INDIRECT TAX ALERT

Collins Barrow

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VOLUNTARY DISCLOSURES

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This article provides information about the Voluntary Disclosure Program (VDP) administered by the Canada Revenue Agency (CRA). The VDP encourages taxpayers to come forward voluntarily to declare information that may not have been previously reported. It may be used to divulge unreported or underreported financial information. Use of this provision provides defense against penalty and prosecution.

The CRA's Income Tax Information Circular IC00-1R3 states that the VDP can be used if a taxpayer "failed to fulfill their obligations under the applicable act, failed to report any taxable income they received, claimed ineligible expenses on a tax return, failed to remit source deductions of their employees, failed to report an amount of GST/HST, failed to file information returns and failed to report foreign sourced income that is taxable in Canada."

The VDP also entitles the taxpayer to come forward anonymously under a "No-Name Policy" that allows the taxpayer to achieve compliance and still remain unknown. No-name disclosures may be used in instances where a taxpayer is determining the validity of his or her particular situation under a VDP. This gives the taxpayer the chance to present the facts to the CRA and gain an understanding of the effects of remaining non-compliant or seeking coverage under a VDP.

Under the VDP, the taxpayer is required to satisfy all outstanding tax amounts as well as interest on the outstanding amounts. However, any applicable penalties will be waived. Relief from interest is also available in certain situations, depending on the nature of the transactions within the scope of the business.

Non-residents may also use the VDP and are subject to the same rules and requirements for a successful disclosure.

The criteria for a valid voluntary disclosure are as follows, as described in the CRA's Income Tax Information Circular IC00-1R3:

1. **The disclosure must be voluntary.** In the event the taxpayer has been contacted or informed by the CRA of an audit or similar investigation, or has been requested to file outstanding returns, the disclosure will not be considered valid. A disclosure submitted after any of the above enforcements will not be granted.
2. **The disclosure must be complete and accurate.** The facts provided in the disclosure must include all previously unreported or underreported information.
3. **The disclosure requires a penalty to exist.** As a result of the information being disclosed, if a penalty is not present, all such information will not be considered under a voluntary disclosure and should therefore be reported regularly.
4. **The disclosure must include information that is one year past due.** If the information included is less than one year old, it must be used to correct a previous return and it must include information that is one year past due.

The documentary requirements for a valid VDP must include an RC-199, which is a "taxpayer agreement." This form can be obtained from the CRA website. Personal information, as well as necessary CRA registration numbers, must also be included. In addition, depending on the specific program account that is involved in the disclosure, all necessary forms, slips and returns must be included. Finally, the disclosure must also include a detailed explanation of the facts and the taxpayer's validity under the VDP. Upon review, the CRA may request further information from the taxpayer before accepting the disclosure.

In recent years, due to taxpayers realizing that the CRA is aggressively pursuing non-compliance, Collins Barrow Toronto LLP has completed many voluntary disclosures on behalf of clients. Each case poses different facts and requires the understanding of the applicable legislation to accurately present the disclosure to the CRA.

IN THIS ISSUE

However, in our recent submissions since April 2013, one aspect that remains consistent is the complexity and inefficiency of the CRA's review of the disclosure process. For example, in instances where we present a disclosure for non-resident non-registrants, in addition to the full documentary requirements of a disclosure we also include an RC-1 requesting backdating of registration, an RC-59 authorizing us to speak with the CRA on behalf of the client and completion of all necessary tax returns. We understand it is CRA policy, upon receipt of this package, to send the various documents to the appropriate tax service centers across the nation for processing. As a result of different offices in different provinces processing what was submitted as a collective package, each separate portion of the disclosure is reviewed individually. If certain aspects of the disclosure are processed before others, the system might issue a request to file, an arbitrary assessment or even a notice of assessment with full penalty and interest. Undoubtedly, this results in delays and additional fees for our clients.

In response to these experiences with the VDP program, we strive to streamline the package we present to the CRA to minimize the need for additional information requirements. This helps to ensure that disclosures are processed in a timely manner for our clients.

Contact your Collins Barrow advisor for assistance or more information on the VDP. §

FI, LFI, SLFI AND SAM: WHAT DO THEY MEAN AND WHAT CAN THEY CAUSE?

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Revenue is a good thing; we are always looking for ways to increase it. But in the GST/HST world, dividend and interest revenue can reduce income in addition to causing huge compliance costs and issues. This can come as an unwelcome surprise to many taxpayers.

Subsection 149(1) of the *Excise Tax Act* (all references are to the ETA) is a deeming provision to determine if a person is a Financial Institution (FI). When an organization is an FI, the services it provides are exempt from GST/HST and consequently any GST/HST paid by the organization becomes an expense as no input tax credits (ITCs) may be claimed with exempt services. One note of interest: an individual can also be an FI.

Paragraph 149(1)(a) lists business types, which include organizations we would think of as financial institutions: banks, credit unions and insurance companies. Also included are pension plans, brokerage firms, investment plans, mutual funds and even tax discounters. When an organization's business type is listed in this section, it is an FI and is also designated as a Listed Financial Institution (LFI).

If an organization manages to escape from the business types listed under 149(1)(a), the Canada Revenue Agency (CRA) is still not finished; it has a few other tools available to ensnare an organization as an FI. Paragraphs 149(1)(b) and (c) contain two additional tests that can result in an organization being deemed a *de minimis* FI. These tests review the types of revenue an organization earns and the sources of revenue. The first test determines whether interest and dividend revenue (financial revenue) exceeds 10% of the organization's total revenue or is greater than $10 million in a year. The second test looks at whether the organization has interest revenue from credit cards, loans or advances greater than $1 million in a year with no allocation of revenue component.

The CRA does provide some relief for *de minimis* FIs. Subsection 149(4) excludes any dividend or interest revenue from a person that is related to the person whose revenue is being reviewed in the tests under paragraphs 149(1)(b) and (c). Furthermore, if the person is part of the non-profit sector (e.g. charity, NPO, municipality, public college or university, school authority or hospital), the *de minimis* test does not apply.

If an organization is an LFI or a *de minimis* FI and has total annual income in excess of $1 million, it will be required annually to complete GST Form 111, *Financial Institution GST/HST Annual Information Return.* Within this document, the CRA requires a detailed breakdown of revenue, purchases and other expenditures, imports, exports, ITC allocation methods and changes in use of capital property. The form is eight pages in length and will require an in-depth analysis of an organization's operations involving management information that would not be readily available in some companies.

Beyond GST Form 111, the CRA has one last request to exhaust the accounting world. If during a taxation year an LFI organization has a permanent establishment or partner in a participating province that is an HST zone and a permanent establishment or partner in a non-participating province, it is deemed to be a Selected Listed Financial Institution (SLFI). The federal government seeks to ensure that SLFI expenditures are not all made in a province that charges only GST, thus reducing expenses by the provincial component in the HST and causing unfair economic loss to an HST province.

The Special Attribution Method – or SAM – calculation is designed to review an organization's spending and determine specifically if there is a disproportionate amount in a non-participating province. In order to complete a SAM, an organization must record all GST/HST paid even though it cannot be claimed as an ITC. The CRA has specific rules in the Selected Listed Financial Institutions Attribution Method (GST/HST) Regulations within the *Excise Tax* Act on provincial attribution percentages specific to various legal structures and business types, which can require detailed management information.

The good news is, at the end of the SAM calculation there is a potential refund if too much GST/HST is paid compared to the provincial allocation. Conversely, if the allocation is not favourable, more GST/HST will be due. Unfortunately, more interest and dividend revenue are not always good things in the GST/HST world.

Contact your local Collins Barrow office for additional information on these issues and to discuss planning opportunities. §

Collins Barrow periodically publishes an *Indirect Tax Alert* for its clients and associates. It is designed to highlight and summarize the continually changing tax and business scene across Canada. While *Indirect Tax Alert* suggests general planning ideas, we recommend professional advice always be sought before taking specific planning steps.

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