commissions in those Provinces in which it is a reporting issuer.[172]

[157.] In the absence of a registration requirement, the UITA should recognize, as the law governing the trust, the law expressly chosen as the governing law in the DOT.[173] In the remote case in which a DOT does not contain an express choice of law provision, a fallback rule is needed. Given the sparse jurisprudence, it is proposed that the UITA adopt as its fallback rule the place where the administration of the trust is principally carried out, which is the same fallback rule recommended in the conflict of laws proposals for Provincial Personal Property Security legislation.[174] A fallback rule focused on the place in which administration of the trust is principally carried out will be much easier to apply than the cluster of close connection factors provided for in the ***Hague Convention on the Law Applicable to Trusts and their Recognition*** (Hague Convention).[175]

> **Recommendation 36: The Act set out express conflict of laws rules to determine the governing law of an income trust, a subsidiary trust or an ordinary mutual fund. If the declaration of trust sets out a law governing the trust instrument, that law will be the governing law of the trust. If the declaration of trust omits a choice of law provision, the governing law will be the place where the administration of the trust**

is principally carried out. Each Province is to give reciprocal recognition to a declaration of trust choosing the law of a sister Province.

[158.] Uniform adoption of the UITA across Canada would ensure that a trust formed in one Province would receive recognition in another Province. An identical unitholder liability shield across the country would diminish the practical importance of any conflict of laws rules. Investors could invest with the same degree of confidence as they now enjoy when investing in a corporation, regardless of whether the corporation is incorporated under federal or Provincial statute. Unitholders in income trusts and ordinary mutual funds are entitled to the same degree of certainty and uniformity. Likewise, trustees are entitled to the same degree of uniformity and certainty of treatment with respect to liability exposure, regardless of which Province's laws govern the trust.

(b) Change of Governing Law

[159.] Similarly, unitholders should be entitled to change the governing law of the trust to another jurisdiction, a potentially important tool for achieving flexibility (although one that will likely not matter much if substantial uniformity is achieved).[176] Generally, DOTs provide that a fundamental change requires the approval of unitholders holding not less than 2/3rds of the votes cast thereon.[177] Given the importance to unitholders of the trust's governing law (particularly if the trust can be exported to a foreign jurisdiction), we recommend that the 2/3rd approval threshold be imposed as a minimum requirement in the Act.

Recommendation 37: The Act specify that, in addition to any other requirement provided for in a declaration of trust, holders of not less than 2/3rds of units voted may change the governing law of an income trust, subsidiary trust or ordinary mutual fund to another Province or jurisdiction. A declaration of trust may provide a greater, but not lesser, approval threshold.

(c) LPs

[160.] For analogous reasons and subject to the more detailed considerations of the ULCC working group on partnership law being chaired by Professor Heavin,[178] the liability shield available to investors in LPs should apply uniformly throughout the country. An LP formed in one Province, and the rules applicable to it, should be recognized in another Province. The comments at Parts V.12(a) and (b) above[179] with respect to determining or changing the governing law of the income trust or ordinary mutual fund appear to us to apply with equal force to relying on the Province where the LP is registered to determine or change the governing law of an LP. Adoption of such a rule is again consistent with the recommendations relating to LPs of the PPSL Subcommittee.[180]

VI. Issues Not Considered Appropriate for the UITA At This Time

[161.] In addition to the issues that the UITA ought to address as discussed at Part V above, we also considered many other areas that, for one reason or another, we concluded should not be dealt with in the UITA at this time. Some of these, such as excluding unitholder liability under agency theories and capping the liability of trustees for misfeasance have been discussed at Part V above. As well, there are other areas that, while eligible for consideration, do not, for various reasons, warrant specific legislative treatment in the UITA at this time. It is important that this report provide reasons explaining our rationale for recommending that certain topics not be dealt with at this time in the UITA.

1. Registration

[162.] Contrary to the law for corporations and LPs, we do not recommend that any separate registration or public filing be required in order to create, or maintain, an income trust - apart from the disclosure filings required under prevailing Provincial securities laws. Registration would be pointless and would necessitate the creation of a new public filing system for a small set of issuers.

[163.] First, as reporting issuers, income trusts must file their DOTs and any amendments thereof (as well as other information) on SEDAR.[181] Arguably, SEDAR supplants the need for a Provincial filing to create or establish the income trust. SEDAR is a web-based information retrieval database, is free to users and does not impose an incremental cost on Provincial taxpayers. Moreover, SEDAR is not jurisdiction-dependent. Hence, unlike searches conducted on provincially-formed corporations or LPs, a search conducted on SEDAR is one-stop.

[164.] Second, parties generally conduct business with the general partner of the underlying LP or the management of an underlying corporation rather than directly with the income trust. Thus, a registration is not necessary to protect unsophisticated transacting parties, contrary to what is arguably needed in the case of small corporations and LPs.[182]

[165.] Third, imposing a registration scheme similar to that which exists for corporations would be corporation-like and might adversely affect the tax characterization of the income trust.[183]

[165.] Thus, the UITA ought to apply exclusively on the basis of the status of the trust as a reporting issuer under Provincial law. In that respect, the formation of income trusts would be more analogous to general partnerships than to corporations or LPs.[184]

Recommendation 38: No registration or additional filing be required under the Act to create or recognize an income trust.

2. Matters Adequately Covered Under Securities Legislation

[166.] The working group recommends that the UITA not deal with matters that are adequately covered under securities laws or under substantially all DOTs. While there is some overlap between corporate and securities legislation, it is not considered desirable that the UITA add duplication and confusion or, conversely, risk the imposition of inconsistent rules.

(a) Mergers and Take-over Bids

[167.] Provincial legislation such as Part XX (***Take-over Bids and Issuer Bids)*** of the OSA[185] already applies to income trusts because trusts are included in the definition of "person" and, therefore, fit within the definitions of "issuer" in s. 2(1) and "offeree issuer" in s. 89(1). Thus, the statutory code for take-over bids and issuer bids in the OSA and comparable Provincial securities legislation applies to income trusts. If there are any deficiencies in the applicable law, these should be addressed in amendments to securities law, not in the UITA.

[168.] However, as discussed at Part V.11(a) above, mergers, especially friendly mergers, might be facilitated through adoption of a statutory arrangement provision for income trusts. Court-ordered reorganizations of income trusts could be facilitated through adoption of companion reorganization provisions akin to s. 191 of the CBCA. Likewise, as discussed at Parts V.11(c) and (d) above, compulsory and compelled acquisition rules have no counterpart in securities laws and, therefore, might also be adapted for purpose of the UITA.

(b) Insider Trading

[169.] Provincial securities legislation governs insider trading,[186] the filing of insider trading reports[187] and insider liability.[188] Again, insider liability applies to persons who are insiders of "issuers". If there are any deficiencies in the insider trading reporting or liability regimes as applied to income trusts, these should be addressed through amendments to securities legislation, not in the UITA.

(c) Continuous Disclosure

[170.] Securities legislation such as Part XVIII (***Continuous Disclosure)*** of the OSA governs continuance disclosure of material changes. For example, a reporting issuer, which includes trusts that are reporting issuers, must, among other things, file regular financial reports and also must issue and file press releases disclosing the nature and substance of any material changes.[189] Again, if there are any deficiencies in the application of the continuous disclosure regime to trusts, these should be addressed in amendments to securities legislation.

(d) Unitholder Meetings, Including Notices

[171.] While Provincial securities laws do not provide for annual meetings, they do provide for a default proxy solicitation regime where a meeting is held, and annual meetings are almost invariably required under DOTs.[190] In addition, N.I. 51-102 provides for the filing of financial statements,[191] circulation of management discussion and analysis forms[192] and filing of annual information forms.[193] It also provides for proxy solicitation[194] and information circulars.[195] The regime applies equally to trusts and corporations (except to the extent that the applicable corporate law provides a comparable regime).[196]

(e) Audits

[172.] Securities laws require that every annual financial statement of a reporting issuer (including a trust) be accompanied by the report of an auditor.[197] Further, securities laws, such as N.I. 51-102, require the public filing of audited financial statements on SEDAR. Once again, there is little need to replicate these requirements in the UITA.

(f) Audit Committees

[173.] Multilateral Instrument 52-110 (***Audit Committees***) governs the composition, duties and authorities of audit committees. With limited exemptions for U.S. listed issuers and venture issuers, M.I. 52-110 applies to all reporting issuers, including trusts.[198]

> **Recommendation 39: To avoid unnecessary duplication and confusion, the Act not cover insider trading, continuous disclosure, unitholder meetings, notices of unitholder meetings, proxy solicitation, appointment of auditors, audits, dissemination of audited financial statements, the composition and functions of audit committees, mergers or take-over bids (except to the extent that the Act includes provisions on statutory arrangements, insolvency reorganizations, compulsory acquisitions and compelled acquisitions).**

3. Matters Adequately Covered under Declarations of Trust

[174.] The Goodmans Survey indicates that there are some areas where DOTs are almost completely uniform, from which we draw the inference that there would be little point to codifying their provisions. One of the perceived advantages of the income trust structure has been its relative flexibility as compared with corporations. It may be premature, or unwise, to introduce legislation seeking to dictate the substantive content of DOTs – particularly in areas where there would be much effort for little gain. We see the purpose of the UITA as filling gaps in trust law insofar as it applies to the new world of income trusts. We do not see that its purpose is to replicate the whole of corporate law for income trusts. However, we recognize that a case can also be made for codifying standard provisions in the statute and that, therefore, the dividing line between what provisions to include or exclude from the Act may need to be revisited from time to time as experience with the new Act is gained.

(a) Voting Rights

[175.] For example, the CBCA establishes, in effect, an opt-out rule whereby each share entitles the holder to one vote except where the articles otherwise provide.[199] Articles so provide where appropriate. Thus, corporations can, for example, issue non-voting, subordinate voting or multiple voting shares. All DOTs included in the Goodmans Survey have substantially the same provision, entitling a holder to exercise one vote per unit.[200] There are variances, however, which may be appropriate in certain cases. Apart from enshrinement of the equality principle as discussed at Part V.6(a) above, codifying the law would, therefore, add nothing.

(b) Termination

[176.] Under the CBCA, the voluntary liquidation of a solvent corporation requires the approval of not less than 2/3rds of the shares voted for each class of shares.[201] Voluntary liquidations of publicly traded corporations are rare. In the usual DOT, termination of a trust requires a resolution passed by a special majority of unitholders, which, again, is usually not less than 2/3rds of all units voted.[202] Accordingly, trust termination does not need to be addressed in the UITA, as it appears to be adequately dealt with in DOTs.

(c) Amendments to Declarations of Trust

[177.] Similarly, under Part XIV of the CBCA, most fundamental changes (including changes to share capitalization, continuances, amalgamations and the sale of all or substantially all of the property of the corporation) require a special resolution, which is defined as not less than 2/3rds of those shares voted thereon.[203] In some cases, holders of not less than 2/3rds of each class or series of shares must approve the fundamental change.[204] However, changes to corporate by-laws are generally made by the directors, subject to later confirmation by a simple majority of voting shareholders. By-law amendments do not give rise to dissent remedies.

[178.] According to the Goodmans Survey, there is some variance with respect to the approval of fundamental changes in income trusts.[205] For example, in the case of the sale of all or substantially all of its assets, all the DOTs surveyed as part of the Goodmans Survey were substantially consistent with the CBCA except that, as discussed at Part V. 8(b) above, historically, some DOTs have made certain decisions of unitholders binding on trustees. With respect to amendments to the DOT that would change the unit structure, approximately 93% of the DOTs surveyed as part of the Goodmans Survey conformed to the CBCA model.[206] The remaining trusts surveyed allowed trustees to exercise powers to make certain changes to the unit structure without unitholder approval. It seems appropriate to allow for flexibility here, as the CBCA has proven somewhat inflexible in practice, failing to distinguish between transactions that are potentially harmful (***e.g.*** sale of substantially all assets) and those that are harmless (***e.g.*** continuance to a Province with substantively similar corporate laws). Also, DOTs contain some elements that are analogous to corporate articles and other elements that are analogous to by-laws. Accordingly, it makes functional sense to allow some DOT provisions to be amended by trustees while other, more fundamental, provisions may only be amended by a special majority of unitholders.

(d) Other Matters

[179.] Other matters that are generally well covered under trust instruments and where, therefore, there are diminishing returns in setting them out in the UITA include distributions of capital and income, qualifications of trustees, meetings of trustees and written resolutions of trustees.[207]

> **Recommendation 40: The Act not cover voting rights (except to enshrine the equality principle), termination of the trust, amendments to declarations of trust, distributions of capital and income, qualification of trustees, meetings of trustees and written resolutions of trustees of income trusts because these issues are generally adequately addressed in declarations of trust.**

VII. Conclusion

[180.] Income trusts are still a comparatively recent phenomenon in Canadian capital markets. Any new legislation dealing with income trusts must be sensitive to the distinct tax treatment that led to the rise of the income trust as an efficient vehicle for employing investment capital and operating more stable, cash-generating businesses. While, as this report indicates, there are several areas where legislation could fill in the gaps in the commercial law regime governing income trusts, there is also a need to proceed with caution. Income trusts are still young and the commercial law underpinning them is still under development. Tax laws applicable to income trusts provide comparative benefits but also impose a significant amount of discipline on trusts not found in the case of corporations.

[181.] We do not recommend simply mirroring the entire body of corporate law in the UITA for the sake of substantive uniformity without taking into full account the very different tax and commercial law character of trusts. Nor do we recommend the wholesale application of corporate law rights and remedies to the very different world of income trusts. While a strong case exists for ensuring that investors enjoy similar protections regardless of whether their investment is made in a corporation or a trust, it is equally important not to lose sight of the crucial differences between these fundamentally different investment vehicles and blindly assimilate trust and corporate law.

[182.] Some may see the recommendations set out in this report as conservative or cautious. However, we think that, at this stage, such an approach is best. The market has proven quite adept at selecting appropriate provisions to regulate trusts, while allowing for flexibility. Our recommendations here do not preclude further convergence between trusts and corporations to address any remaining important gaps and inconsistencies in the law, if the need for further convergence is demonstrated. Such convergence could occur ***via*** either law or market practice. In the meantime, the new legislation ought not to address issues that do not appear to be problematic or that do not appear to be responsive to investor demands.

THE ***UNIFORM INCOME TRUSTS ACT***

SCHEDULE A

Effect that UITA Report Recommendations Are Expected to Have on Existing Declarations of Trust ("DOTs")

Recommendation	Description	Expected Effect
1-5	Scope of Statute; Exclusion of Ordinary Mutual Fund Trusts and Foreign Trusts; and Statutory Purpose	Nil.
6	Legal Status of Trust	No change. Ensures that income trusts and subsidiary trusts are not corporations or separate legal persons - the current legal position.
7	Unitholder Immunity	Consensus view is that there is no change in the law – especially in those Provinces that have passed income trust liability legislation. Statutory provisions supplant need for provisions in DOT exempting unitholders from liability.
8	Immunity Retroactivity	Consensus view is that there is no substantive change. See comment on R7 above.
9	No Partnership Characterization	No change. Statutory provision may partly supplant need for provision in DOT stating that trust is not general partnership or LP.
10	Equality of Units; and Disenfranchisement of Controlled Subsidiaries	UITA would override any contrary provision of a DOT that disenfranchises a unitholder based on the proportion of units held. A controlled subsidiary entity would not be permitted to vote units held in the parent income trust.
11	Appointment or Election of Trustees; and Filling Vacancies	DOTs will not need to repeat the statutory provisions.

Recommendation	Description	Expected Effect
12	Removal of Trustees	UITA would override contrary provisions of a DOT that provide for removal by super-majority and/or require cause.
13	Unitholder Proposals	Few DOTs now provide for unitholder proposals. Thus, UITA would introduce unitholder proposals as a substantive right.
14	Requisitioned Unitholder Meetings	UITA would override the contrary provisions of a DOT providing that one or more holders of not less than 5% of units entitled to vote may requisition a unitholder meeting.
15	Statutory Investigations	Few DOTs provide for investigations and none are equivalent to the proposed statutory regime. UITA would introduce investigations as a new unitholder remedy.
16	Oppression Remedy	Few DOTs provide for an oppression remedy and none are equivalent to statutory regime. UITA would enable a trust to opt-in to the oppression remedy, providing a statutory framework but not compelling trusts to make it available.
17	Derivative Action	Few DOTs provide for a derivative action and none are equivalent to the statutory regime. UITA would enable a trust to opt-in to the statutory derivative action, providing a statutory framework but not compelling trusts to adopt it. The statutory derivative

Recommendation	**Description**	**Expected Effect**
		action would clarify and largely supplant comparable beneficiary actions against trustees for breach of trust.
18	Dissent and Appraisal Remedy	Few DOTs provide for unitholder dissent and appraisal rights. UITA would enable a trust to opt-in to the dissent and appraisal remedy and to define or shape the triggering events that apply. As well, in an arrangement transaction, a court-ordered dissent and appraisal right could be extended to dissenting unitholders.
19	Trustees' Power to Manage or Supervise; Inability of Unitholders to Direct Trustees How to Act	Mandatory rules subject to grandfathering in favour of trusts formed before UITA goes into effect. Trustees would have the power to manage or supervise management of the property and affairs of the trust. While unitholders would have the power to approve or veto certain transactions, they would not have the power to direct trustees on what action to take. Trustees also given extensive powers to delegate. See R20.
20	Trustees' Power to Delegate	New mandatory rule subject to grandfathering in favour of trusts formed before UITA goes into effect. UITA would set out a very short list of non-delegable matters that would override any contrary provisions of a DOT. See R20 for specifics.
21	Fiduciary Duties of Trustees	Mandatory rule, but UITA would codify prevailing

Recommendation	**Description**	**Expected Effect**
		practice in DOTs.
22	Duty of Care of Trustees	Mandatory rule, but UITA would largely codify prevailing practice in DOTs.
23	No Exculpation	New mandatory rule. Minimum statutory standards would override any lower standards set out in DOT.
24	Trustee Conflicts of Interest	New mandatory rule. Minimum statutory standards would override any lower (but not higher) standards set out in DOT.
25	Corporate and Individual Trustees	No immediate effect. Facilitates greater flexibility in using corporate trustees that are not regulated trust companies. Subject to companion changes in Provincial trust company legislation and continuing power of securities regulators to prohibit trustees from acting.
26	Trustee Statutory and Contractual Liability	Little change. UITA would codify prevailing practices in which trustees, by contract, limit their personal liability to the ***corpus*** of the trust.
27	Trustee Tortious Liability	Trustees would be put on substantially the same plane as corporate directors. Liability of trustees in tort limited to ***corpus*** of trust if director would not be personally liable for same tort. Liability of trustees in tort extends beyond ***corpus*** of trust if director would be personally liable for that tort.

Recommendation	**Description**	**Expected Effect**
28	Trustee Indemnification	No change. UITA would provide statutory underpinning for prevailing market practices in DOTs.
29	Liability Insurance	Comment on R28 above applies here as well.
30	Trustee Resignation	Supplements existing DOT provisions dealing with trustee resignation.
31	Unsecured Creditors and Other Claimants	External to DOTs, ***i.e***. clarifies the law but does not affect DOTs ***per se***. A corollary to R26 and R27. Recommendation to be revisited if someone shows that it would adversely affect characterization of income trusts for tax purposes.
32	Arrangements	New provision would facilitate, ***inter alia,*** take-overs and other complex transactions involving income trusts where, among other things, the transaction meets fair and reasonable standards. Court would have power to extend the dissent and appraisal remedy to dissenting unitholders.
33	Reorganizations	New. Would enable court to amend DOTs of insolvent income trusts.
34	Compulsory Acquisitions	UITA would provide a uniform compulsory acquisition regime and supplant existing provisions of DOTs.
35	Compelled Acquisitions	New. Few DOTs provide for a compelled acquisition right in favour of minority.

Recommendation	Description	Expected Effect
36	Choice of Governing Law	Few DOTs would omit an explicit governing law provision. Choice of governing law will now take on increased significance, as it will decide which Provincial law governs the trust.
37	Change of Governing Law	New. However, UITA would largely codify the prevailing DOT requirement for amending fundamental terms of DOT. UITA would set minimum standard (***i.e***. not less than 2/3rds of votes cast) to change governing law of trust. DOT could increase but not reduce approval threshold or impose additional requirements.
38-40	No Registration Requirement; and Matters Adequately Covered under Securities Legislation or DOTs	No change.

ENDNOTES

---

[*] The members of the working group and their affiliations are: Janice Brown (Nova Scotia Department of Justice); John Cameron (Torys LLP); Glenda Campbell (Vice-Chair, Alberta Securities Commission); Paul Festeryga (Stewart McKelvey Stirling Scales); Mark Gillen (University of Victoria Faculty of Law); Wayne Gray (McMillan Binch Mendelsohn LLP), William Maslechko (Burnet Duckworth & Palmer LLP); Stephen Pincus (Goodmans LLP); Simon Romano (Stikeman Elliott LLP); and Susan Zimmerman (Goodmans LLP). Mr. Gray served as chair and reporter. The working group also acknowledges with thanks the contributions of Robert Vaux of Goodmans LLP and Carrie Aiken, a tax associate at McMillan Binch Mendelsohn LLP.

[1] W.D. Gray and Raymond Crete, "Report on Forms of Business Association in Canada", Uniform Law Conference of Canada, Civil Law Section (April 2005), available online, at: www.ulcc.org (ULCC Business Associations Report).

[2] Peter Beck and Simon Romano, ***Canadian Income Funds: Your Complete Guide to Income Trusts***, ***Royalty Trusts and Real Estate Investment Trusts*** (John Wiley & Sons Ltd.: Toronto, 2004), (Beck & Romano), at pp. 27-30.

[3] As of February 28, 2006, the aggregate market capital of all 237 income trusts listed at that time was estimated to be $193.7 billion (representing approximately 10.6% of the aggregate market capitalization of the Canadian-based entities listed on the TSX or TSX Venture Exchange). These statistics have been provided courtesy of Scott Keyworth and Andrew Gubbels of CIBC World Markets.

[4] Beck & Romano, ***supra*** endnote 2, at pp. 25-6.

[5] ***Ibid***.

[6] R.S.C. 1985, c.1 (5th Supp.), s. 132(6).

[7] Beck & Romano, ***supra*** endnote 2, at p. 18.

[8] ***Ibid***., at pp. 23-4.

[9] W.D. Gray and G. R. Courage, "Vehicles for Operating a Business", Law Society of Upper Canada, ***Special Lectures 2004: Corporate and Commercial Law*** (LSUC: Toronto, 2005) (Business Vehicles), 69 at 139.

[10] ***Ibid.***, p. 140.

[11] In the May 2, 2006 Federal Budget, the new Conservative Government affirmed that these amendments would become law. For the proposed draft modifications to dividend taxation, see the Department of Finance website at www.fin.gc.ca/drleg/

[12] Business Vehicles, ***supra*** endnote 9, p. 138.

[13] ***Ibid.***, p. 142. For example, Ontario imposes capital taxes on corporations under the ***Corporations Tax Act***, R.S.O. 1990, c. C-40.

[14] ITA, at Part I-3. Note that federal large corporations tax is being substantially reduced through the 2007 taxation year and is scheduled to be eliminated.

[15] Although, given the phase-out of PCT and LCT, these advantages are diminishing and will likely disappear.

[16] ITA, ***supra*** endnote 6, s. 132(6).

[17] ***Ibid.***

[18] ***Income Tax Regulations***, Consolidated Regulations of Canada, c. 945, as am. (ITR), s. 4801.

[19] ITA, ***supra*** endnote 6, s. 132(7).

[20] ***Ibid.***, s. 108(2).

[21] "Blocks of units" is defined in s. 4803(1) of the ITR as 100 units if the FMV of a unit is less than $25, 25 units if the FMV of a unit is $25 or more but less than $100, and 10 units if the FMV of one unit is $100 or more.

[22] Business Vehicles, ***supra***, endnote 9.

[23] ***Ibid***., p. 134, except where certain at-risk rules apply.

[24] S.Q. 1991, c. 64, art. 1260 to 1370.

[25] 1st Session, 38th Parl., 53-54 Eliz II, 2004-5, An Act to establish the ***Wage Earner Protection Program Act***, to amend the ***Bankruptcy and Insolvency Act*** and the ***Companies' Creditors Arrangement Act*** and to make consequential amendments to other Acts. Bill C-55 was scheduled to go into force on June 30, 2006 but its implementation has been delayed if not derailed.

[26] R.S.C. 1985, c. B-3.

[27] R.S. C. 1985, c. C-36.

[28] See Department of Finance Canada, "Tax and Other Issues Related to Publicly Listed Flow-Through Entities" (Income Trusts and Limited Partnerships), Consultation Paper (September 2005), pp. 22-3 quoting the U.S. National Association of Real Estate Investment Trusts for the estimate that there were, at that time, nearly 180 publicly traded REITs in the U.S. having an aggregate market capitalization in excess of US $400 billion.

[29] Canadian Institute of Public and Private Real Estate Companies, "Summary of Trust Limited Liability Provisions in Selected U.S. Statutes" (CIPREC Survey) (December 2002), p. 2, stating that more than 80% of U.S. REITs organized as trusts are formed in Maryland.

[30] R.S.C. 1985, c. C-44.

[31] Bill C-21 died on the order paper when Parliament dissolved for the January 23, 2006 general federal election.

[32] W.D. Gray and C.W. Halladay, ***Guide to CBCA Reform: Analysis and Precedents*** (Carswell: Toronto, 2002), p. 89 (CBCA Reform).

[33] See endnotes 35 and 36 for statistics used in the calculations.

[34] CIBC World Markets, ***supra*** endnote 3.

[35] As of March 31, 2006, there were approximately 6,677 corporate reporting issuers in Canada. All reporting issuers are active SEDAR filers. These statistics are provided courtesy of Andrew Gubbels of CIBC World Markets and Lindsey Donovan of The Canadian Depository for Securities Limited.

[36] Estimate from figures provided by Ms. Cheryl Ringor, Director, Compliance and Policy, Corporations Canada, Industry Canada on March 21, 2006, based on statistics as of March 31, 2005. Note that it is difficult to tell the number of inactive corporations.

[37] Business Vehicles, ***supra*** endnote 9, p. 96.

[38] ***Ibid.***

[39] See, for example, the ***Partnerships Act***, R.S.O. 1990, c. P.5, s. 2.

[40] See, for example, the ***Business Names Act***, R.S.O., c. 13-17, s. 2(3).

[41] See, for example, combined effect of the ***Partnerships Act***, ***supra,*** endnote 39***,*** s. 43(1) and (3) and the ***Business Names Act***, ***ibid.***, s. 2(3) and (3.1).

[42] Interpretation Bulletin IT-343R (Meaning of the term "Corporation"), September 26, 1977.

[43] ***Ibid***., para. 2.

[44] CIPREC Survey, ***supra*** endnote 29. See also Delaware Code Title 12 (***Delaware Statutory Trusts***), s. 3801(a). Although unincorporated, a statutory trust is a "separate legal entity".

[45] 30 & 31 Vict., c.3, reprinted in R.S.C. 1985, Append. No. 5.

[46] CBCA, s. 107.

[47] ***Ibid***., s. 28(1).

[48] ***Ibid.***, s. 163.

[49] ***Ibid.***, s. 146.

[50] ***Ibid.***, s. 135(1.1).

[51] ***Ibid.***, ss. 24(3) and 140(1).

[52] ***Ibid.***, ss. 139(1) (quorum requirement for shareholder meetings) and 114(2) (quorum requirement for board meetings).

[53] R.S.N.S. 1989, c. 81.

[54] Beck & Romano, ***supra*** endnote 2, at pp. 81-3.

[55] The description of an ordinary mutual fund is adapted from the definition of "mutual fund" in the ***Securities Act***, R.S.O., c. S-5, as am.

[56] M.R. Gillen "Income Trust Unitholder Liability: Risks and Legislative Response" (2005), 42 Can. Bus. L.J. 325 at p. 367-368 (Gillen on Unitholder Liability).

[57] ***Ibid***, c. 365. Indeed, Bill 13, the new ***Income Trust Liability Act*** (BC Act) states that it is retroactive, thereby codifying the consensus view of the prior law. See recommendation 8 at Part V.6 (d).

[58] ULCC Business Associations Report, ***supra*** endnote 1, p. 26.

[59] R.S.O. 1990. c. B.16.

[60] R.S.A. 2000, c. B-9.

[61] CBCA, s. 45(1). Note that the unanimous shareholder agreement exception would not, in practice, apply to a corporation that is a reporting issuer.

[62] S.O. 2004, c. 29, Sch. A, s. 1(1).

[63] S.A. 2004, c. I-1.5, s. 2(1).

[64] C.C.S.M., c. 1105, s.2.

[65] S.S. 2006, p. 1-2.02, which received Royal Assent on May 19, 2006.

[66] The BC Act passed third reading in the British Columbia Legislative Assembly on March 30, 2006.

[67] Gillen on Unitholder Liability, ***supra*** endnote 56, p. 368.

[68] See further discussion on the BC Act at paragraph 67 of the text.

[69] R.S.O. 1990, c. S-5, as am. (OSA).

[70] R.S.A. 2000, c. S-4, as am. (ASA).

[71] See, for example, the ***Partnerships Act*** (Ontario), ***supra*** endnote 39, s. 2, which states, in part, as follows:

> but the relation between the members of a company or association that is incorporated by or under the authority of any special or general Act in force in Ontario or elsewhere, or registered as a corporation under any such Act, is not a partnership within the meaning of this Act.

[72] Gillen on Unitholder Liability, ***supra*** endnote 56, at p. 328.

[73] ***Ibid.***

[74] See, for example, ***White v. E.B.F. Manufacturing Ltd***. (2005), 12 B.L.R. (4th) 1 (N.S.C.A.).

[75] Importantly, there appears to be no reported case in Canada in which a court has lifted the veil of a corporate reporting issuer.

[76] See, for example, CBCA, s. 24(3).

[77] ***Bowater Canadian Ltd. v. R.L. Crain Inc***. (1987), 62 O.R. (2d) 752, 46 D.L.R. (4th) 161 (C.A.).

[78] ***Jacobsen v. United Canso Oil & Gas Ltd***., [1980] 6 W.W.R. 38, 113 D.L.R. (3d) 427 (Alta. Q.B.).

[79] CBCA, ss. 33(1) and (2).

[80] Goodmans LLP, "Governance of Income Trusts in Canada", Report to Industry Canada (December 31, 2005). The Goodmans Survey was of 53 income trusts, representing approximately 22% of all income trusts in existence in Canada.

[81] ***Ibid.***, Sched. A, s. 2. See, also, Mark Gillen "A Comparison of Business Income Trust Governance and Corporate Governance: Is There a Need For Legislation or Further Regulation?" (Capital Markets Institute, June 19, 2005) (Gillen on Trust Governance), p. 9 and Table A. Broadly, the findings of Professor Gillen are consistent with those of the later and statistically more representative Goodmans Survey. Hence, this report generally refers to the Goodmans Survey.

[82] Goodmans Survey, ***ibid***., endnote 80, Sch. A, p. 5, and see also, Gillen on Trust Governance, ***ibid***., p. 35. Since completion of the Goodmans Survey, the Royal Utilities Income Fund offer affords another example of a voluntary unitholder proposal regime. Further, as will be discussed below, the Royal Utilities DOT contains many other shareholder-like rights and remedies.

[83] Janis Sarra "Shareholders as Winners and Losers under the ***Amended Canada Business Corporations Act"*** (2003), 39 Can. Bus. L.J. 52, at p. 54-7.

[84] CBCA Reform, ***supra*** endnote 32, p. 47.

[85] CBCA, s. 137.

[86] CBCA, s. 137(5)(a) and ***Canada Business Corporations Regulations***, 2001, SOR/2001-512 (CBCR), s. 49.

[87] CBCA, s. 137(5)(b).

[88] ***Ibid***., s. 137(5)(e).

[89] ***Ibid***., s. 137(5)(1.1) Consideration should nevertheless be given to deleting the "significant" test because it is unclear and can possibly be abused to block the circulation of legitimate proposals.

[90] CBCA, s. 173(3) and CBCR, supra endnote 86, s. 48.

[91] CBCA, s. 137(5)(d) and CBCR, ss. 51(1) and (2).

[92] CBCA, s. 137(5)(c) and CBCR, s. 50.

[93] CBCA, s. 143.

[94] However, see, the recent decisions in ***D'Addario v. Environmental Management Solutions Inc***. (2005), 11 B.L.R. (4th) 286 (Ont. S.C.J.) and ***Paulsen & Co. Inc. v. Algoma Steel Inc.,*** (2006), 79 O.R. (3d) 191 (Ont. S.C.J, ***per*** Cumming J.).

[95] Goodmans Survey, ***supra*** endnote 80, Sched. A, p. 6.

[96] See, as just five of the reported decisions, ***Catalyst Fund General Partner I Inc. v. Hollinger Inc***. (2004), 48 B.L.R. (3d) 194 (Ont. S.C.J.), ***Catalyst Fund General Partner I Inc. v. Hollinger Inc***. (2004), 50 B.L.R. (3d) 250 (Ont. S.C.J.), ***Catalyst Fund General Partner I Inc. v. Hollinger*** (2004), 1 B.L.R. (4th) 186 (S.C.J.) and ***Catalyst Fund General Partner I Inc. v. Hollinger Inc***. (2005), 8 B.L.R. (4th) 117 (Ont. S.C.J. ***per*** C. Campbell, J.) affd. (2006), 79 O.R. (3d) 288 (Ont C.A.).

[97] There were several decisions surrounding Principal Trust. See, in particular, ***First Investors Corp., Re***. (1988), 54 D.L.R. (4th) 730 (C.A.), ***Associated Investors of Canada Ltd., Re.*** (1988), 52 D.L.R. (4th) 168 (C.A.), ***First Investors Corp., Re***. (1988), 71 C.B.R. (N.S.) 299 and ***Principal Group Ltd. (Trustee of) v. Principal Savings & Trust Co***., [1996] 1 W.W.R. 727 (Alta. C.A.).

[98] Goodmans Survey, ***supra*** endnote 80, Sched. A., p. 7.

[99] Gillen on Trust Governance, ***supra*** endnote 81, pp. 30-1.

[100] Stephanie Ben-Ishai and Poonam Puri "The Canadian Oppression Remedy Judicially Considered: 1995-2001" (2004), 30 Queen's L.J. 79, reporting that only 8% of cases involved public companies (and only 1/3rd of these, or 2 cases, were successful). Since the article was published, there have been other successful oppression suits against publicly traded corporations, particularly involving institutional

investors as complainants. See, for example, ***UPM-Kymmene Corp v. UPM-Kymmene Miramichi Inc***. (2004), 42 B.L.R. (3d) 34, 250 D.L.R. (4th) 526, (Ont. C.A.), affirming (2002), 27 B.L.R. (3d) 53, 214 D.L.R. (4th) 496 (S.C.J. [Commercial List]).

[101] Gillen on Trust Governance, ***supra*** endnote 80, pp. 26-7.

[102] R.W.V. Dickerson, J. L. Howard and L. Getz, ***Proposals for a New Business Corporations Law for Canada***, Vol. I (Information Canada: Ottawa, 1971), para. 482.

[103] (1843), 2 Hare 461 (H.L. ***per*** Wigram V-C).

[104] Stanley M. Beck "The Shareholders' Derivative Action" (1974), 52 Can. Bar Rev. 159 at p. 167.

[105] See, for example, the ***Class Proceedings Act***, 1992, S.O., c. 6 and the decision of the Supreme Court of Canada in ***Western Canada Shopping Centres Inc. v. Dutton***, [2001] 2 S.C.R. 534, holding that courts must fill any vacuum in provincial Rules of Court providing for class actions.

[106] Goodmans Survey, ***supra*** endnote 86, Sched. A, p.7. Again, The Royal Utilities Income Fund affords another example of voluntary adoption of a unitholder dissent and appraisal right. See endnote 82.

[107] ***Ibid***. Otherwise stated, the right was poorly conceived. This is not the case with respect to dissent and appraisal right provided for in the Royal Utilities DOT. See endnote 82.

[108] Gillen on Trust Governance, ***supra*** endnote 81, at footnote 217.

[109] Continuances and amalgamations do not apply to income trusts. Rather, one trust can be wound-up into another. Also, a trust may change its governing law by amending its DOT.

[110] Gillen on Trust Governance, ***supra*** endnote 81, at footnote 206.

[111] CBCA, s. 102(1).

[112] Report of the Toronto Stock Exchange Committee, ***Corporate Governance in Canada, Where Were the Directors? Guidelines for Improved Corporate Governance in Canada*** (TSE: Toronto, 1994) (TSE Report), at para. 4.10.

[113] Liability caps are permitted in Delaware and many other U.S. states, but, apart from Part XIII.1 (***Civil Liability for Secondary Market Disclosure***) of the OSA, do not generally exist in Canada.

[114] CBCA, s. 102(1).

[115] The case most often cited here is ***Automatic Self-Cleansing Filter Syndicate Co. v. Cuninghame,*** [1906] 2 Ch. 34 (Eng. C.A.). In Canada, a leading case is ***Teck Corp. v. Millar*** (1972), 33 D.L.R. (3d) 288 (B.C.S.C ***per*** Berger J.).

[116] CBCA, s. 115(1).

[117] ***Ibid***., s. 115(3).

[118] Goodmans Survey, ***supra*** endnote 80, p.3. See also Beck & Romano, ***supra*** endnote 2, at pp. 92-3.

[119] ***Ibid***.

[120] CBCA, s. 122(1).

[121] ***Peoples Department Stores Inc. v. Wise*** (2004), 244 D.L.R. (4th) 564 (S.C.C.) (***Peoples***).

[122] See, for example, the symposium on the Supreme Court's judgment in ***Peoples*** collected at 46 (2005), 41 Can. Bus. L.J. at pp. 167-235, consisting of: Catherine Francis "***Peoples Department Stores Inc. v. Wise***: The Expanded Scope of Directors' and Officers' Fiduciary Duties and Duties of Care"; W. D. Gray "A Solicitor's Perspective on ***Peoples v. Wise***"; Warren Grover "The Tangled Web of the Wise Case"; Ian B. Lee "***Peoples Department Stores v. Wise*** and the 'Best Interests of the Corporation'"; Stéphane Rousseau "Directors' Duty of Care after ***Peoples***: Would it be Wise to Start Worrying about Liability?"; and Jacob S. Ziegel "The ***Peoples*** Judgment and the Supreme Court's Role in Private Law Cases".

[123] Goodmans Survey, ***supra*** endnote 80, Sched. A, p. 2.

[124] ***Peoples***, ***supra*** endnote 121, para. 64.

[125] See, however, the ***obiter dicta*** of Farley J. in his 2001 unreported decision in ***Rio Tinto Canadian Investments Ltd. v. Labrador Iron One Royalty Income Fund (Trustee of)***. There, Farley J. said:

> The Fund Trust is a commercial one which is modelled upon a corporate enterprise including providing for the duties and obligations of Trustees to be equivalent to those of the directors of a (public issuer) corporation incorporated under the ***Canada Business Corporations Act***. Thus, the subject trust and the Declaration of Trust should be viewed according to quasi-corporate principles… In assessing the actions of trustees in a quasi-corporate situation such as this, trust obligations and duties of trustees should be appropriately modified to take into account the "corporate aspect". This corporate aspect would include the business judgment rule.

[126] See, for example, the CBCA, s. 122(3).

[127] ***Ibid.***

[128] See, for example, the CBCA, s. 120.

[129] ***Ibid.***

[130] ***Ibid***., ss. 120(7) and (7.1).

[131] ***Ibid***.

[132] (1726) Scl. Cas. ch. 61, 25 E.R. 223 (Eng. Ch. Div. ***per*** King L.C.).

[133] D.W.M. Waters, M.R. Gillen and L.D. Smith, ***Waters***' ***Law of Trusts in Canada***, 3rd Ed. (Carswell: Toronto, 2005), p. 914.

[134] See, for example, ***Aberdeen Rail Co. v. Blaikie Bros.*** [1843-60] All E.R. Rep. 249 (H.L.) and ***Imperial Mercantile Credit Association v. Coleman*** (1873), L.R. 6 H.C. 189 (H.L.).

[135] Goodmans Survey, ***supra***, endnote 80, Sched. A, p. 2-3.

[136] CBCA, s. 105(1)(c) and definition of "individual" in s. 2(1).

[137] Goodmans Survey, ***supra*** endnote 80, Sched. A., p.1.

[138] See, for example, the OBCA, s. 2(1) and the ***Loan and Trust Corporations Act***, R.S.O. 1990, c. C.25.

[139] TSE Report, ***supra*** endnote 112, para. 5.56.

[140] See, for example, CBCA, s. 119, OBCA, s.131, ABCA, s. 119 and the ***Canada Labour Code***, R.S.C. 1985, c. L-2 as amended by ***An Act to Amend the Canada Labour Code*** and the ***Public Service Staff Relations Act***, S.C. 1993, c. 47, s. 37, which added s. 251.18 to the ***Canada Labour Code***.

[141] ***Supra*** endnote 6 , s. 227.1.

[142] R.S.C. 1985, c. C-8, s. 21(1).

[143] R.S.C. 1985, c. U-1, s. 54(1).

[144] R.S.C. 1985, c. E-15, s. 323(1).

[145] For example, the ***Retail Sales Tax Act***, R.S.O. 1990, c. R.31, s. 43(1).

[146] See, for example, the definitions of "issuer" and "person" (which includes both trusts and trustees) in the OSA, ***supra*** endnote 69, s. 1(1).

[147] ***Millgate Financial Corp. v. BF Realty Holdings Ltd***. (1995), 19 B.L.R. (2d) 271 (Ont. Ct. (Gen. Div.)).

[148] ***GATX Corp. v. Hawker Siddeley Canada Inc***. (1996), 27 B.L.R. (2d) 251, 1 O.T.C. 322 (Ont. Ct. (Gen. Div.) – Commercial List).

[149] ***Stern v. Imasco Ltd***. (1999), 1 B.L.R. (3d) 198, 38 C.P.C. (4th) 347 (Ont. S.C.J.).

[150] (1999), 43 O.R. (3d) 101, 168 D.L.R. (4th) 351 (C.A.), leave to appeal to S.C.C. refused 134 O.A.C. 400n.

[151] [1992] 3 S.C.R. 299, 97 D.L.R. (4th) 261.

[152] [1993] 3 S.C.R. 206, 107 D.L.R. 94th) 169.

[153] See, for example, Christopher C. Nicholls "Liability of Corporate Officers and Directors to Third Parties" (2001), 35 Can. Bus. L. J. 1 at pp. 26-9.

[154] See, for example, ***Said v. Butt*** [1920] 3 K.B. 497 and, more recently, ***Normart Management Ltd. v. West Hill Redevelopment Co***. (1998), 37 O.R. (3d) 97, 155 D.L.R. (4th) 627 (C.A.).

[155] See, for example, the OSA ***supra*** endnote 69, s.130 (prospectus civil liability) and Part XXX.1 (***Civil Liability for Secondary Market Disclosure***).

[156] Such a formulation would leave scope for such egregious cases such as ***NBD Bank, Canada v. Dofasco Inc***. (1999), 46 O.R. (3d) 514, 181 D.L.R. (4th) 37 (C.A.).

[157] CBCA, ss. 124(1) and (3).

[158] ***Ibid***., s. 124(5). The foregoing states the mandatory rule under the CBCA. As well, a CBCA corporation is permitted to indemnify individuals in other circumstances subject to s. 124(3). The UITA should include this permitted indemnification.

[159] ***Ibid***., s. 124(6).

[160] ***Ibid.***, s. 120(5)(b).

[161] ***Ibid***., s. 108. Note that first directors of an OBCA corporation cannot resign before the first meeting of shareholders unless replacement directors are concurrently appointed or elected. The same restriction does not apply to directors of a CBCA corporation.

[162] See, for example, the ***Trustee Act***, R.S.O. 1990, c. T-23, s. 5(1).

[163] David A. Steele and Andrew G. Spence "Enforcement Against the Assets of a Business Trust by an Unsecured Creditor" (1998), 26 Can. Bus. L. J. 72.

[164] ***Ibid*** at p. 73-5.

[165] ***Ibid*** at pp. 78-82.

[166] CBCA, s. 192(4).

[167] ***Ibid***., s. 206 (2) and the definitions of "take-over bid", "offeror" and "dissenting offeree" in s. 206(1).

[168] However, this criticism does not apply to the Royal Utilities DOT. See endnote 82.

[169] ***Ibid***., s. 206.1.

[170] ***Ibid.***, s. 206.1(1) and the definitions of "offeror" and "take-over bid" in s. 206(1).

[171] ***Ibid***., s. 206.1(2).

[172] National Instrument 51-102 (***Continuous Disclosure Obligations***).

[173] A position consistent with each of the Income Trust Liability Acts.

[174] See the memorandum dated May 16, 2006 from the Personal Property Security Law (PPSL) Subcommittee, Business Law Section, Ontario Bar association to the Honorable Gerry Phillips, Minister of Government Services posted on the website to the Ontario Bar Association, at: www.oba.org. The PPSL recommendation is meant to be adopted uniformly across the country.

[175] 1664 U.N.T.S. 311. As well, the Hague Convention is not in force in Ontario, Quebec or Nova Scotia.

[176] While, in theory, this rule would permit the unitholders of an income trust by 2/3ds vote to change the trust's governing law to a foreign jurisdiction, any such change would of course entail tax considerations. However, the UITA is primarily intended as enabling legislation.

[177] ***Ibid***., Goodmans Report, ***supra*** endnote 80, Sched. A, pp. 6-7.

[178] See the discussion on the ULCC working group on partnership law at Part V.6(f) above.

[179] See discussion at Part V.12(a) and (b).

[180] ***Supra*** endnote 175 for the PPSL Subcommittee recommendations.

[181] N.I. 51-102, ***supra*** endnote 171, s. 12.1(a). SEDAR is the acronym for the ***System for Electronic Data Analysis and Retrieval***.

[182] See, for example, the discussion on the notice theory in ***Trustee v. Tri-Lux Fine Homes Ltd.*** (1998), 18 R.P.R. (3d) 1, 39 C.L.R. (2d) 6 (Ont. C.A.).

[183] See discussion at Part III.6(a) above.

[184] Registration is not required to form a general partnership but may be required as a condition of using the operating business name. See, for example, the ***Business Names Act***, R.S.O. 1990, c. B.17, ss. 2(3) and (3.1).

[185] ***Supra*** endnote 69.

[186] ***Ibid***., Part XXI (ss. 106 through 121) and ss. 76, 134 and 135.

[187] ***Ibid***., ss. 107, 108 and 109.

[188] ***Ibid***., ss. 76, 134 and 135.

[189] ***Ibid***., s. 75.

[190] See, for example, OSA, Part XIX (***Proxies and Proxy Solicitation***).

[191] N.I. 51-102, supra endnote 171, ss. 4.1 and 4.2.

[192] ***Ibid***., s. 5.6.

[193] ***Ibid***., ss. 6.1 and 6.2.

[194] ***Ibid***., Part 9.

[195] ***Ibid***.

[196] ***Ibid.***, s. 9.5.

[197] See, for example, OSA ***supra*** endnote 69, s. 78(2).

[198] M.I. 52-110, s. 1.2 and the interrelated definitions of “reporting issuer”, “issuer”, “person” and “company” in s. 1(1) of OSA, ***ibid***.

[199] CBCA, s. 140(1).

[200] Goodmans Survey, ***supra*** endnote 80, Sched. A, p.5.

[201] CBCA, s. 211(3).

[202] Gillen on Trust Governance, ***supra*** endnote 81, p. 10 and Table A.1.

[203] CBCA, definition of “special resolution” in s. 2(1).

[204] Typically, under the CBCA, the holders of a class or series of shares are entitled to vote separately as a class if, but only if, such class or series is affected by the transaction in a manner different from the shares of another class or series.

[205] Goodmans Survey, ***supra*** endnote 80, Sched. A, p. 6.

[206] ***Ibid***.

[207] ***Ibid***., Sched. A, p.1.