LEGAL BUSINESS REPORT
ALPERT LAW FIRM
THE TAX LAW PROFESSIONALS
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# VOLUNTARY DISCLOSURES - PART II

**This issue of the Legal Business Report provides current information to the clients of Alpert Law Firm on the rules relating to the tax treatment of Voluntary Disclosures. Alpert Law Firm is experienced in providing legal services to its clients in tax dispute resolution and tax litigation, tax and estate planning matters, corporate-commercial transactions and estate administration. Howard Alpert has been certified by the Law Society as a Specialist in Estates and Trusts Law, and also as a Specialist in Corporate and Commercial Law.**

**Pursuant to subsection 220(3.1) of the *Income Tax Act* ("Act"), the Canada Revenue Agency ("CRA") has wide discretion to give equitable relief to a taxpayer accepted into the Voluntary Disclosures Program ("VDP") by waiving penalties and interest that would otherwise be payable under the Act. A taxpayer may also receive relief from prosecution. On December 15, 2017, the CRA issued Information Circular IC00-1R6 entitled "Voluntary Disclosures Program" outlining a program for taxpayers to make an application to correct inaccurate or incomplete information, or to disclose information not previously reported. A "taxpayer" in the context of the VDP includes an individual, an employer, a corporation, a partnership or a trust. This program applies to disclosures made after March 1, 2018.**

The Minister's ability to grant interest and penalty relief under the VDP is limited to any taxation year that ended within the previous 10 years before the calendar year in which the application is filed. However, interest relief may be granted in respect of interest that accrued during the 10 previous years before the calendar year in which the application is filed, regardless of the taxation year in which the tax debt originally arose. There is no limitation period applicable to the ability of the Minister to examine unreported income. The Minister can assess back taxes, interest and penalties for an infinite number of years, while only offering relief from interest and penalties for the most recent 10 years.

## A. CIRCUMSTANCES UNDER WHICH VDP RELIEF WILL BE CONSIDERED

The CRA has outlined specific circumstances under which VDP relief may be granted, which include circumstances where a taxpayer: (i) failed to fulfill his obligations under the applicable act; (ii) failed to report any taxable income he received; (iii) claimed ineligible expenses on a tax return; (iv) failed to remit source deductions for employees; (v) failed to report an amount of goods and services tax ("GST"); (vi) failed to file information returns; or (vii) failed to report foreign income that is taxable in Canada.

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The CRA has also listed the following examples of circumstances that will not be eligible for the VDP: (i) tax returns with no tax owing; (ii) provisions in the Act under which a taxpayer can elect specific treatment of certain transactions; (iii) advance pricing arrangements for certain transactions; **(iv) applications that depend on an agreement being made at the discretion of the Canadian competent authority under a provision of a tax treaty; (v) bankruptcy returns; (vi) post-assessment requests for penalty or interest relief; (vii) income derived from criminal activity; and (viii) transfer pricing adjustments or penalties. Matters related to transfer pricing will be referred to the Transfer Pricing Review Committee for their consideration under subsection 220(3.1) of the Act.**

**There are two different subprograms relating to applications for the VDP and the CRA will determine the appropriate subprogram for each disclosure on a case-by-case basis. The CRA is not required to grant relief to all applications made to the VDP. In exercising discretion, the Minister is guided by principles of procedural fairness, which require decisions to be made in good faith and promote the objects of the Act. The CRA reserves the right to audit or verify any information provided in a VDP application, whether it is accepted under the VDP or not. If there is misrepresentation in the information provided due to neglect, carelessness, willful default, or fraud, a reassessment can be issued at any time for any tax year to which the misrepresentation relates, not just those years included in the VDP application. Any relief granted by the VDP as a result of the misrepresentation will be cancelled. If relief is denied, the taxpayer may request penalty and interest relief in accordance with the "taxpayer relief provisions". The commentary below discusses (i) the General Subprogram; and (ii) the Limited Subprogram:**

## (1) GENERAL SUBPROGRAM

The General Subprogram is the default subprogram unless the Limited Subprogram applies. If the VDP application is accepted under the General Subprogram, a taxpayer will not be charged penalties, subject to the 10 year limitation period, and will not be referred for criminal prosecution. Full interest will be charged for the 3 most recent years of returns required to be filed. The Minister may grant partial interest relief to a taxpayer at his or her discretion, which generally will be 50% of the interest owed for assessments that precede the 3 most recent years of returns required to be filed. The amount of partial interest relief granted may differ from 50% in some circumstances. A "sophisticated" taxpayer is not specifically precluded from accessing relief under the General Subprogram.

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### (2) LIMITED SUBPROGRAM

The Limited Subprogram offers reduced relief compared to the General Subprogram. The VDP application will be considered under the Limited Subprogram if the CRA determines that the taxpayer or a closely related party was intentionally non-compliant. In addition, where a corporation having gross revenues exceeding $250,000,000 in at least 2 of its last 5 taxation years will generally be considered under the Limited Subprogram. The CRA may take a consolidated approach when determining whether the $250,000,000 threshold has been met by considering all related entities. Alternatively, in some circumstances, which are as yet unspecified, these types of corporations may be considered under the General Subprogram.

The Limited Subprogram provides that: (i) relief will be limited to immunity from prosecution and gross negligence penalties, but a disclosing taxpayer will receive no relief from other applicable penalties or interest arrears; and (ii) a disclosing taxpayer will be required to waive their rights of objection and appeal with respect to the substance of their disclosure and any consequential tax assessments.

The CRA may consider the following factors in determining whether an application should be dealt with through the Limited Subprogram: (i) efforts made to avoid detection; (ii) the dollar amount; (iii) the years of non-compliance, (iv) the sophistication of the taxpayer; and (v) whether the disclosure is made subsequent to official CRA statements declaring its intended specific focus on an area of compliance (e.g. the launch of a compliance project or campaign) or following broad-based CRA correspondence (e.g. a letter issued to taxpayers working in a particular sector about a compliance issue). For example, a taxpayer who opened an offshore bank account in 2010 and has been transferring undeclared business income earned in Canada to that account would not normally qualify under the General Subprogram. No single factor is necessarily determinative. A sophisticated taxpayer may still correct a reasonable error under the General Program.

The current rules relating to the Limited Subprogram create uncertainty for the taxpayer in not knowing whether an application will be considered under the Limited Subprogram or the General Subprogram. This will likely dissuade a taxpayer from making an application under the VDP.

## B. GST/HST DISCLOSURES

There are three subprograms relating to the VDP disclosures for GST/HST under the *Excise Tax Act*, which are discussed below:

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## (1) WASH TRANSACTIONS SUBPROGRAM

Disclosures involving GST/HST that involve eligible "wash transactions" may fall under this subprogram. A wash transaction generally occurs when a taxpayer supplies goods or services, but fails to collect and remit tax as required, and the recipient of the goods or service was entitled to an input tax credit. If the application is granted, the taxpayer is entitled to full relief from all applicable penalties and interest.

The CRA will consider granting the relief if the following conditions are met: (i) the taxable supply was made to a registrant entitled to a full input tax credit, a federal department, or participating provincial government; (ii) the taxpayer must have a history of voluntary compliance with their GST/HST obligations, and must not have been previously assessed for the same matter; (iii) the taxpayer must have implemented corrective methods to ensure future compliance; and (iv) the taxpayer must not have been negligent or careless in satisfying its GST/HST obligations.

In contrast to the VDP requirement relating to the Act, the taxpayer must only provide disclosures of non-compliance relating to the 4 calendar years before the date the application is filed to satisfy the completeness requirement. For greater certainty, all other VDP requirements relating to the Act must be complied with.

## (2) GST/HST GENERAL SUBPROGRAM

The General Subprogram for GST/HST disclosures is basically similar to the General Subprogram for disclosures under the Act. The following types of disclosures will usually be considered under this subprogram: (i) non-eligible "wash transactions"; (ii) reasonable errors; (iii) failures to file information returns; (iv) no gross negligence or deliberate avoidance of tax; or (v) over-claimed rebates.

In contrast to the VDP requirement relating to the Act, the taxpayer must only provide disclosures of non-compliance relating to the 4 calendar years before the date the application is filed to satisfy the completeness requirement. For greater certainty, all other VDP requirements relating to the Act must be complied with.

## (3) GST/HST LIMITED SUBPROGRAM

The Limited Subprogram for GST/HST disclosures is basically similar to the Limited Subprogram for disclosures under the Act. The following types of disclosures will usually be considered under the GST/HST Limited Subprogram: (i) where GST/HST was charged or collected but not remitted; (ii) where the registrant made active efforts to

avoid detection (e.g. participation in underground economy); (iii) where the disclosure is made after an official CRA statement regarding its intended specific focus of compliance (e.g. the launch of a compliance project or campaign) or following broad-based CRA correspondence (e.g. a letter issued to registrants involved in a particular sector about a compliance issue); or (iv) there was deliberate or willful default or carelessness amounting to gross negligence.

## C. EFFECTIVE DATE OF DISCOSURE

The effective date of disclosure is the date the CRA receives a completed and signed VDP application. If the application is valid, the taxpayer is granted: (i) protection from the initiation of prosecution related to the disclosure; and (ii) penalty relief after this date. An invalid application has no effective date of disclosure.

If necessary, a taxpayer may have up to 90 days from the effective date of disclosure to submit additional CRA-requested information and/or documentation to complete the application. Additional time may be authorized for complex applications or in extraordinary circumstances, upon receipt of a written request from the taxpayer. If additional information and/or documentation is not received within the stipulated time, the CRA may commence enforcement action, investigation and subsequent prosecution.

## D. PRE-DISCLOSURE DISCUSSION SERVICE

Prior to March 1, 2018, a taxpayer could elect to proceed with the VDP on a “no-name” basis, but this option has now been replaced by the Pre-Disclosure Discussion Service. Under the previous “no-name” option, a taxpayer, through an authorized representative, could anonymously engage the CRA in discussion regarding the taxpayer’s qualification for the VDP, and then make an informed choice of whether to proceed with a named disclosure. If the taxpayer chose to proceed with a “no-name” disclosure, the taxpayer was required to provide his name to the CRA within 90 days of the CRA receiving the VDP application. If the taxpayer did not disclose his name within 90 days, this VDP disclosure application was closed and the taxpayer was no longer protected from penalties or investigation in the future.

The Pre-Disclosure Discussion Service will permit the taxpayer’s representative to speak to a CRA official anonymously about the taxpayer’s situation to determine if the taxpayer will still wish to proceed with the VDP application process. This type of discussion with the CRA is: (i) informal; (ii) non-binding; and (iii) may occur before the

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identity of the taxpayer is revealed. For complex technical reporting issues, taxpayers will be referred to a CRA official in a specialized audit area.

Participation in the Pre-Disclosure Discussion Service does not constitute acceptance into the VDP and the CRA retains the ability to audit, penalize, or refer a case for criminal prosecution. It is unclear how this service will differ from the general assistance that the CRA currently provides taxpayers. More details about this service will likely be released by the CRA in the future.

## E. SECOND DISCLOSURE BY THE SAME TAXPAYER

The CRA expects taxpayers to remain compliant after using the VDP. Under normal circumstances, a taxpayer is entitled to utilize the benefits of the VDP only once.

**A second disclosure for the same taxpayer may be considered by the CRA if the circumstances surrounding the second disclosure are beyond the taxpayer's control and relate to a different matter than the first application. At the time of making a second disclosure, a taxpayer must provide his name and specify that he had previously made a disclosure.**

If it is discovered during the course of the disclosure review that the taxpayer had previously made a disclosure and the taxpayer has not disclosed this fact, the CRA may deem the disclosure to be invalid for VDP purposes. If the second disclosure relates to the same issue that was previously denied for the VDP on the basis that it was incomplete due to information not being received by the stipulated date, then the second disclosure will be denied.

## F. SOLICITOR-CLIENT PRIVILEGE

A taxpayer may make a voluntary disclosure to the CRA personally or through an agent. When a taxpayer makes a voluntary disclosure through a lawyer, the taxpayer is protected by solicitor-client privilege with respect to the taxpayer's identity, solicitor-client communications and any documents revealed to a lawyer up until the time the voluntary disclosure is made.

Generally, solicitor-client privilege does not extend to communications between an accountant and their client. However, in certain circumstances solicitor-client privilege can extend to communications between an accountant and a taxpayer where an accountant and a lawyer together assist a taxpayer in making a voluntary disclosure.

Where an accountant acts as a representative of the taxpayer to communicate facts or issues to a lawyer for the purpose of giving or obtaining legal advice, the communication is viewed as communication between the taxpayer and the lawyer and is therefore protected by solicitor-client privilege.

Once a voluntary disclosure is initiated and the taxpayer's history is revealed to the CRA, any solicitor-client privilege that may have attached to the disclosed documents is lost.

In ***Visser v. M.N.R.***, 89 DTC 5172, a taxpayer argued that the documents requested for verification by the CRA in a voluntary disclosure were subject to solicitor-client privilege. The Court held that in applying for the VDP, there is an implied undertaking to produce supplementary information, regardless of its privileged character. Solicitor-client privilege cannot be claimed against documents related to matters forming the substance of a disclosure because in making the voluntary disclosure a taxpayer is demonstrating an intention to waive solicitor-client privilege with respect to the relevant documents.

## G. ONTARIO VOLUNTARY DISCLOSURE POLICY

Ontario's tax laws provide civil penalties, fines and jail terms for taxpayers, vendors, registrants and benefit recipients who do not comply voluntarily with their legal obligations. In most cases, the maximum punishment for those who are convicted of offences is a fine of twice the amount of tax evaded, plus a jail term of two years. Convicted taxpayers must also pay the unreported taxes, plus civil penalties and interest. Those who voluntarily approach the Ontario Ministry of Finance to correct inaccurate or incomplete information, or to disclose information that they never previously reported, will not be prosecuted.

The Ontario Ministry of Finance has outlined similar conditions to those of the federal VDP for corporations and individuals who wish to voluntarily disclose a violation of a provincial tax statute. The Ministry requires that five conditions be satisfied for the voluntary disclosure to qualify as valid:

(i) Disclosure must be voluntary as determined by the Ministry and initiated by the individual, corporation, or their representative. The disclosure will not be considered voluntary if it was motivated by any enforcement action by the Ministry. For the purposes of voluntary disclosure, an enforcement action is deemed to include any action by the Ministry that is directed toward the detection or resolution of non-compliance with a statute administered by the Tax and

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Benefits Administration of the Ontario Ministry of Finance. Individuals, corporations, and their authorized representatives who are unsure if they want to make a voluntary disclosure are entitled to discuss their situation on a no-name basis with a Ministry representative responsible for handling voluntary disclosures. After this discussion, up to a 90 day grace period will be granted for the preparation and submission of a detailed disclosure.

(ii) The disclosure must be full and accurate. The disclosing party will be responsible for all costs related to the submissions, calculations, schedules or other relevant information. Minor errors or omissions will not disqualify the disclosure under the Voluntary Disclosure policy, but material errors or omissions may result in penalties and prosecution.

(iii) The Ministry will verify the validity of all Voluntary Disclosures. Full cooperation with the Ministry is expected by making all books of account, records and documents available upon request and by answering questions which may arise. Failure to cooperate fully may result in the loss of protection under this policy.

(**iv) Full payment is expected of the total amount due, including interest, upon disclosure. Where the whole amount owing cannot be paid immediately, the Ministry may consider reasonable payment arrangements.**

**(v) The voluntary disclosure must be made to the Ministry.** The Ministry of Finance encourages voluntary compliance with the taxation statutes it administers, and all bona fide Voluntary Disclosures will be favourably received. This policy applies to taxation statutes administered by the Ministry of Finance including, but not limited to, the following: (i) Employer Health Tax Act; (ii) Estate Administration Tax Act, 1998; (iii) Fuel Tax Act; (iv) Gasoline Tax Act; (v) Land Transfer Tax Act; (vi) Mining Tax Act; (vii) Provincial Land Tax Act; (viii) Race Tracks Tax Act; and (ix) Tobacco Tax Act.

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