



## **Aggressive Tax Reporting What it means to STEP Members**

*Moderator: Caroline Rhéaume*

*Speakers: Paul Lynch, KPMG LLP*

*Brett Anderson, Felesky Flynn LLP*

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## Overview

- Policy reasons for the Aggressive Tax Planning (“ATP”) reporting regime (“Regime”)
- Proposed section 237.3 of the *Income Tax Act* (Canada)
- Similar Provincial equivalents – Quebec in force for transactions after October 14, 2009; Ontario Budget 2013 announcement
- Case Studies – Highlight the challenges and practical impacts of these rules



## Global Context

- Forum on Tax Administration, Seoul Declaration, September 2006
- Global Forum on Transparency and Exchange of Information for Tax Purposes
- Joint International Tax Shelter Information Centre (JITSIC)
- Seven Country Tax Haven Working Group
- Leeds Castle Group



## Canadian Context- Federal

- ATP Regime intended to improve the fairness of the tax system
  - Some ATP arrangements undermine the tax base and the fairness and integrity of the tax system
  - The ATP regime represents a balancing act between
    - “a taxpayer’s entitlement to plan ... affairs in a manner that legally minimizes ... tax liability” and
    - “the need to ensure that the tax law is not abused”



## Canadian Context – Federal Objectives of the ATP Regime

- Help the CRA identify ATP arrangements in a timely manner
  - Identify potentially abusive tax avoidance transactions, their participants, provisions being relied on, etc.
- Discourage design and distribution of marketed tax plans
  - If it is not a “provocative” tax plan, there is no need for alternative fee arrangements, confidential protection or contractual protection
- Modify legislation
- Improve the effectiveness of the GAAR
  - Taxpayers do not self-assess under the GAAR
  - Unless there is a reporting regime, the CRA may not detect transactions that may rise to the level of “misuse” or “abuse”



## Canadian Context - Quebec

- January 2009 Working Paper – Aggressive Tax Planning (ATP)
- “ATP phenomenon was a matter of serious concern for Québec’s tax authorities”
- “ATP schemes undermine the integrity and the fairness of the tax system and threaten the tax base”
- “Aggressive tax planning is one of the risks tax administrations must deal with and, in managing this risk, obtaining information plays an essential role.”
- Builds upon tax shelter reporting rules



## Canadian Context - Quebec

- “The actions under consideration are measured and reasonable. They are substantially inspired by what is done in some OECD countries.”
- “the needs of Québec tax authorities in terms of fighting against ATP essentially consist of implementing measures that can alter the taxpayer’s risk/reward ratio and discourage tax intermediaries from using a new business model based on the design and distribution of off-the-shelf tax products.”



## Summary of Canadian Legislation

Federal – Section 237.3 (Proposed)

Quebec – Section 1079.8 (Enacted)

What do STEP Members need to know?

- That they, their client, or someone else connected to a transaction may have a reporting obligation, even in relatively routine situations
- Failure to report can result in a penalty and CRA can apply the GAAR to redetermine tax consequences without needing to prove “misuse or abuse”
- Precedents should be updated (e.g., engagement letters, opinion letters, etc.)

The detailed legislative provisions are reviewed below. It is important to understand that the ATP reporting rules raise two key concerns for a tax practitioner.

First, there is the need to properly advise their client of the reporting regime and whether reporting is required in respect of any particular transaction or series of transactions. It is possible that a failure to properly consider this issue could lead to a negligence claim by the client if the client is subject to penalties or if the tax benefits are reassessed and the taxpayer is prohibited from relying on the “no misuse or abuse” defense to the application of the GAAR.

Second, the regimes impose a reporting obligation on the advisor, and a failure to report when required can lead to the advisor being liable for a penalty, which can be equal to the amount of fees collected from the client under the federal regime.

It is likely that some modifications to the standard practices of many tax practitioners may be required to deal with these new rules appropriately. For example, as an advisor can have a reporting obligation even if they are not personally aware of all of the facts that give rise to that reporting obligation, it may be necessary to revise engagement letters and standard opinion disclaimers to assist with reliance on the due diligence defense.

For ease of reading, we have not included the word “proposed” before each reference to proposed section 237.3 of the Act.





## Section 237.3

- subsection 237.3(2) – imposes a reporting obligation in respect of a “reportable transaction”
- Key question – is there a “reportable transaction”?
  - Two part question:
    1. Is there an “avoidance transaction” as part of the “series of transactions”?  
and
    2. Are there 2 of 3 potential “hallmarks” of an ATP?

The preamble to definition of “reportable transaction” in section 237.3(1) reads as follows:

“reportable transaction”, at any time, means an avoidance transaction that is entered into by or for the benefit of a person, and each transaction that is part of a series of transactions that includes the avoidance transaction, if at the time any two of the following paragraphs apply in respect of the avoidance transaction or series:

[Note – the remainder of the definition describes the three “hallmarks” and is reviewed on the following slides.]

Each element of this definition is reviewed in detail on the next few slides, but there are a few critical takeaways for STEP members at this point.

The avoidance transaction need only be part of the “series” of transactions, and may not be part of the transactions of which the STEP member is aware.

Also, once there is an “avoidance transaction” – every transaction that is part of that series becomes a “reportable transaction”.



## Section 237.3

### 1. Is there an “avoidance transaction” as part of the “series of transactions”?

- Both expressions have very broad meanings
- The answer to this question will very often be yes, and the focus of the analysis is on the “hallmarks”

“avoidance transaction” is defined by cross reference to section 245(3), where that term is defined as follows:

An avoidance transaction means any transaction

(a) that, but for this section, would result, directly or indirectly, in a tax benefit, unless the transaction may reasonably be considered to have been undertaken or arranged primarily for bona fide purposes other than to obtain the tax benefit; or

(b) that is part of a series of transactions, which series, but for this section, would result, directly or indirectly, in a tax benefit, unless the transaction may reasonably be considered to have been undertaken or arranged primarily for bona fide purposes other than to obtain the tax benefit.

Given the breadth of the definition of “tax benefit” in subsection 245(1) and the expansive definition of “avoidance transaction” the existence of an avoidance transaction has been conceded in nearly all GAAR case law to date. It is likely a fairly safe assumption that if there is any element of tax planning in developing the transactions, there very well could be an avoidance transaction in the series of transactions.

The term “series of transactions” also has been given a very broad meaning for purposes of the Act, as the courts have interpreted subsection 248(10) as expanding on the common law definition of a series such that a series will include not only the pre-ordained series of transactions that give rise to the tax benefit, but also any transaction completed in contemplation of that series. Moreover, contemplation is not only prospective, so a series of transactions that did not contain an avoidance transaction at the time implemented can become part of a series of transactions that includes an avoidance transaction if an avoidance transaction is completed after the original series and that later transaction took into account the earlier series. For a recent discussion, see the Supreme Court of Canada’s decision in *Copthorne Holdings Ltd. v. R.*, 2011 SCC 63.



## Hallmarks - Preliminary Question

### Is there an advisor or promoter?

- Advisor – very broad, includes anyone who provides any assistance or advice regarding the creation, developing, planning, organizing, or implementing the transaction or series
- Promoter – also broad, includes anyone who promotes or sells a tax plan, makes a statement that a tax benefit could arise, or accepts consideration in respect of certain arrangements
- Question – are all tax practitioners not only “advisors” but also “promoters”?

A preliminary question for each of the hallmarks is whether there is an “advisor” or “promoter”. Each of these terms is defined in subsection 237.3(1) as follows: “advisor”, in respect of a transaction or series of transactions, means each person who provides, directly or indirectly in any manner whatever, any contractual protection in respect of the transaction or series, or any assistance or advice with respect to creating, developing, planning, organizing or implementing the transaction or series, to another person (including any person who enters into the transaction for the benefit of another person).

“promoter”, in respect of a transaction or series of transactions, means each person who

- (a) promotes or sells (whether as principal or agent and whether directly or indirectly) an arrangement, plan or scheme (referred to in this definition as an arrangement”), if it may reasonably be considered that the arrangement includes or relates to the transaction or series;
- (b) makes a statement or representation (whether as principal or agent and whether directly or indirectly) that a tax benefit could result from an arrangement, if it may reasonably be considered that
  - (i) the statement or representation was made in furtherance of the promoting or selling of the arrangement, and
  - (ii) the arrangement includes or relates to the transaction or series; or
- (c) accepts (whether as principal or agent and whether directly or indirectly) consideration in respect of an arrangement referred to in paragraph (a) or (b).



## Hallmark 1 – Fee

- para (a) of “reportable transaction” - the “fee” hallmark

1. Is an “advisor” or “promoter” entitled to a “fee” in respect of the avoidance transaction or series?
2. Is the fee:
  - based on the amount of the tax benefit resulting from an avoidance transaction;
  - contingent upon the obtaining of (or the failure to obtain) a tax benefit; or
  - attributable to the number of persons who participate in the avoidance transaction or who have access to advice regarding the tax consequences from the avoidance transaction?

The first hallmark is set out in paragraph 237.3(a):

(a) an advisor or a promoter, or any person who does not deal at arm's length with the advisor or promoter, has or had an entitlement, either immediately or in the future and either absolutely or contingently, to a fee that to any extent

- (i) is based on the amount of a tax benefit that results, or would result but for section 245, from the avoidance transaction or series,
- (ii) is contingent upon the obtaining of a tax benefit that results, or would result but for section 245, from the avoidance transaction or series, or may be refunded, recovered or reduced, in any manner whatever, based upon the failure of the person to obtain a tax benefit from the avoidance transaction or series, or
- (iii) is attributable to the number of persons
  - (A) who participate in the avoidance transaction or series, or in a similar avoidance transaction or series, or
  - (B) who have been provided access to advice or an opinion given by the advisor or promoter regarding the tax consequences from the avoidance transaction or series, or from a similar avoidance transaction or series;



## Hallmark 1 – Fee

(notes continued)

“fee” is defined in subsection 237.3(1) as follows:

“fee”, in respect of a transaction or series of transactions, means any consideration that is, or could be, received or receivable, directly or indirectly in any manner whatever, by an advisor or a promoter, or any person who does not deal at arm's length with an advisor or promoter, for

- (a) providing advice or an opinion with respect to the transaction or series;
- (b) creating, developing, planning, organizing or implementing the transaction or series;
- (c) promoting or selling an arrangement, plan or scheme that includes, or relates to, the transaction or series;
- (d) preparing documents supporting the transaction or series, including tax returns or any information returns to be filed under the Act; or
- (e) providing contractual protection.

Again, fairly broad definitions could allow this hallmark to exist in non-obvious situations.



## Hallmark 2 – Confidential Protection

- para (b) of “reportable transaction” – the “confidential protection” hallmark
  1. Has an advisor or promoter (or non-arm’s length person) obtained “confidential protection” in respect of the avoidance transaction or series?
    - Generally – confidential protection is anything that limits the disclosure, to any person (including CRA), of the details of the series
    - Should not be met where an advisor states that others cannot rely on an opinion, provided no limit on disclosing details
      - Practice point – review your standard engagement letters/opinions
    - Should not exist if advisor or promoter agrees to keep client’s information confidential

The second hallmark is set out in paragraph (b) of the definition of “reportable transaction” as follows:

(b) an advisor or promoter in respect of the avoidance transaction or series, or any person who does not deal at arm's length with the advisor or promoter, obtains or obtained confidential protection in respect of the avoidance transaction or series,

(i) in the case of an advisor, from a person to whom the advisor has provided any assistance or advice with respect to the avoidance transaction or series under the terms of an engagement of the advisor by that person to provide such assistance or advice, or

(ii) in the case of a promoter, from a person

(A) to whom an arrangement, plan or scheme has been promoted or sold in the circumstances described in paragraph (a) of the definition “promoter”,

(B) to whom a statement or representation described in paragraph (b) of the definition “promoter” has been made, or

(C) from whom consideration described in paragraph (c) of the definition “promoter” has been received; or

“confidential protection” is defined in subsection 237.3(1) as follows:

“confidential protection”, in respect of a transaction or series of transactions, means anything that prohibits the disclosure to any person or to the Minister of the details or structure of the transaction or series under which a tax benefit results, or would result but for section 245, but for greater certainty, the disclaiming or restricting of an advisor's liability shall not be considered confidential protection if it does not prohibit the disclosure of the details or structure of the transaction or series.



## Hallmark 3 – Contractual Protection

- para (c) of “reportable transaction” - the “contractual protection” hallmark
  1. Does anyone have “contractual protection” in respect of the avoidance transaction or the series of transactions?
- Contractual protection can exist if:
  - there is financial protection for anyone against a failure to achieve the tax benefit or to fight a dispute
  - a promoter agrees to provide any assistance with a tax dispute (even if not compensated for assistance)

The third hallmark is set out in paragraph (c) of the definition of “reportable transaction” as follows:

(c) either

(i) the person (in this subparagraph referred to as the “particular person”), another person who entered into the avoidance transaction for the benefit of the particular person or any other person who does not deal at arm's length with the particular person or with a person who entered into the avoidance transaction for the benefit of the particular person, has or had contractual protection in respect of the avoidance transaction or series, otherwise than as a result of a fee described in paragraph (a), or

(ii) an advisor or promoter in respect of the avoidance transaction or series, or any person who does not deal at arm's length with the advisor or promoter, has or had contractual protection in respect of the avoidance transaction or series, otherwise than as a result of a fee described in paragraph (a).





## Hallmark 3 – Contractual Protection

(notes continued)

“contractual protection” is defined in subsection 237.3(1) as follows:  
“contractual protection”, in respect of a transaction or series of transactions, means

(a) any form of insurance (other than standard professional liability insurance) or other protection, including, without limiting the generality of the foregoing, an indemnity, compensation or a guarantee that, either immediately or in the future and either absolutely or contingently,

- (i) protects a person against a failure of the transaction or series to achieve any tax benefit from the transaction or series, or
- (ii) pays for or reimburses any expense, fee, tax, interest, penalty or similar amount that may be incurred by a person in the course of a dispute in respect of a tax benefit from the transaction or series; and

(b) any form of undertaking provided by a promoter, or by any person who does not deal at arm’s length with a promoter, that provides, either immediately or in the future and either absolutely or contingently, assistance, directly or indirectly in any manner whatever, to a person in the course of a dispute in respect of a tax benefit from the transaction or series.





## Reportable Transaction - Consequences

- If there is a reportable transaction, many people involved in series may have a reporting obligation
- Failure to satisfy the reporting obligation can lead to:
  - Penalties
  - The GAAR can apply to deny the tax benefit, with no need for the CRA to prove “misuse or abuse”

Once it is determined that there is an avoidance transaction and two of the three hallmarks exist in connection with the series of transaction, every transaction in the series is a reportable transaction. As discussed below, many people could have a reporting obligation in respect of those reportable transactions.



## Operational Elements: 237.3(2)-(17)

- Who must report (2)-(4)
- By when (5)
- Non-compliance resulting in deemed application of the GAAR (6)
- Abrogation of limitation periods (7) for penalties under (8)
- Monetary penalties for non-compliance (8)
- Joint and several liability for penalties (9)
- Limits on advisor or promoter non-compliance penalty (10)
- Due diligence exemption (11)
- Reporting compliance does not result in an admission that the GAAR applies or that any transaction is part of a series of transactions (12)
- Enforcement of inspection, audit, disclosure, search provisions (13)
- Non-application of provisions to tax-shelter or flow-through share offerings (14)-(16)
- Solicitor – client privilege exception (17)



## Who has a reporting obligation?

- Every person for whom a tax benefit results from a reportable transaction or from any other reportable transaction that is part of the series (e.g., the taxpayer)
- Every person who has entered into an avoidance transaction that is a reportable transaction for someone else's benefit (e.g., trustee, general partner)
- Every advisor or promoter (and non-arm's length persons) entitled to any of 4 types of "fees": the 3 listed in Hallmark 1 or a fee for providing contractual protection
- Practical tip – if avoid charging the four type of fees, an advisor may avoid a reporting obligation (client may still have one)

Subsection 237.3(2) sets out the reporting requirement as follows:

An information return in prescribed form and containing prescribed information in respect of a reportable transaction must be filed with the Minister by

- for
- (a) every person for whom a tax benefit results, or would result but for section 245, from the reportable transaction, from any other reportable transaction that is part of a series of transactions that includes the reportable transaction or from the series of transactions;
  - (b) every person who has entered into, for the benefit of a person described in paragraph (a), an avoidance transaction that is a reportable transaction;
  - (c) every advisor or promoter in respect of the reportable transaction, or in respect of any other transaction that is part of a series of transactions that includes the reportable transaction, who is or was entitled, either immediately or in the future and either absolutely or contingently, to a fee in respect of any of those transactions that is
    - (i) described in paragraph (a) of the definition "reportable transaction" in subsection (1), or
    - (ii) in respect of contractual protection provided in circumstances described in paragraph (c) of the definition "reportable transaction" in subsection (1); and



## Who has a reporting obligation?

(notes continued)

(d) every person who is not dealing at arm's length with an advisor or promoter in respect of the reportable transaction and who is or was entitled, either immediately or in the future and either absolutely or contingently, to a fee that is referred to in paragraph (c).

Note that while the definitions of advisor and promoter are fairly broad, only those advisors or promoters who receive fees described in hallmark 1 or fees for providing contractual protection will have a reporting obligation. Accordingly, while the scenarios that give rise to a reporting obligation for the taxpayer are quite diverse, an advisor should be able to conclude they do not have a reporting obligation by reviewing the types of fees they charged in respect of a file. However, an advisor who charges any of the four types of fees in a circumstance where they believe there is no avoidance transaction or that neither of the other two hallmarks exist should proceed with caution as those hallmarks may exist even though the particular advisor is not aware of them. The reporting obligation is triggered by the existence of the facts, not the knowledge of those facts, subject to the due diligence defense.



## When/How to Fulfill Filing Obligation?

- An information return in prescribed form
- Transactions in a series can be reported on one form  
- EVERY transaction must be reported
- Reporting by one person may fulfill the reporting obligations of all persons
- June 30<sup>th</sup> of the calendar year following the calendar year in which the transaction first became a reportable transaction in respect of the person

Subsection 237.3(2) requires an information return in prescribed form be filed. As of writing, no prescribed form has been released.

Subsection 237.3(3) provides that the filing requirement that is triggered for each reportable transaction in a series that contains an avoidance transaction (again, every transaction in that series is a reportable transaction) can be satisfied by filing one form that reports each transaction. The provision reads as follows:

For greater certainty, and subject to subsection (11), if subsection (2) applies to a person in respect of each reportable transaction that is part of a series of transactions that includes an avoidance transaction, the filing of a prescribed form by the person that reports each transaction in the series is deemed to satisfy the obligation of the person under subsection (2) in respect of each transaction so reported.

Subsection 237.3(4) provides that if any person with a reporting obligation in respect of a reportable transaction files an information return in respect of that reportable transaction, all other persons with a reporting obligation in respect of that reportable transaction will be deemed to have fulfilled their reporting obligation. The provisions reads as follows:



## When/How to Fulfill Filing Obligation?

(notes continued)

For the purpose of subsection (2), if any person is required to file an information return in respect of a reportable transaction under that subsection, the filing by any such person of an information return with full and accurate disclosure in prescribed form in respect of the transaction is deemed to have been made by each person to whom subsection (2) applies in respect of the transaction.

Care should be exercised when relying on this provision as other people with a reporting obligation about one or two reportable transactions in the series may not be aware of all of the transactions in the series. Such persons may fulfill their reporting obligations (taking into account the due diligence defense) but that reporting will not satisfy the reporting obligations of those with knowledge or more transactions in the series.

Subsection 237.3(5) sets out the deadline for when information returns must be filed as follows:

An information return required by subsection (2) to be filed by a person for a reportable transaction is to be filed with the Minister on or before June 30 of the calendar year following the calendar year in which the transaction first became a reportable transaction in respect of the person.

A transaction only becomes a reportable transaction once there is an avoidance transaction and two hallmarks in respect of the avoidance transaction or series. These events may occur long after the particular transaction is concluded, but if the transaction is part of the series of transactions a reporting obligation can arise at this later time.



## GAAR Deemed to Apply

- One of the most adverse implications of these rules is that GAAR can be deemed to apply, without the Minister having to establish “misuse” or “abuse”
  - The tax consequences may be determined as is reasonable in the circumstances to deny the tax benefit
- Deemed application of the GAAR only occurs if:
  - the taxpayer has not satisfied their reporting obligation (narrower than original proposals);
  - any person is liable to a penalty under subs. 237.3(8); and
  - the penalty or interest on the penalty has not been paid

Subsection 237.3(6) sets out the circumstances in which the GAAR is deemed to apply:

Notwithstanding subsection 245(4), subsection 245(2) is deemed to apply at any time to any reportable transaction in respect of a person described in paragraph (2)(a) in relation to the reportable transaction if, at that time,

- (a) the obligation under subsection (2) of the person in respect of the reportable transaction, or any other reportable transaction that is part of a series of transactions that includes the reportable transaction, has not been satisfied;
- (b) a person is liable to a penalty under subsection (8) in respect of the reportable transaction or any other reportable transaction that is part of a series of transactions that includes the reportable transaction; and
- (c) the penalty under subsection (8) or interest on the penalty has not been paid, or has been paid but an amount on account of the penalty or interest has been repaid under subsection 164(1.1) or applied under subsection 164(2).

In the original proposed legislation, the GAAR was deemed to apply if any person with a reporting obligation failed to satisfy their reporting obligation. This has been narrowed to circumstances where the taxpayer fails to satisfy their obligation. When an advisor is the one who reports the series of transactions, care should be taken to confirm that all transactions of which the taxpayer is aware are included in the disclosure. As discussed above, the reporting by the advisor only satisfies the clients obligations if all reportable transactions of which the client is aware are disclosed.



## Penalty

- Each person who fails to file a required return is liable to a penalty
- The amount of the penalty is the total of
  - each and every fee to which each advisor and promoter (or non-arm's length persons) is, or may become, entitled; and
  - that is any of 4 types of "fees": the 3 listed in Hallmark 1 or a fee in respect of contractual protection
- No time limits for assessing the penalty
- Joint and several liability for the penalties among those liable for a penalty
- Advisors and Promoters – maximum penalty is the amount of the fee received by that advisor or promoter in respect of the transaction

The provisions relevant to the penalties that can be imposed for failing to satisfy a reporting obligation are subsections 237.3(7) through (10), which read as follows:

(7) Notwithstanding subsections 152(4) to (5), the Minister may make any assessments, determinations and redeterminations that are necessary to give effect to subsection (8).


(8) Every person who fails to file an information return in respect of a reportable transaction as required under subsection (2) on or before the day required under subsection (5) is liable to a penalty equal to the total of each amount that is a fee to which an advisor or a promoter (or any person who does not deal at arm's length with the advisor or the promoter) in respect of the reportable transaction is or was entitled, either immediately or in the future and either absolutely or contingently, to receive in respect of the reportable transaction, any transaction that is part of the series of transactions that includes the reportable transaction or the series of transactions that includes the reportable transaction, if the fee is

- (a) described in paragraph (a) of the definition "reportable transaction" in subsection (1); or
- (b) in respect of contractual protection provided in circumstances described in paragraph (c) of the definition "reportable transaction" in subsection (1).





## Penalty (notes continued)



(9) If more than one person is liable to a penalty under subsection (8) in respect of a reportable transaction, each of those persons are jointly and severally, or solidarily, liable to pay the penalty.

(10) Notwithstanding subsections (8) and (9), the liability of an advisor or a promoter, or a person with whom the advisor or promoter does not deal at arm's length, to a penalty under those subsections in respect of a reportable transaction shall not exceed the total of each amount that is a fee referred to in subsection (8) to which that advisor or promoter, or a person with whom the advisor or promoter does not deal at arm's length, is or was entitled, either immediately or in the future and either absolutely or contingently, to receive in respect of the reportable transaction.



## Due Diligence Exception

- Persons otherwise required to file are not liable for a penalty if they have exercised the degree of care, diligence and skill to prevent the failure to file that a reasonably prudent person would have exercised in comparable circumstances
- An advisor may avoid penalties if they can demonstrate that, based on reasonable enquiries, they concluded there was no reporting obligation or if they report the transactions they are aware of
- Can a taxpayer establish due diligence defense by obtaining an opinion that there is no reporting obligation in the circumstances?
- Can an advisor rely on their own opinion that there is no reporting obligation?

Subsection 237.3(11) provides the due diligence defense:

A person required to file an information return in respect of a reportable transaction is not liable for a penalty under subsection (8) if the person has exercised the degree of care, diligence and skill to prevent the failure to file that a reasonably prudent person would have exercised in comparable circumstances.



## Other Provisions

- Subsections 237.3(12) – (16) are set out in the notes but will not be discussed.
- Subsection 237.3(17) – provides that a lawyer that is an advisor is not required to disclose any information that is protected by solicitor-client privilege

Subsections (12) through (17) read as follows:

(12) The filing of an information return under this section by a person in respect of a reportable transaction is not an admission by the person that

- (a) section 245 applies in respect of any transaction; or
- (b) any transaction is part of a series of transactions.

(13) Without restricting the generality of sections 231 to 231.3, even if a return of income has not been filed by a taxpayer under section 150 for the taxation year of the taxpayer in which a tax benefit results, or would result but for section 245, from a reportable transaction, sections 231 to 231.3 apply, with such modifications as the circumstances require, for the purpose of permitting the Minister to verify or ascertain any information in respect of that transaction.

(14) For the purpose of this section, a reportable transaction does not include a transaction that is, or is part of a series of transactions that includes,

- (a) the acquisition of a tax shelter for which an information return has been filed with the Minister under subsection 237.1(7); or
- (b) the issuance of a flow-through share for which an information return has been filed with the Minister under subsection 66(12.68).



## Other Provisions (notes continued)

(15) Notwithstanding subsection (8), the amount of the penalty, if any, that applies on a person under that subsection in respect of a reportable transaction shall not exceed the amount determined by the formula

$A - B$

where

A is the amount of the penalty imposed on the person under subsection (8), determined without reference to this subsection; and

B is

(a) if the reportable transaction is the acquisition of a tax shelter, the amount of the penalty, if any, that applies on the person under subsection 237.1(7.4) in respect of the tax shelter,

(b) if the reportable transaction is the issuance of a flow-through share, the amount of the penalty, if any, that applies on the person under subsection 66(12.74) in respect of the issuance of the flow-through share, and

(c) in any other case, nil.

(16) Subsection (14) does not apply to a reportable transaction if it is reasonable, having regard to all of the circumstances, to conclude that one of the main reasons for the acquisition of a tax shelter, or the issuance of a flow-through share, is to avoid the application of this section.

(17) For greater certainty, for the purpose of this section, a lawyer who is an advisor in respect of a reportable transaction is not required to disclose in an information return in respect of the transaction any information in respect of which the lawyer, on reasonable grounds, believes that a client of the lawyer has solicitor client privilege.



## Application

- In respect of avoidance transactions that are entered into after 2010 or that are part of a series of transactions that began before 2011 and is completed after 2010
- If the series began before 2011, the definition of confidential protection is modified to exclude standard prohibitions on disclosure of tax advice in agreements entered into before March 4, 2010
- Information returns that are, technically, required to be filed earlier, are deemed to be filed on time if filed within 120 days of Royal Assent
- Practical issue – when does a series end?

The coming into force of subsection 237.3 is set out in section 356 of Part 5 of Bill C-48 (Second Reading, March 8, 2013). Section 237.3 is applicable in respect of avoidance transactions that are entered into after 2010 or that are part of a series of transactions that began before 2011 and is completed after 2010, except that, in its application to an avoidance transaction that is part of a series that began before 2011, the definition “confidential protection” in subsec. 237.3(1) is to be read as follows:

“confidential protection”, in respect of a transaction or series of transactions, means anything that prohibits the disclosure to any person or to the Minister of the details or structure of the transaction or series under which a tax benefit results, or would result but for section 245, but does not include a prohibition on disclosure that relates to an agreement entered into before March 4, 2010 between an advisor and his or her client for the provision of accounting, legal or similar tax advisory services, and for greater certainty, the disclaiming or restricting of an advisor's liability shall not be considered confidential protection if it does not prohibit the disclosure of the details or structure of the transaction or series.

If the filing of an information return under s. 237.3 would be required before July 1, 2012, the information return is deemed to be filed before that day if it is filed before the day that is 120 days after the day on which Bill C-48 receives Royal Assent.

There can be some difficulty determining when a series of transactions that began before 2011 is completed.



## Quebec Disclosures

New Penalty for GAAR

Mandatory Disclosures

Preventive Disclosures



## Quebec Penalty Regime for GAAR

- Taxpayer:
  - 25 % of additional tax payable (or reduced refund)
  - Except if:
    - Preventive or mandatory disclosure made, or
    - Due diligence defense applies
- Adviser: 12.5 % of consideration received
  - Except if:
    - Preventive or mandatory disclosure made by taxpayer, or
    - Due diligence defense applies to adviser or taxpayer



## Quebec – Definition of "Adviser"

- “adviser” in respect of a transaction means a person or partnership that provides help, assistance or advice regarding the design or implementation of the transaction, or that commercializes or promotes it;





## Quebec - Mandatory Disclosure

Three conditions:

1. Transaction (or series) gives rise to a tax benefit of at least \$25,000 for the year or an impact on income of \$100,00 or more for they year
2. An “adviser” was retained, and
3. The transactions is a confidential transaction or there is conditional remuneration

Prescribed form: TP-1079.DI (11 pages long)

Due date: normal filing deadline for the year of the transaction or the year that income was impacted



## Quebec – Failure to disclose

\$10,000 + \$1,000 day (maximum \$100,000) and extension of the limitation period by 3 years, and

If GAAR Applies:

- 25% penalty
- Adviser penalty

Can make a voluntary disclosure



## Quebec - Application

- Transactions completed after October 14, 2009, however
- A transaction that is part of a series of transactions that began before October 15, 2009, and was completed before January 1, 2010, is not subject to disclosure.



## Quebec – Preventive Disclosure

- Objective:
  - Avoid extended reassessment period
  - Avoid GAAR penalties
- Same prescribed form



## Quebec – Preventive Disclosure

### Preventive disclosure deadline

- A taxpayer that elects to make a preventive disclosure must submit a duly completed preventive disclosure form by the deadline for filing the taxpayer's income tax return for the taxation year during which the transaction **began** to be carried out.



## Quebec – Failure to disclose

- GAAR penalties
- Extended Reassessment period



## Federal/Quebec Comparison

	Quebec	Federal
Transaction	Tax Benefit $\geq$ \$25 000 or Impact on income $\geq$ \$100 000	Avoidance Transaction
Advisor	Yes	Yes
Contractual arrangement : 1) Conditional remuneration 2) Confidentiality 3) Contractual protection	# 1 or # 2	2 of 3
Failure to disclose	<input checked="" type="checkbox"/> \$10 000 \$ + 1 000 \$/day <input checked="" type="checkbox"/> Extended reassessment period <input checked="" type="checkbox"/> GAAR Penalties (25 % / 12.5%)	<input checked="" type="checkbox"/> Remuneration <input checked="" type="checkbox"/> Denial of tax benefit



## Case Study 1

- Facts
  - Dad owns shares of a corporation, wants to “freeze” his value, transfer growth to his two adult children
  - Dad does not want his current wife to know about the transfer
  - Dad asks his corporate lawyer for assistance
  - Corporate lawyer engages tax accountant to design transactions, has accountant sign confidentiality agreement to prevent disclosure to the wife





## Case Study 1

- Facts
  - Transactions completed include:
    - Dad transferring all common shares to corporation for fixed value preferred shares
    - Each adult child subscribing for 100 common shares for \$100
  - Accountant's standard practice for tax planning advice is to charge one fee that covers the advice, filing the related returns and responding to any queries from CRA audit



## Case Study 1

- Facts
  - Accountant advises corporate lawyer that Dad deferred tax of approximately \$1 million through the transaction
  - Corporate lawyer’s billable time was \$5,000, but given the dollar values involved, he billed the taxpayer \$10,000
- Federal Issues
  - Is there a “reportable transaction”?
  - If so, who has a reporting obligation and what does each person have to report?
- Quebec Issues



## Case Study 1 – Analysis

### Issue 1

- Is there an avoidance transaction? If no, stop
- If yes, is there an advisor or promoter? If no, stop
- If yes, do two of the three hallmarks exist?
  - Is an advisor or promoter entitled to a fee that is described in paragraph (a) of the definition of reportable transaction?
  - Did an advisor or promoter obtain “confidential protection”?
  - Does any person have “contractual protection”?

### Issue 2

- Who obtained a tax benefit?
- Of the advisers and/or promoters, who was entitled to a fee described in paragraph (a) of the definition of reportable transaction or provided contractual protection?



## Case Study 2

- Facts
  - Dr. who has carried on practice through a PC wants to wind-down his practice, asks accountant for advice
  - Accountant devises a plan, tells Dr. he can get access to cash in PC for “capital gains” tax rates instead of “dividend” rates
  - Assets of PC liquidated, only cash remains in PC
  - Shares of PC sold to brother-in-law (“**BIL**”) for a note
  - BIL sells shares of PC to wholly owned corporation (“**BILCo**”) for shares and note



## Case Study 2

- Facts
  - PC declared a dividend and paid it to BILCo by note (“**PC Note**”)
  - BILCo paid note owing to BIL with PC Note, BIL used PC Note to pay note owing to Dr.
  - Dr. reports sale of PC shares as capital gain
  - Accountant only charged hourly rate



## Case Study 2 - Analysis

- Is there a reportable transaction?
- Does the answer change if Dr. provides BIL with an indemnity for any tax that BIL may owe, now or in the future, as a result of the transactions?
- Does the answer change if there is the indemnity described above and the accountant's standard engagement letter stated that Dr. was not to disclose the transaction steps to any other individuals who may be considering similar transactions?



## Summary of Key Takeaways

- A reportable transaction can arise in almost any file with a tax aspect, however minor
- While a tax practitioner may be able to limit their requirement to report, need to properly advise clients on their reporting obligations
- Failure to report can result in a penalty and CRA can apply the GAAR to redetermine tax consequences without needing to prove “misuse or abuse”
- Precedents should be updated (e.g., engagement letters, opinion letters, etc.)
- Need to review all files where there is a “series” that could end after 2010, file reporting form within 120 days of subsection 237.3 receiving Royal Assent



**Thank You**

Questions?