

MONTHLY NEWSLETTER

The Voluntary Disclosure Program (“VDP”)



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Our goal is to provide updates on topical tax issues. Information contained in the newsletters is not meant to be a comprehensive summary of the issues raised. Rather, we wish to bring what we believe to be important issues to the attention of our valued clients. We would be pleased to discuss any questions that you, the reader, might have in greater detail.

BACKGROUND INFORMATION ABOUT THE VDP

Canada’s income tax system requires taxpayers to self-assess, report their income and pay the resultant tax each year. Taxpayers are also required to submit reporting information to the Canada Revenue Agency (“CRA”) in prescribed form and adhere to filing deadlines. Where a taxpayer has previously reported incorrect or incomplete information, or has failed to disclose the required information to the CRA entirely, the taxpayer may voluntarily come forward and disclose the errors in exchange for penalty relief. The taxpayer is required to pay all tax outstanding, plus, in most circumstances, interest applicable in respect of the tax to be paid.

Often, the penalties related to non-compliance can be extremely punitive, making the VDP an appealing option. Consider the following examples:

- 1) Form T1135 reports foreign investment assets where the aggregate cost of such property exceeds \$100,000. The maximum penalty for failure to file the form is \$2,500 per year. A taxpayer who has not filed the form for 4 years would be subject to a \$10,000 penalty (4 years x \$2,500 per year), even if they had properly reported the related income on their tax return. By coming forward under the VDP, the risk of penalty exposure can potentially be avoided.

- 2) Failure to report income in two or more consecutive years can result in a flat penalty of 20% of the unreported income, even if there is no resultant income tax payable. A taxpayer who fails to report \$5 of income in one year and a \$10,000 T4 slip in the next would be subject to a \$2,000 penalty (\$10,000 of unreported income x 20%). Again, the VDP would potentially allow the penalty to be avoided.

VDP CONDITIONS

The application for relief must be within 10 calendar years from the end of the year in respect of which the taxpayer is seeking relief. For example, if an application was made on February 1, 2015, relief is only available in respect of the 2005 and subsequent years.

The CRA will typically only accept a voluntary disclosure from a taxpayer once. A second disclosure will be considered if the taxpayer's non-compliance was due to factors beyond the taxpayer's control. A second disclosure must be a named disclosure as discussed below, and must disclose the fact that it is the second such disclosure for the taxpayer.

The CRA will consider the application made under the VDP valid where the disclosure:

- 1) Is made voluntarily;
- 2) Is complete;
- 3) Involves the application or the potential application of a penalty; and
- 4) Includes information that is at least one year past due.

The CRA considers a disclosure to have been made voluntarily where the CRA has not previously taken any enforcement action such as an audit or other investigation with respect to the specific issue being disclosed and CRA has not requested the information in writing or by phone. The taxpayer is required to provide full and accurate facts and documentation for all taxation years or reporting periods. Accordingly the taxpayer cannot limit a disclosure to select errors or omissions or to specific taxation years.

NAMED VS. NO NAMES DISCLOSURES

In a "named" disclosure, the identity of the taxpayer is revealed to the CRA in the initial submission requesting relief under the VDP. This approach is advisable where the issue is straightforward and almost certain to be accepted.

There are limited circumstances where the CRA will not accept a voluntary disclosure even where all of the above conditions are met. A "no-names" disclosure conceals the taxpayer's identity during the initial presentation of facts and related discussions with the CRA. This approach is often advantageous because it allows a taxpayer or their representative to discuss the situation with a VDP officer and to gain a better understanding of the CRA's position on the potential availability of relief with limited risk. Also, a no-name disclosure allows the taxpayer the opportunity to determine what information would need to be filed as part of the disclosure process. In a no-names disclosure, the taxpayer has 90 days from the effective date of disclosure to provide their identity and any required information.

CONCLUSION

The tax reporting landscape in Canada is constantly evolving. Legislative changes continue to increase the complexity of income tax reporting and the risk of errors and omissions thereon. The VDP offers a mechanism for taxpayers to adhere to the self-assessment requirements and mitigate potential penalties for non-compliance. We recommend seeking professional advice prior to proceeding with a voluntary disclosure. If you believe you may be eligible for the VDP, please do not hesitate to contact us for more information about the disclosure process.