

OVERVIEW

A business is an activity or enterprise carried on with some regularity for gain and profit. There are several different types of mechanisms or structures that can be used for carrying on a business. The legal structure of such organizations has evolved over time from businesses carried on by a single individual, to partnerships and finally to more complex organizations, such as limited partnerships and companies.

The form of business entity selected by a person or persons who wish to start a business must take into account the complexity of the business, and should be decided after obtaining professional advice. The structure selected might be a sole proprietorship, a partnership, a limited partnership, or a company. In the latter case, the incorporators must choose the jurisdiction of incorporation (for example, provincial or federal).

SOLE PROPRIETORSHIP

A **sole proprietorship** is the simplest form of business organization, carried on by one person with or without the assistance of employees and without any formal legal organization. A sole proprietorship is not a suitable legal structure when others expect to participate in the ownership of the business.

The main advantage of carrying on business as a sole proprietorship is that it does not need to be regulated internally. One individual is the owner, director and manager of the business and collects all the revenues of the business. On the other hand, the sole owner is personally liable for debts and obligations incurred in carrying on the business and, apart from bankruptcy and insolvency laws, there are no laws to protect the sole owner from creditors.

A sole proprietorship is generally carried on under a business or firm name, such as “A.B.C. Trading”. All legal documents, cheques, invoices and other business documents should show the sole proprietor’s name, and wording to indicate that the sole proprietor is carrying on business under the business name. An example might be “John Brown doing business as A.B.C. Trading”. Such business names can be registered with the Corporate Registry, though such a registration does not result in any protection for the sole proprietor or the business. Note that a company can also register a business name, different from the company’s legal name, in this manner.

A person who carries on a sole proprietorship must generally obtain a business licence and fulfil all the requirements of his or her trade. The only legal requirement for a sole proprietorship, apart from general laws (income tax, G.S.T. registration, licences, etc.), is that, if a person is engaged in business for trading, manufacturing or mining purposes, and uses a business name other than his or her own, he or she is required to reserve the name with the Registrar of Companies and file a **Statement of Registration of Sole Proprietorship** of this name under the *Partnership Act*. This form can easily be prepared by anyone and filed online with the appropriate fee at the BC Registries and Online Services site maintained by the Province of BC (<https://www.bcregistry.gov.bc.ca/>) The fee for filing such a Statement is much less expensive than the incorporation fee for a company.

PARTNERSHIP

When two or more persons carry on a business without incorporating a company, they generally form a **partnership**. The *Partnership Act* defines a partnership as the “relation which subsists among persons carrying on business in common with a view of profit”.

Individual partners are each personally jointly and severally liable for all the debts of the partnership, including debts resulting from actions of other partners. The profits of the business are divided among the partners according to their interests in the partnership and this earned income forms part of each partner’s personal income for tax purposes.

Although incorporated companies sometimes join partnerships, more often companies try to avoid actual “partnership”, and the liability that comes with it. “Joint venture agreements” between companies intended to carry on a business together often contain clauses that specifically state that the joint venture does not constitute a partnership among the parties. Note, however, that simply including such a clause in an agreement does not mean that there is no partnership: It is the courts, and not the written agreement between the companies, which have the ultimate power to decide whether the companies were, according to the law, true partners.

There are several advantages to carrying on business as a partnership:

- it can be simple and inexpensive;
- there are very few legal requirements for forming a partnership. The main requirement, as for a sole proprietorship is that, if two or more persons are partners for the purpose of trading, manufacturing or mining, the partners must file a **Statement of Registration of General Partnership** under the *Partnership Act* (s. 81(1)). The **Statement** must include a brief description of the business of the partnership. It has become more common for general partnerships to register voluntarily as they must provide a filed **Statement** to their bank to open a bank account in the name of the partnership and the **Statement** is often a requirement to obtain a business license;
- the cost of filing such a **Statement** is much less than the cost of incorporating a company;
- the *Partnership Act* sets out the rights and duties of partners which may be varied by a partnership agreement entered into by the partners;
- a partnership agreement is not mandatory, although it is usually recommended, and depending on the needs of the partners and the complexity of their business arrangements some partnership agreements are extremely complex and expensive;
- generally, each partner has the right to participate in the management of a partnership, depending on the terms of the agreement among the partners;
- the partners in a partnership determine when and how much of the profits of the business will be paid to the partners, whereas the shareholders in a company often only receive payment of profits if and when the directors, in their discretion, declare dividends; and

- in some situations, a partnership may provide a tax advantage over an incorporated company.

There are also several disadvantages of carrying on a partnership (as opposed to incorporating a company):

- a partnership may be immediately dissolved in several situations, for example, if the partnership consists of two partners and one of them dies or becomes bankrupt;
- each partner is personally liable for all losses, debts and obligations of the partnership and may also be responsible for the other partners' wrongful acts committed in connection with the partnership business, whether authorized or not;
- the transfer of ownership in a partnership may be difficult and cumbersome;
- since there is no way of limiting the authority of various partners⁽¹⁾, a partnership is only suitable for a relatively small number of partners when the partners have confidence in one another.

LIMITED PARTNERSHIPS

A limited partnership is a modified form of the partnership described above and is really a hybrid of a partnership and a company. The limited partnership consists of two kinds of partners:

- **general** partners, who are managing partners who have the same liabilities, rights and duties as ordinary partners in a partnership. In reality, such general partners are usually incorporated companies in order to limit the liability of the general partner's shareholders. General partners manage the day-to-day operation of the business of the limited partnership; and
- **limited** partners, who are investors whose liability for the company's business debts is limited by the *Partnership Act* to the extent of capital that they have contributed or agree to contribute to the limited partnership. These individuals or corporations often seek tax advantages derived from the limited partnership's participation in a particular type of investment. Limited partners cannot take part in the management of the limited partnership, or else they lose the protection of limited liability.

The rights of the limited partners are set out in the agreement creating the partnership and in the *Partnership Act*. The limited partners' ability to transfer their interests in the limited partnership may be restricted.

COMPANIES

Most businesses, whether large or small, are carried on in the form of a company (also known as a limited-liability company or corporation). The limited-liability company is a relatively recent innovation. It is since the mid-19th century that companies have been the leading means of ownership and operation of businesses.

⁽¹⁾ Some special forms of partnerships such as Limited Partnerships and Limited Liability Partnerships limit the liability of individual partners.

Since prehistoric times, individuals have carried on business enterprises for profit and have joined together for collective purposes. When a group of merchants in ancient Greece pooled their resources to build and operate a trading vessel, they formed a partnership rather than a company since ancient societies did not have laws that regulated the scope and standards of business activity. These early enterprises were forerunners of the contemporary company in terms of their functions and activities, but not in terms of their mode of incorporation.

The corporate form itself developed in the early Middle Ages with the growth and codification of civil and canon laws. However, it took business owners several centuries to adopt this arrangement. The first companies were towns, guilds (which dominated many trades and occupations), universities and ecclesiastical orders. These differed from partnerships and modern companies in that they were not the property of their participants. For example, the holdings of medieval guilds belonged to the guild itself and individuals did not own shares in its assets. Guild members were individual proprietors who ran their own businesses. As corporate bodies, the government chartered guilds and public statutes regulated their business practices.

By the end of 15th century, the courts agreed to uphold the principle of “limited liability” which was originally applied to guilds and municipalities. This principle was later applied to shareholders in business corporations and served to encourage investment because the most an individual shareholder could lose in the event of the company’s failure would be the amount that the individual originally paid for his or her shares.

The incorporation of business enterprises began in England during the Elizabethan period, with the creation of the first joint-stock companies. Joint stock companies were financed with private capital but were regulated by public charter which set out in detail the activities in which the enterprises could operate. The East India Company (incorporated on December 31st, 1600 as the Governor and Company of Merchants of London, trading into the East Indies) and the Hudson’s Bay Company (which was granted a Royal Charter on May 2nd, 1670 and was then known as The Governor and Company of Adventurers of England Trading into Hudson’s Bay) were semi-public enterprises acting both as arms of the state and as vehicles for private profit. Similar principles applied to many syndicates and colonial charters on the North American continent and much of the settlement of North America was initially underwritten as business ventures.

The growth of independent companies happened slowly over time. Great Britain was an innovator in the field. In England, laws were changed and liberalized with the onset of the industrial revolution (from the end of the 16th to the beginning of the 17th century) to provide that any group complying with certain minimum conditions had the right to incorporate and the principle of limited liability was extended to such groups. Other countries followed suit.

By the 21st century, the company has become the dominant business form in industrial nations.

A company is a legal entity, a “person” in its own right, distinct and separate from the persons who own it - its shareholders. When all the requirements of the applicable federal or provincial statutes are fulfilled, and a company is created (incorporated), a “body

corporate” is created under the law. This new entity has the ability to do anything a natural person of full legal capacity can do, such as entering into contracts, owning property (including land), borrowing money, suing in its own name or being sued.

The rights of ownership and the power to manage the company are separate. The shareholders are the owners of the company, and they elect a Board of Directors who are responsible for managing the business of the company in the best interests of the company.

Various rules regarding the relationships among the shareholders, and between the shareholders and the directors, are set out in the company’s *Articles* (British Columbia) or *Bylaws* (Federal) and may be supplemented by a *Shareholders’ Agreement*.

The company, and not its individual shareholders, owns its assets and is liable for its debts. Except in small companies where the shareholders are also the directors, shareholders have little power or authority to deal with a company’s assets because management of the company is vested in its directors and officers. However, in most companies, the shareholders have the power to replace the directors if they do not agree with the way the directors are managing the company.

Advantages of a Company

A company has many advantages over a natural person, sole proprietorship or partnership:

Limited liability

Limited liability is one of the most important benefits of incorporating a business. Canadian laws provide that the liability of shareholders is limited to the amount that the shareholders paid for shares and to any amount that is owed to the company by the shareholders for unpaid shares. For example, Section 87 of the *Business Corporations Act* (British Columbia) specifically provides that a shareholder of a company is not personally liable for the debts, obligations, defaults or acts of the company and a shareholder is not, in respect of the shares held by that shareholder, personally liable for more than the lesser of:

- the unpaid portion of the issue price for which those shares were issued by the company, and
- the unpaid portion of the amount actually agreed to be paid for those shares.

Simply put, persons who form a company and who become its shareholders are only required to contribute toward the debts of the company the amount that they have agreed to pay for their shares in the company⁽¹⁾.

Continued Existence or Immortality

A company is a separate entity from its shareholders. A company will have perpetual existence as long as it continues to fulfil the statutory requirements

⁽¹⁾ If a company is dissolved and assets are distributed to the shareholders, the shareholders may also be liable for the value of the assets distributed to them if claims are made against the company within two years of the dissolution of the company (s. 348).

governing its continuation, unlike a natural person who may die or a partnership that may be dissolved when one of its partners dies or becomes bankrupt.

The existence of a company continues even if its shareholders transfer their shares to other persons or it has no shareholders.

Transferability of shares

The transfer of a shareholder's shares to another person or entity is relatively simple, unless the Articles of the company restrict transfers. Most private companies' Articles do, however, restrict the transfer of shares to protect existing shareholders from the possibility of other shareholders selling their shares to unwanted newcomers.

Capital or Resources

Shareholders who are not also directors or officers of a company may invest money without being responsible for the day-to-day conduct of the business in which they invest and without fear of liability for the debts of the company. This makes raising capital for the business much easier. One of the original purposes of the formation of a company was to bring together a large number of people who would pool their capital or resources to carry out enterprises that were too costly for one person or for a small partnership.

A shareholder of a company may contribute assets to a company in two ways:

- by transferring or selling to the company the shareholder's personal assets, such as an unincorporated business, real property or investment. When all or a portion of the consideration for the transfer of the asset is in the form of shares in the company issued to the shareholder, the payment of capital gains taxes on the sale of the asset by the shareholder may be deferred by filing an election with the Canada Customs and Revenue Agency; or
- by paying for shares in cash. The company may then use the shareholders' collective investments in the company to finance the operations of the company.

A company may also raise capital by borrowing money from its shareholders, a bank or other financial institution although institutional lenders often require some form of personal guarantee from the shareholders of private companies as security for a loan.

Tax advantages

Preferential income tax treatment for the profits of small companies and for dividend income in the hands of shareholders, flexibility in deferring taxes (e.g. estate planning), and the possibility of income splitting may make the use of a corporate structure very attractive from a tax perspective. Companies are often incorporated on the advice of legal or accounting professionals in order to reduce or defer the income taxes payable by individuals or their estates.

Disadvantages of Incorporating

In spite of all the advantages of incorporating a company, there are several disadvantages:

- the cost of incorporating is relatively high in comparison to the cost of registering a business name;
- companies have ongoing costs of maintaining the company's records, including maintaining the registered and records offices, preparing minutes or resolutions, and filing notices and annual reports;
- companies have additional accounting and administrative obligations (and expenses) that other forms of business may not, including:
 - preparation every year of financial statements. Section 198 of the Act and the Regulations to the Act describe the accounting records which must be maintained for each company; and
 - preparing and filing a corporate income tax return each year, separate from the returns of the shareholders.

Jurisdiction

When the principals of a business decide to incorporate in Canada, they must choose whether to incorporate:

- **Federally:**

A corporation incorporated federally under the *Canada Business Corporations Act* has the right to carry on business in any province or territory under its incorporated name but is subject to the laws of each province or territory where it carries on business. Before carrying on business in any province or territory, a federal corporation must first register extraprovincially or extraterritorially in each such province or territory;

- **Provincially (or Territorially):**

A company incorporated under a particular provincial or territorial statute (e.g. the *Business Corporations Act* in British Columbia) may only carry on business in another province or territory if it registers extraprovincially or extraterritorially in the other province or territory.

The provisions of the *Canada Business Corporations Act* and the relevant provincial/territorial statutes may be very different and the procedures and forms in each province and territory vary greatly.

Companies (or corporations) incorporated **outside** Canada may be permitted by the laws of each province or territory to register and carry on business in that province or territory if they register extraprovincially/extraterritorially in that province or territory.

Any reference to “the Act” in this Guide is a reference to the *Business Corporations Act* of British Columbia. The materials in this **Guide** are restricted to corporate record keeping

requirements for private companies governed by the Act. However, most of the basic procedures described in this *Guide* are common to both public and private companies.

Types of Companies

Under the Act, there are several types of companies:

- **Public companies** are, generally, companies the shares of which are listed and traded on the stock exchange. Section 1 (1) of the Act defines such a company as also including “**reporting issuers**” as that term is defined in the *Securities Act*, which includes certain companies that are not actually listed or trading on a stock exchange, but which have taken certain steps involving filing documents with the Securities Commission in order to permit shares of the company to be offered to members of the public. Public companies are **not** covered by this *Guide*.
- **Private Companies** are companies whose shares are not offered for sale to the public. The shares of a private company:
 - are usually owned by relatively few shareholders;
 - have never been, and cannot be, traded on securities markets or stock exchanges or otherwise offered for sale to the public; and
 - usually cannot be transferred unless certain restrictions are observed.
- **Special Act Corporations** are companies incorporated by a special Act of Parliament (Canada) or of the Legislative Assembly (British Columbia) by passing a private or public Act. In British Columbia, those are the companies that have not been recognized as a company, and have not been converted into a society under section 96 (2) of the *Societies Act*. Federally, special Act corporations are corporations that are excluded from Part 1, Section 5 of the *Business Corporations Act* (Canada), and include, for example, banks, railways, telephone, insurance, trust, and loan companies. In British Columbia, they include school boards, drainage and sewer disposal boards, park boards, religious orders, professional bodies, schools, unions, universities and colleges.

As these companies are relatively rare, their incorporation process, organization or the maintenance are not covered in the *Guide*. Information regarding this may be obtained from the clerk of the House (see the official websites of the Canadian Parliament or the British Columbia Legislative Assembly).

- **Community Contribution companies** (“CCC” or “C3”) are hybrids that fall between for-profit businesses and not-for-profit enterprises. They are taxable corporations which can generate a profit but no more than 40% of the profits may be paid out as dividends. They must have a community purpose beneficial to society at large or to a segment of society that is broader than the group of persons who are related to the community contribution company and include, the provision of health, social, environmental, cultural, educational or other services. Upon dissolution after providing for any debts, any remaining assets must be transferred to a like entity.

- **Benefit Companies** are for-profit companies that commit to conducting their business in a responsible and sustainable manner. A benefit company must also promote one or more public benefits that have a positive effect for a group of people (other than business shareholders), communities, organizations, or the environment. The public benefits may include any of the following activities of an artistic, charitable, cultural, economic, educational, environmental, literary, medical, religious, scientific or technological nature. A benefit company must publish an annual benefit report and post it on its website (if it has one).

As the CCC and the benefit companies are quite new, only their incorporation process is covered in the *Guide*. If there is a demand for the organization or the maintenance process, they will be covered in a future update to the *Guide*. In the meantime, see the link: **Community Contribution Companies** in Appendix C (Some Useful Websites) of Chapter 21.

- **Unlimited Liability Companies** or “ULC” is a hybrid body corporate. Unlike a limited liability company (discussed above), in the event of the company’s failure where the maximum an individual shareholder could lose would be the amount that the individual originally paid for his or her shares, the shareholders of the ULC are jointly and severally liable to satisfy the debts and liabilities of the ULC on dissolution or liquidation. The *Notice of Articles* of a ULC must contain a statement to this effect. Therefore, the ULC has the appearance of functioning as a corporation but has none of the advantages of a limited liability company and is generally only used as a vehicle for US tax purposes. Under U.S. tax law, unless the ULC elects to be classified as a corporation, the Internal Revenue Service classifies it as a partnership if it has more than one shareholder, and disregards it if it has a single shareholder, with the result that various tax attributes, such as income, losses, interest expenses and taxes payable by a ULC are treated as those of the individual shareholders of the ULC.

- **Business Number**

The federal **Business Number** (BN) is a numbering system that simplifies and streamlines the way businesses deal with the federal government and is based on the idea that there will be one identifying number for each business. The BN includes the four major accounts of Canada Revenue Agency (CRA):

- corporate income tax;
- import/export;
- payroll deductions; and
- goods and services tax/harmonized sales tax.

There are other types of CRA accounts that the BN does not include.

The BN consists of 15 characters divided into two parts: the registration number and the account identifier:

Registration Number				Account Identifier										
1	2	3	4	5	6	7	8	9	R	P	0	0	0	0
									Program Identifier		Reference Number			

The Province of British Columbia has entered into a partnership with CRA to use the BN as a convenient way for businesses to identify themselves when communicating with federal and provincial governments.

The Corporate Registry, under the authority of the *Business Number Act*, is collecting the BN's for both corporations applying for registration in British Columbia and corporations currently registered in British Columbia. This will allow corporations to use their BN as an identifier the next time they communicate with the Corporate Registry.

This Guide is divided into chapters covering each task that a person looking after corporate records may be requested to document when working with British Columbia companies.

- Several chapters cover the recognition, registration and organization of companies:
 - the **Incorporation, Amalgamations** and **Continuations** chapters respectively cover the creation (recognition) by way of **incorporation, amalgamation** and **continuation** of companies;
 - the **Extra-Provincial Companies** chapter covers the registration, maintenance and dissolution of extra-provincial companies in British Columbia; and
 - the **Organization** chapter explains the organization of a company after its incorporation.
- Several other chapters describe the procedures for keeping a recognized company in existence and in good standing with the Registrar:
 - the **Records** chapter explains the requirements for maintaining the company's official documents or "records" in the **Records Book** of the company;
 - the **Registered and Records Offices** chapter describes the Registered and Records offices and changes which may occur to either or both offices during the life of a company; and
 - the **Annual Maintenance** chapter describes the requisite annual procedures to maintain a company, particularly the filing of yearly annual reports and the holding of annual general meetings, or passing annual consent resolutions. This chapter also explains the requirements under the Act for the annual preparation of financial statements.
- Further, other chapters deal with other events that can occur over the life of the company affecting its ownership and management:

- the **Allotments** chapter describes how new shareholders may purchase shares in a company;
 - the **Transfers and Transmissions** chapter explains how existing shareholders may transfer shares to new or current shareholders, or when a shareholders die how their shares are to be transmitted to the persons entitled to the deceased's estate,;
 - the **Directors and Officers** chapter explains how new directors and officers may be appointed or may resign;
 - the **Dividends** chapter explains how and when the profits of a company may be distributed by way of dividends of various sorts; and
 - the **Repurchases and Redemptions** chapter explains how a company may repurchase or redeem shares from a shareholder.
- In addition, during its life, the company's charter or structure may be changed:
- the **Name Changes** chapter covers the simplest change: the change of the company's name; while
 - the **Authorized Share Structure** chapter covers more complex changes to the company's authorized share structure and the special rights and restrictions attached to the various classes of shares.
- the **Dissolutions** chapter describes the termination or winding up of a company's existence.
 - The **Restoration** chapter covers how a company can be restored or "revived" within 10 years of its dissolution.
 - the **Miscellaneous** chapter includes other useful documents which do not fit into any particular chapter or which relate to several chapters.
 - The **Transition** chapter sets out the procedure for the transition of private B.C. companies from the *Company Act* to the *Business Corporations Act*. Note: As this chapter is rarely used, the printed copy of this chapter is not available in the **Guide** but can be found on Evin Ross Publications Ltd.'s website.

Fully formatted copies of all the precedents used in this Guide are included on the CD-ROM or Flash Drive accompanying this Guide.

Regular updates for this Guide may be obtained by subscribing for the update service available at www.evinross.ca.

