Grant Thornton

TAX ALERT

New mandatory disclosure rules

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Taxpayers, advisors, and promoters (and certain other parties) are required to disclose relevant information on certain tax planning or transactions to the CRA, under the new mandatory disclosure rules. Overall, the compliance burden for taxpayers, advisors, and promoters has significantly increased. These rules received Royal Assent on June 22, 2023.

Taxpayers and their advisors should determine whether they have reporting requirements under the new mandatory disclosure rules introduced as part of Bill C-47, which came into effect on June 22, 2023. The rules contain the following changes:

1. An expansion of the reportable transaction rules in the Income Tax Act (the Act), along with a significantly reduced reporting deadline;
2. A new requirement to report notifiable transactions;
3. A new requirement for certain corporations to report uncertain tax treatments;
4. An extension of the normal reassessment period in non-compliance situations; and
5. New related penalties (some of which accrue daily or weekly)

Effective dates

As outlined below, the new mandatory disclosure rules apply as follows:

Type of transaction	Reporting requirement application	Penalty provision application
Reportable transactions **and** Notifiable transactions	Applicable to transactions entered into after June 22, 2023	Applicable to transactions entered into after June 22, 2023
Uncertain tax treatment	Applicable to taxation years beginning after 2022	Will not apply to taxation years that begin before June 22, 2023

Reportable transactions

Under the new mandatory disclosure rules[1], a transaction[2] is reportable if it is an "avoidance transaction" as defined under the General Anti-Avoidance Rule (GAAR), and has one of the following three hallmarks (previously two were needed):

1 **Fees:** A promoter or tax advisor in respect of the transaction is entitled to a direct or indirect fee (absolutely or contingently) that is:
   - based on the tax benefit;
   - contingent upon obtaining a tax benefit; or
   - attributable to the number of taxpayers that participate in or have been provided access to the advice given on the tax consequences of the transaction.

   A taxpayer will not be subject to new reporting requirements as a result of paying a contingent fee for the preparation of a Scientific Research & Experimental Development (SR&ED) claim under subsection 37(11) of the Act.

2 **Confidential Protection:** A promoter or tax advisor requires "confidential protection" with respect to an avoidance transaction. The prohibition on disclosure specifically involves the tax treatment of the avoidance transaction (e.g., where the client is prohibited to disclose the details or structure of the transaction involving a tax treatment to any person or to the Minister of National Revenue).

3 **Contractual Protection:** The taxpayer, promoter or advisor (or certain other specified or non-arm's length persons), receives "contractual protection" in respect of the transaction, including any form of insurance (other than standard professional liability insurance), or any form of undertaking provided by a promoter that aids a person in a dispute about the tax benefit.

The definition of contractual protection excludes insurance or other protections (e.g., guarantees) integral to an arm's length agreement for the sale of a business where it's reasonable to consider that the insurance or protection is:

- intended to ensure the purchase price takes into account any liabilities of the business immediately prior to the sale and;
- obtained primarily for purposes other than to achieve a tax benefit from the sale or a series of transactions

This exception doesn't extend to tax liability insurance or similar protection related to an avoidance transaction.

The new mandatory disclosure rules significantly expand the scope of a "reportable transaction" and increase the compliance burden for the relevant parties as each party would need to report separately. Furthermore, the new penalties can be significant, and the filing deadline is reduced to only 90 days.

1 Section 237.3 of the Act.
2 A "transaction" for the purposes of this article also includes the series of transactions in which a particular transaction is included.

The changes are summarized in Table 1 as follows:

Table 1: High-level comparison of previous and the new rules

	Newly enacted legislation	Previous legislation
Purpose test	Transaction is an avoidance transaction if it can reasonably be concluded that one of the main purposes of entering into the transaction is to obtain a tax benefit	Transaction is an avoidance transaction if the primary purpose of entering into the transaction is to obtain a tax benefit (i.e., definition under GAAR)
Three hallmarks	Only needs to meet at least one of the three hallmarks	Must meet at least two of the three hallmarks
Reporting deadline	Within 90 days of the earlier of when the taxpayer (or anyone acting on behalf of the taxpayer) enters the transaction or become contractually obligated to enter the transaction	On or before June 30th of the calendar year following the year in which the transaction became a reportable transaction
Reporting obligation	All relevant parties (e.g., any taxpayer receiving a tax benefit[4] from the plan, anyone who has entered into the transaction on behalf of a taxpayer benefitting from the plan, and each advisor[5] or promotor) must file an information return in respect of the same reportable transaction. The reportable transaction reporting obligation wouldn't apply to persons that provide only clerical or secretarial services with respect to the planning.	One person can file an information return in respect of the reportable transaction on behalf of all relevant parties.
Penalties for non-compliance	Significant penalties for taxpayers, promoters, advisors and certain other parties, which can be as high as $100,000 or more (see Table 2 for details)	The amount of the penalty for each relevant party is generally the total of all the fees for the transaction that the promoter or advisor is entitled to receive

4 A taxpayer expecting to receive a tax benefit under the plan based on their tax treatment of the reportable transaction must also report, even if their filing position is successfully challenged.
5 An advisor may be excluded from the reporting requirements where there is solicitor-client privilege as defined in relevant case law.

Notifiable transactions

In addition to the "reportable transactions" disclosure requirement, the government introduced a similar requirement to report "notifiable transactions", which include types of transactions the CRA has either found to be abusive or to be of interest (and for which more information is needed to determine whether the transaction is abusive).

The CRA published five notifiable transactions on November 1, 2023:

1. Avoiding or deferring the deemed disposition rules for trusts in certain circumstances.
2. Using "back-to-back" arrangements to circumvent the thin capitalization rules or Part XIII withholding tax.
3. Using partnerships in derivative transactions to generate artificial losses and avoid the application of the "straddle transaction" stop-loss rules.
4. Avoiding a deemed acquisition of control and the resulting tax attribute trading restrictions, in certain circumstances.
5. Temporarily obtaining bankruptcy status to reduce a forgiven amount in respect of a commercial obligation.

The transaction would only need to be substantially similar to a notifiable transaction, with the phrase "substantially similar" intended to be interpreted broadly and in favour of disclosure.

The CRA and the Department of Finance may designate additional notifiable transactions over time, and publish them on the CRA's website.

The provisions for the filing deadline, reporting obligation and penalties in respect of a "notifiable transaction" mirror those provisions for a "reportable transaction" described in Table 1 above.

While Québec's rules are beyond the scope of this article, it's notable that the Québec mandatory disclosure rules contain a requirement to report certain "determined transactions" to Revenu Québec, similar to the "notifiable transactions" that must be reported to CRA under the federal rules. Quebec's list of determined transactions currently includes avoiding the deemed tax attribution trading (similar to the federal rules), along with transactions involving payment to a non-treaty country and transactions used to multiply the capital gains deduction.

Uncertain tax treatments

The mandatory disclosure rules also include a new requirement to disclose particular uncertain tax treatments. An uncertain tax treatment is generally a tax position taken by the taxpayer for which there is uncertainty (less than 50% probability) over whether the position will be accepted as being in accordance with the tax law. The rules generally apply to a corporation that meets the following conditions for a taxation year:

- The corporation is required to file a Canadian income tax return for the year;
- The carrying value of the corporation's assets at the end of the year is $50 million or more;
- The corporation, or a consolidated group of which the corporation is a member, has audited financial statements in accordance with International Financial Reporting Standards (IFRS) or country-specific Generally Accepted Accounting Principles (GAAP) for domestic public companies (e.g., US GAAP); and
- One or more uncertain tax treatments are reflected in those audited financial statements.

Under the new rules, if a corporation meets the criteria for a tax year, the uncertain tax treatment(s) must be disclosed in an information return to be filed with the CRA no later than the date the corporate income tax return is due (e.g., six months after the taxation year-end). The penalties to the taxpayer for failure to report an uncertain tax treatment when required are significant (up to $100,000 – see Table 2 for details).

Reassessment period

Where a taxpayer has a mandatory disclosure reporting requirement (e.g., reportable transactions, notifiable transactions, uncertain tax treatments), the normal reassessment period[6] wouldn't begin in respect of the transaction until the taxpayer is compliant. In other words, a reassessment will not become statue-barred if these reporting requirements are not met.

6 Where an information return required under the mandatory disclosure rules is filed late, the reassessment period would be four years from the date it is filed for mutual fund trusts or corporations that are not Canadian-controlled private corporations, and three years for other taxpayers.

Penalties

The penalties for non-compliance with the new mandatory disclosure rules are summarized in Table 2 as follows:

Table 2: Penalties for failure to file

	Taxpayer		Each Promoter or Advisor
	Weekly penalty	Maximum penalty	
Reportable or notifiable transactions (Corporations with $50 million assets or more)	$2,000 per week	Greater of: a. $100,000 or b. 25% of tax benefit	Total of: • 100% of the fees charged for the transaction; • $10,000; and • $1,000 per day to a maximum of $100,000
Reportable or notifiable transactions (All other taxpayers)	$500 per week	Greater of: a. $25,000 or b. 25% of tax benefit	
Uncertain tax treatment	$2,000 per week for each position	$100,000 for each position	Not Applicable

Additional information

The new mandatory disclosure rules have received Royal Assent and became law on June 22, 2023. The rules are complex and the penalties for non-compliance are significant. Please reach out to your Grant Thornton advisor if you require assistance navigating the new rules.

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