Comité mixte sur la fiscalité de
l'Association du Barreau canadien

et

Comptables professionnels agréés du Canada
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Le 5 avril 2022

Monsieur Trevor McGowan
Directeur général
Division de la législation de l'impôt
Direction de la politique de l'impôt
Ministère des Finances du Canada
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Courriel : Consultation-Legislation@fin.gc.ca

**Objet : Propositions relatives aux opérations à déclarer et aux opérations à signaler**

Monsieur,

Veuillez trouver ci-joint un mémoire exposant le point de vue du Comité mixte sur la fiscalité de l'Association du Barreau canadien et de Comptables professionnels agréés du Canada (le Comité mixte) sur les propositions relatives aux opérations à déclarer et aux opérations à signaler incluses dans les propositions législatives publiées le 4 février 2022.

Le Comité mixte tient à remercier le Ministère pour sa volonté de participer au dialogue sur ces mesures et espère poursuivre ces travaux.

Des membres du Comité mixte et d'autres experts en fiscalité ont pris part aux discussions ayant abouti au mémoire et ont contribué à sa rédaction, notamment :

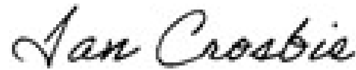
- Bruce Ball – CPA Canada
- Tara Benham – Grant Thornton LLP
- Fabio Bonanno – CPA Canada
- Cathie Brayley – Miller Thomson LLP
- Mike Dolson – Felesky LLP
- Kim Moody – Moodys Private Client Law LLP
- Hugh Neilson – Kingston Ross Pasnak LLP
- Carmela Pallotto – KPMG Canada
- Ken Saddington – Goodmans LLP
- Jeffrey Shafer – Blake, Cassels & Graydon LLP

- Ken Griffin – PwC LLP
- Rob Jeffery – Deloitte LLP
- Vivian Leung – CPA Canada
- Anthony Strawson – Felesky Flynn LLP
- Gwendolyn Watson – Torys LLP
- Peter Wong – Borden Ladner Gervais LLP

Les membres du Comité seront heureux de discuter de ces questions plus en détail si cela peut être utile.

Nous vous prions d'agréer, Monsieur, nos salutations distinguées.

David Bunn
Président, Comité sur la fiscalité
Comptables professionnels agréés du Canada



Ian Crosbie
Président, Section du droit fiscal
Association du Barreau canadien

c. c.

- Shawn Porter, sous-ministre adjoint délégué, Direction de la politique de l'impôt, ministère des Finances du Canada

**Submission of the Joint Committee on Taxation of The Canadian Bar Association and Chartered Professional Accountants of Canada**
**February 4, 2022 Draft Legislation on Reportable Transactions and Notifiable Transactions**

## INTRODUCTION

This submission sets out our comments and recommendations on the Draft Legislation released on February 4, 2022 relating to reportable transactions and notifiable transactions. It should be noted that the Chartered Professional Accountants of Canada will be making a separate submission on the uncertain tax treatment proposals given the different nature of these rules and the financial reporting issues associated with them. Consequently, this submission will focus on the proposals for reportable transactions and notifiable transactions.

According to the 2021 Federal Budget, "the lack of timely, comprehensive and relevant information on aggressive tax planning strategies is one of the main challenges faced by tax authorities worldwide." Based on this statement, it is assumed that the goal of the mandatory reporting proposals is to create a reporting system that provides the Canada Revenue Agency ("**CRA**") with information it would not receive otherwise on aggressive tax planning and sooner than other information is received through conventional tax compliance processes.

The OECD describes the key features of a mandatory reporting system as follows:

> "Mandatory disclosure regimes should be clear and easy to understand, should balance additional compliance costs to taxpayers with the benefits obtained by the tax administration, should be effective in achieving their objectives, should accurately identify the schemes to be disclosed, should be flexible and dynamic enough to allow the tax administration to adjust the system to respond to new risks (or carve-out obsolete risks), and should ensure that information collected is used effectively."[1]

The main objective is also set out clearly by the OECD:

> "The main objective of mandatory disclosure regimes is to increase transparency by providing the tax administration with early information regarding potentially aggressive or abusive tax planning schemes and to identify the promoters and users of those schemes."[2]

As discussed by the OECD, achieving the right balance is important. If too many transactions, and in particular, transactions that are not aggressive tax planning are subject to the rules, this will increase administration and costs for both the CRA and taxpayers without providing valuable incremental information to the CRA. The Appendix to this submission has more information from the OECD report which we believe is important to consider as Canada sets mandatory reporting rules.

[1] OECD (2015), Mandatory Disclosure Rules, Action 12 - 2015 Final Report, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, 9.

[2] Ibid.

Tax certainty is also important. Taxpayers and their advisors should have a clear understanding of what is reportable or notifiable and what is not. If the reporting requirements are not clear, then this can lead to over-reporting (i.e. information returns will be filed for routine tax planning and other transactions for which additional reporting would not be useful).

In our view, the short reporting deadline should influence the structure of these rules. These reporting requirements should be restricted to information that warrants a short deadline, being information that cannot wait until an income tax return or other filing is made. If the CRA requires additional information on a specific issue but that information will not be needed until the CRA reviews a tax return, that information should only be required to be provided as part of the regular tax compliance process. One-off issue reporting is more costly, and the chances of missing a relevant filing are higher when compared with filing an annual return.

In the balance of this submission, we provide our views on the detailed rules for reportable transactions and notifiable transactions. In our view, filing requirements will frequently arise for transactions or series of transactions that would not be considered aggressive tax planning and these will be areas where further refinement of the rules should be considered.

## GENERAL COMMENTS APPLICABLE TO BOTH REGIMES

### Implementation Date

The proposed changes to the reportable transaction rules and introduction of the notifiable transaction rules will impose significant additional compliance and reporting obligations on affected taxpayers. In particular, the changes to the definition of avoidance transaction combined with only needing one hallmark for reporting will significantly expand the range of reportable transactions. Combined with the entirely new notifiable transaction regime, taxpayers and their advisors will require a reasonable amount of time to understand the breadth of their obligations and develop the necessary systems and processes to identify transactions, capture the necessary information, and comply with their reporting obligations.

Larger, decentralized taxpayers will also face additional hurdles in order to educate their broader organization of the rules so that transactions that do not pass through the tax department can be properly assessed and reported if appropriate. Smaller taxpayers that do not have the resources of larger taxpayers will also face significant challenges.

These considerations make the January 1, 2022 effective date potentially problematic for a significant number of taxpayers, a situation that is significantly aggravated by the broad range of transactions that may be reportable transactions, which may include many transactions that provide a tax benefit but are not aggressive transactions in any way. There is a significant risk that the fact that these transactions are reportable will be missed by many taxpayers, who will assume the rules are focussed on aggressive strategies.

An additional concern with respect to the January 1, 2022 effective date is that some taxpayers will be offside of a 45-day deadline when the final rules become law. In particular, the 45-day reporting deadline may have already passed for some transactions. Although penalties will only apply after Royal Assent, the fact that some taxpayers will be automatically offside of specific tax rules upon enactment may create commercial issues. For example, covenants to financing agreements may require compliance with tax filing rules.

A series of transactions also raises concerns. For example, in a merger and acquisition transaction, the final step may be an amalgamation on January 1, 2022. In this situation, since the final step is in 2022, does that mean that the series is potentially reportable even though all other steps in the series occurred in 2021 or earlier?

> ***Recommendations***
>
> *We believe that all aspects of these rules should apply on Royal Assent generally and on a prospective basis. We also recommend that taxpayers are provided with an additional period of time to adapt their reporting systems to track any transactions or series of transactions that will be subject to the rules. If the proposals will apply commencing on January 1, 2022, the requirements to report should not apply until after Royal Assent, building in a reasonable period to collect the required information and prepare the information return that is required to be filed. In the case of a series of transactions, a series that commenced prior to January 1, 2022 should not be subject to the rules.*

**Materiality**

It would be consistent with the goal of the proposals, being to assist the CRA in identifying aggressive tax planning strategies that will affect tax revenues, if there were a requirement that the tax planning strategy in question be material to justify advance reporting.

As will be discussed further, we are concerned that routine tax planning may inadvertently trigger a hallmark in the reportable transaction rules or could be substantially similar to a notifiable transaction, notwithstanding that it will be unobjectionable to CRA when reviewed. The extent of this potential overbreadth could be reduced by excluding minor transactions through a materiality test. Under such an approach, it would not be necessary to examine whether a particular plan is reportable if the tax benefit in question is small.

In its report, the OECD explains the purpose of a *de minimis* test to both taxpayers and tax administrators:

> "A de-minimis filter could be considered as an alternative to, or in addition to, a broader threshold test and could operate to remove smaller transactions, below a certain amount, from the disclosure requirements. It would therefore narrow the ambit of the mandatory disclosure regime and reduce the risk of over-disclosure. It may also enhance the usefulness of the information collected because the focus would be on more significant transactions and

excessive or defensive filings could be reduced. This could reduce the costs and administrative burden for certain taxpayers and for the tax administration."[3]

***Recommendation***

*We recommend including a de minimis test or other filter in order to reduce the potential administrative burden for tax authorities and the compliance burden for taxpayers, especially for smaller businesses and their advisors.*

**Definition of "Advisor"**

The definition of an "advisor" under both sets of proposed rules is broad. In particular, it will include each person who provides any assistance or advice with respect to creating, developing, planning, organizing or implementing the transaction or series of transactions in question. As defined, advisors may not even know that they have a reporting requirement if they have been engaged to provide specific services with respect to the transaction without knowledge of the broader circumstances.

As an example, if an estate plan is being prepared for a taxpayer and it is determined that reporting of a transaction or a series is required, there may be many advisors employed by different firms or companies involved:

- an accountant or lawyer acting as an overall coordinator,
- a tax specialist providing tax advice,
- a corporate lawyer dealing with share reorganizations and other corporate work,
- an estate lawyer dealing with the drafting of wills,
- a lawyer dealing with family law issues,
- a valuator dealing with the valuation of certain assets, and
- a financial planner and/or investment advisor dealing with financial planning.

Using this example, we can foresee that the rules will be difficult for some advisors to comply with due to a number of uncertainties, which include:

- a specific advisor may not be aware of an aspect of the work being done which may give rise to a reporting requirement even though they are assisting with the plan;
- in a comprehensive plan, it may not be clear which aspects are part of the plan or the series and which are not;
- some of the advisors assisting in the plan may not be tax professionals, and may not be aware or understand the implications of the mandatory reporting proposals;
- those working on a very specific part of a plan may not know whether the plan was actually implemented; and
- the assistance provided by a particular advisor may be required for a broader plan but are considered to be routine when viewed in isolation.

[3] Ibid., 38 (paragraph 87).

As summarized in the Appendix to this submission, the OECD discusses these issues in its commentary on mandatory reporting. In particular, the OECD suggests an "advisor" should include persons who provide advice or assistance relating to the tax aspects of a transaction that causes the transaction to be a reportable transaction and that persons who provide services incidental to the transaction or series ought not to be burdened with reporting obligations where they did not have knowledge of the tax elements of the transaction or series.[4]

***Recommendation***

*Consideration should be given to narrowing the scope of advisors who are required to report under the proposed rules, and therefore, would be subject to a potential penalty if they fail to report. At a minimum, the proposals should be amended to recognize that a number of advisors could potentially be involved in setting up a reportable or notifiable transaction, but there may be a smaller circle of key decision-makers, including the taxpayer.*

*Although we recommend narrowing the scope of the legislation, examples in the explanatory notes would also be helpful to describe the key considerations for determining who is an "advisor" that has a reporting obligation, and especially those who are not part of the decision-making group*.

**Requirement for Multiple Reporting**

As just discussed, several advisors may be involved in a transaction and all of them could have a filing requirement for a transaction or series of transactions that is reportable. They may be from different firms or may be from one firm (or a combination). Additional concerns include whether some advisors will recognize the need to report and whether they will have sufficient information for the disclosure. The fact that an employee of a firm may have a reporting requirement themselves even if the firm reports has been raised as a concern.

Under the original rules for reportable transactions, subsection 237.3(4) stated that "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."

It is unclear why this subsection is being repealed and why multiple filings are required which may give rise to inconsistencies due to the different knowledge levels of each advisor.

[4] Ibid., at 36 (paragraph 77).

***Recommendation***

*Subsection 237.3(4) should not be repealed, and a similar rule should be included for notifiable transactions under section 237.4. The reporting requirement should apply at the firm level and not to individual members or employees of a firm.*

### Interaction of the proposed reporting requirements

It is possible that more than one of the proposed reporting requirements could apply to the same transaction or series of transactions. For example, a transaction could be substantially similar to a notifiable transaction and a hallmark also applies under the reportable transaction rules. The proposed legislation does not appear to deal with this possibility.

***Recommendation***

*Amendments should be made to the proposed legislation to clarify the requirements where a transaction or series of transactions is subject to more than one reporting regime. It should not be necessary to report the same information more than once and multiple penalties should not arise where the information was provided to the CRA under another reporting regime.*

## REPORTABLE TRANSACTIONS

For reportable transactions, the February 4, 2022 draft legislation proposes to broaden rules that already existed under section 237.3. The key changes are a much broader purpose test, requiring that only one hallmark apply rather than two and a much earlier filing deadline.

From a general perspective, we are concerned that the broadening of the rules will capture transactions that would not be consistent with the overall goals of the draft legislation based on the 2021 Federal Budget and may result in over-reporting. In particular, it will be important to ensure that common commercial practices do not cause a hallmark to apply in order to avoid potentially substantial broadening of the scope of these provisions beyond their stated purpose. Our more specific observations and recommendations are presented below.

### Avoidance Transaction

Under the current version of section 237.3, there must be an “avoidance transaction” for the rules to apply and this definition serves as an initial purpose test for the rules.

For the purposes of section 237.3, an avoidance transaction has the same meaning as in subsection 245(3) and means any transaction that 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. Under this test, transactions that were primarily commercial in nature would not be subject to the reporting rules.

Under the proposed change to the definition, avoidance transaction means a transaction if it may reasonably be considered that one of the main purposes of the transaction, or of a series of transactions of which the transaction is a part, is to obtain a tax benefit.

This is a very significant change. For a single transaction, the definition does not differentiate between tax benefits that are permissible under the rules of the Act and those that are more aggressive in nature. As an example, if an advisor assists an individual in transferring their unincorporated business to a corporation, and a joint election is made under subsection 85(1) to defer immediate Canadian tax on the transfer of assets to the corporation, this will be an avoidance transaction even though the taxpayer is using rules specifically designed for the transfer in question (as confirmed in Information Circular 88-2, *General Anti-Avoidance Rule: Section 245 of the Income Tax Act,* paragraph 11). Although this in itself will not create a filing requirement, if only one hallmark applies, a reporting requirement will exist.

The implications for a series of transactions are also a concern. Under the proposed rule, any individual transaction that is tax motivated may make the entire series of transactions reportable without any regard of the importance of the individual transaction when compared with the series as a whole. For example, if a holding company sells the shares of the operating company it owns, the series of steps to complete the sale will be an avoidance transaction if the operating company pays a relatively minor safe income dividend to the holding company prior to the sale. This dividend would generally be paid due to tax reasons, which meets the definition. We believe that a tax-motivated transaction that meets the proposed avoidance transaction definition will be common where a series of transactions has a main commercial purpose.

The missing element in this definition is a concept of materiality given the link to the general anti-avoidance rule has been dropped. In the incorporation of a business example, the quantum of the tax benefit in question is likely not significant in absolute terms. In the sale of a business example, the safe income dividend may not be significant when compared to the series of transactions as a whole. But, in both cases, the avoidance transaction purpose test has been met. Even if a hallmark does not apply, taxpayers and their advisors will need to verify this in a large number of situations even if the tax benefit is insignificant.

Overall, meeting the definition of avoidance transaction will not create a reporting requirement alone, but it does create a significant range of transactions where reporting will be required if one of the hallmarks apply.

***Recommendations***

*We believe that an element of materiality should be added to the avoidance transaction definition. Transactions that produce an insignificant tax benefit should not be subject to the rules.*

*Also, given that the range of potentially reportable transactions will be very large, the hallmarks will need to be carefully considered to ensure over-reporting will not arise. Although some clarifications have been proposed below for common commercial practices, we are concerned that other commercial steps will still trigger a hallmark.*

**Fee Hallmark**

An amendment to the fee hallmark contained in paragraph 237.3(1)(a) of the definition of reportable transactions has not been proposed. However, concerns have been identified since the definition of avoidance transaction is broader and only one hallmark needs to apply under the proposed changes to create a reporting requirement.

Under this hallmark, the factors to be considered include a fee that "is based on the amount of a tax benefit that results", "is contingent upon the obtaining of a tax benefit" or is "based on the number of taxpayers who participate". These factors can arise in commercial situations which do not appear to be consistent with the goals of the proposals. For example:

- ***Fees based on the value of the tax advice.*** Although professionals generally bill based on time, they also bill for specialized knowledge and know-how that they have transferred to a client. They may do this through a higher hourly rate or may simply "value" bill for the know-how and knowledge that is brought to bear in respect of the transaction. Many clients prefer this approach, and it does not necessarily indicate that the transaction is aggressive in tax policy terms. We are concerned because the "to any extent attributable" reference is broad and could apply to these common fee arrangements.

- ***Contingency work.*** It is unclear whether this hallmark will apply where the advisor is providing tax services in return for a contingent fee. Where this billing practice is used, there is usually an uncertainty as to whether a tax benefit exists or the quantum of that benefit prior to the services being provided, and the fee is based on the final amount of the tax benefit. This protects a client from being charged a fee that is unreasonable when compared to the benefit where uncertainty exists. This can occur in areas that are not "aggressive" tax planning. As an example, this practice is common for advisors assisting clients in Scientific Research & Experimental Development (SR&ED) filings given the complexities and uncertainties inherent in those rules. Similarly, concerns have been raised regarding legal services in tax disputes where the fee charged is based on the outcome.

- ***Fees based on the number of taxpayers.*** The hallmark criteria assumes that where a group of taxpayers are involved in a transaction where the fee is based on the number of participants, then the plan may be aggressive. This will not be the case in many situations. As an example, a large commercial reorganization may require the filing of dozens or hundreds of T2057s for the purpose of deferring capital gains (an avoidance transaction), and an accounting firm may bill for the preparation of the T2057s on a per-transferor basis given the work to be done for each taxpayer will be similar. The hallmark would apply as currently drafted. With ever increasing automation of tax work, this method of billing may become more common.

***Recommendations:***

*As the fee hallmark can trigger a reporting requirement on its own under the proposals, we recommend narrowing the proposed definition for the fee hallmark as follows:*

- *In the reference to value, there should be a more specific correlation between the tax benefit and the fee for this hallmark to apply. A reference to "any extent" is too broad and the wording used should be more focused.*

- *The issue of fees based on the number of taxpayers should be reconsidered. In particular, the sort of arrangements that are a concern should be more narrowly described.*

- *With the broader application of the reportable transaction rules, an exclusion should be provided for contingency work such as SR&ED claims or fees related to tax disputes that are based on a specific tax result. In the case of SR&ED claims, a large amount of information is already provided to the CRA including information on the fee paid to advisors.*

- *As observed by the OECD (see the Appendix), factors such as the location of the advisor, the urgency of the tax advice, the size of the transaction, the skill or reputation of the advisor or the scarcity of specific expertise could influence a fee amount, and these factors should be disregarded.*

- *Depending on how the other fee concerns are dealt with, a de minimis test should be considered based on the amount of the fee. A reference to fees being "to any extent attributable" to tax benefits could cause this hallmark to be met in far too many situations, as will a reference to fees being "to any extent attributable to the number of taxpayers who participate in the transaction or who have been provided access to advice given by the promoter or tax advisor".*

**Confidential Protection Hallmark**

In the case of the confidential protection hallmark, which is described in paragraph 237.3(1)(b) of the definition of "reportable transaction", we believe that the hallmark is too broad given that a reportable transaction can arise if this hallmark applies on its own.

Under paragraph 237.3(1)(b), "confidential protection" with respect to a transaction means "any limitation on disclosure" to any other person, including the CRA, that is placed by the promoter or the tax advisor on the taxpayer, in respect of the details or the structure of the avoidance transaction that gives rise to any tax benefit. Although the definition excludes a disclaimer of liability where a third party relies on an opinion, professionals may seek to limit the general communication of client advice by stating that the advice given cannot be passed on to others.

Many professionals include a confidentiality clause in engagement letters when they provide tax advice to clients. This practice helps prevent the free use of tax advice by others and situations where others

rely on tax advice or other information where the information or advice is inappropriate for them due to different facts or circumstances. These concerns can apply to non-controversial planning, such as an estate plan.

Professional advisors should not be required to remove these commercial terms from an engagement letter that reduces costs and risks for tax advisors.

As discussed in the Appendix, the OECD observed that the confidential protection is concerning when its purpose is to permit a promotor or advisor to sell the same aggressive tax plan to multiple taxpayers without tax authorities or competitors becoming aware of the plan.

> ***Recommendation***
>
> *The conditions of this hallmark should be revised so that the hallmark only applies where heightened confidentiality conditions were imposed that go beyond common practices for professional advice in general. One way to achieve this would be to focus on whether it is reasonable to conclude that none of the main reasons for the confidential protection was to prevent the Minister or a competitor from becoming aware of the details or structure of the transaction or series. If not, then the confidential protection hallmark should not apply.*

**Contractual Protection Hallmark**

The third hallmark refers to situations where the taxpayer or the person who entered into the transaction for the benefit of the taxpayer obtains "contractual protection" in respect of the transaction (otherwise than as a result of a fee described in the fee hallmark). This hallmark is set out in paragraph 237.3(1)(c) of the definition of reportable transactions and an amendment is proposed to subparagraph (i) which adds an exclusion for protection "as a form of insurance, protection or undertaking described in paragraphs (a) or (b) of the definition contractual protection that is offered to a broad class of persons and in a normal commercial or investment context in which parties deal with each other at arm's length and act prudently, knowledgeably and willingly."

Although the addition of this exclusion is appreciated, uncertainty remains on how the exception should be applied. As we discussed with you in 2021, the Committee was concerned that commercial transaction agreements (such as a merger and acquisition transaction) often contain contractual protection clauses in respect of a broad range of matters, including but not limited to taxes. In this case, the hallmark could apply and there could be an obligation to report. In recent years, it has become standard that the parties obtain insurance to replace the vendor's indemnification obligation for losses for breach of representations and warranties. The result is to reduce or eliminate holdbacks so more cash is in the hands of the vendor while at the same time ensuring that the purchaser retains indemnification – in this case paid by the insurer not the seller. Because of the broad language, the hallmark could apply with the result that numerous legitimate commercial transactions will have to be reported.

For example, in a share sale, the vendor can be considered a “promoter” who has granted “contractual protection” where the purchase agreement includes (i) indemnities related to pre-closing taxes, the potential application of Part III or Part III.1 tax or the amount of tax attributes (tax pools, CCA, etc.) or (ii) covenants for assistance in the event of disputes with third parties (which may include disputes related to tax outcomes expected to apply to the purchaser as a result of the transaction). We believe the proposed exclusion was aimed at dealing with these concerns but there is uncertainty on its application due to the reference to insurance, protection or undertaking “that is offered to a broad class of persons and in a normal commercial or investment context”. In this example, there are only two parties (the vendor and the purchaser), so it is unclear how a reference to “a broad class of persons” is to be interpreted.

The word “offered” may also cause confusion. In many cases, including those where there is no third-party insurance, the contractual protection is an integral component of the agreement as opposed to something that is offered on its own.

The hallmark may also be a concern when protection applies to an advisor. Many tax advisors include standardized limitation of liability and indemnity clauses in their engagement letters that cover tax advice. The exclusion described above for “contractual protection that is offered to a broad class of persons and in a normal commercial or investment context” is also included in clause (c)(ii)(B) of the definition. However, the concerns just discussed for commercial transactions also apply in this context – what does a “broad class of persons” mean and the reference to “offered” will cause confusion since the protection is just one part of the overall conditions of an engagement.

***Recommendations***

*To help address these issues, we have the following recommendations:*

- *Indemnities should be referred to specifically in the exclusion.*
- *The reference to a “broad class of persons” should be removed to avoid confusion.*
- *The word “offered” should be removed and a more general reference should be made to insurance, indemnity, protection or undertaking that is included as part of or related to a transaction or series of transactions.*

## NOTIFIABLE TRANSACTIONS

### Application and Scope

The legislation does not clearly deal with implementation considerations for notifiable transactions that are designated by the Minister of Revenue with the concurrence of the Minister of Finance at the time these rules first come into effect and when new notifiable transactions are designated.

***Coming into Force***

The new notifiable transaction legislation will apply to notifiable transactions entered into after 2021. However, the draft legislation and a sample notifiable transaction list were released on February 4,

2022. It is not clear whether the use of "sample" to describe the list indicates that these are the actual first group of notifiable transactions that will be designated and perhaps some of the wording may be edited or if the actual first group of notifiable transactions will be different than those described. Nor is it clear whether other pronouncements by the CRA that raise concerns with tax plans will interact with this new notifiable transaction process. However, the Taxpayer Bill of Rights issued by the CRA states in point 14 that taxpayers have the right to expect to be warned about questionable tax schemes in a timely manner.

Consequently, there is unnecessary confusion and uncertainty among advisors regarding whether significant efforts need to be expended as soon as possible to review historical records to identify involvement with any of the transactions listed on the sample list. For example, if a person provided advice months or even years before 2022 and that advice assisted a taxpayer early in 2022 in entering into a transaction that is designated, it appears that the advisor has a reporting requirement even though the transaction in question was not a notifiable transaction when the advice was provided.

***Recommendation***

*The coming into force provisions should clearly set out that they will only apply to transactions undertaken after the legislation is enacted and on a prospective basis. Transactions that have already occurred should not be subject to the rules unless a tax benefit arises after the date of Royal Assent.*

***Designation Process***

There is limited information regarding the process that will be followed by the Minister of National Revenue in designating a transaction or series of transactions and how the Minister of Finance will provide concurrence. The explanatory notes for subsection 237.4(3) state "Transactions can be designated in the manner that the Minister of National Revenue considers appropriate, such as on the Canada Revenue Agency webpage."

It is important that a standard process be put in place to give taxpayers and advisors sufficient time to learn that a new transaction was designated. Publishing designated transactions on a website in and of itself is not adequate notification as taxpayers and advisors would need to check the website daily in order to identify newly designated transactions. With the proposed 45-day reporting deadline, there is the risk that taxpayers who do not have an in-house tax professional and do not engage one are not aware of a transaction being notifiable and miss the deadline. Further, there may also be the risk that tax professionals that serve their clients only at year-end are not aware of the transaction until it is too late to report on time.

The process for removing transactions from the notifiable transaction list has also not been specified. For example, a transaction described on the list may be found by the courts to be acceptable. Where Finance and the CRA choose not to take any further action (such as modification of the law, reassessment of taxpayers), such a transaction should no longer be required to be reported.

***Recommendation***

*The notification process should use multiple forms of publication including the CRA website, news releases, and government publications such as the Canada Gazette. There should also be a process for removing transactions from the notifiable transaction list.*

***New Designated Transactions***

As noted above the new federal notifiable transaction regime will be retroactive to January 1, 2022 once the legislation receives Royal Assent. It appears that going forward, taxpayers will be required to report designated transactions potentially as soon as 45 days after they are first designated and published. This does not provide taxpayers and advisors with sufficient time to determine whether they have transactions to report, gather the necessary data and prepare the reporting.

Québec enacted a similar regime to counter aggressive tax planning in 2020 and provided an initial list of specified transactions on March 19, 2021. The Minister of Revenue of Québec will provide lists of additional specified transactions by publishing them in the Gazette Officielle du Québec. A newly designated transaction will need to be reported only after the later of 120 days have passed since it was published in the Gazette and 60 days after the day the Minister of Revenue of Québec determines that the obligation to disclose begins. The reporting is generally applicable to transactions on a going forward basis and does not require taxpayers and advisors to go back in time and determine whether they were previously involved in a notifiable transaction.

***Recommendation***

*The deadline for reporting should incorporate a "later of" concept with the first date beginning a number of days after a transaction is first designated and the second date beginning on the date the transaction is entered into. As many taxpayers operate in Québec and must comply with Québec legislation, consideration should be given to coordinating deadlines.*

***Recurring Transactions***

It is also unclear whether transactions need to be reported on a recurring basis. Subsection 237.4(3) states that transactions or series of transactions may be designated. As discussed further below, the term "series of transactions" may capture an extensive number of transactions beyond just the key transaction that establishes the tax benefit. Further, the sample list of notifiable transactions describes transactions that may provide tax benefits over a period of time.

For example, the sample notifiable transaction in respect of "manipulating CCPC status" results in a benefit as certain investment income that may be earned throughout the year and annually will not be subject to refundable taxes. Would a transaction whereby CCPC status was lost before 2022 need to be reported because the corporation is not subject to refundable taxes on investment income earned in

2022 or later? Also, would the transaction need to be reported on an annual or more frequent basis given its recurrent effect, for example, 45 days after every receipt of investment income.

***Recommendation***

*The Minister of National Revenue and the Minister of Finance should provide specific instructions as to when transactions which provide benefits over a period of time are to be reported. For transactions which may have recurring benefits that are realized throughout a taxation year, reporting should only be required for the initial transaction(s) after the date of Royal Assent that implemented the strategy that generates the ongoing benefits. For transactions implemented before the date of Royal Assent, reporting should be based on the taxation year in which a benefit is claimed and due at the same time as the taxpayer's annual income tax return.*

**Meaning of "Substantially Similar" Transactions**

Proposed paragraph 237.4(2)(a) states that the term "substantially similar" is to be interpreted as including "any transaction, or series of transactions, in respect of which a person is expected to obtain the same or similar types of tax consequences (as defined in subsection 245(1)) and that is either factually similar or based on the same or similar tax strategy."

Tax consequences is defined in subsection 245(1) by reference to various amounts (such as the amount of income and amount payable). However, reporting pursuant to proposed section 237.4 is to be in respect of notifiable transactions and amounts are not included in the sample list of notifiable transactions that was released with the draft legislation. It is not clear how the concept of tax consequences applies in this context.

Furthermore, the concepts of "factually similar" and "similar tax strategy" are vague. Without clarity, the rules say that a transaction should be "interpreted broadly in favour of disclosure" and taxpayers and their advisors may be assessed penalties by CRA for failure to report innocuous transactions.

An example is the notifiable transaction regarding manipulating CCPC status. It is not clear if the primary concern is ongoing deferral of tax or something else. There are many sale transactions to third parties, such as public companies or non-residents, that trigger non-CCPC status. The designated transaction in respect of back-to-back arrangements is also vague. The introduction section for that transaction refers initially to interest and then to rents, royalties or payments of a similar nature. The final sentence then has a reference to character substitution rules in Part XIII but it is not clear which of the payments is being referred to.

Proposed paragraph 237.4(2)(b) states that for the purposes of the "notifiable transactions" definition, "substantially similar" is "to be interpreted broadly in favour of disclosure." The inclusion of this phrase introduces into the legislation a statutory interpretation concept, which appears unusual if not unique. It is unclear as to why this has been included in the legislation or what the implications would be when interpreting other provisions of the Act that also include a reference to "substantially similar". For example, if that phrase is not in another provision is that other provision to be interpreted narrowly?

The use of non-technical terms such as "manipulating", "artificial losses", and "manipulation" in the examples is also not helpful.

***Recommendations***

*The notifiable transactions should be drafted carefully and consistently to avoid confusion and clearly describe the tax avoidance issue and tax consequences. For clarity, the description should not be pejorative or judgmental. Additional guidance should be provided on what a substantially similar transaction means from a practical perspective for each notifiable transaction that is designated. For example, what is substantially similar could be explained in terms of what is achieved (including a threshold for the amount of tax consequences), how it is achieved or both factors. Examples should be provided of what planning should be acceptable and presumably not "substantially similar" as was done in Information Circular 88-2 Supplement 1 – General Anti-Avoidance Rule.*

**Notifiable Transactions that are a Series of Transactions**

Reporting a notifiable transaction that is part of a series of transactions presents various practical issues. A series of transactions frequently last longer than the 45-day reporting window and can be retrospective and prospective for many years.[5] Some of the examples[6] deal with a series of transactions where steps may take place in the future or not at all. Therefore, an advisor may not know that there is a notifiable transaction until all the transactions in the series are completed. Alternatively, a new transaction could be designated while a series of transactions is underway.

Subsection 237.4(5) requires a return to be filed for a notifiable transaction by 45 days after the earliest of the day on which the taxpayer becomes contractually obligated to enter into the notifiable transaction and the day on which the taxpayer enters into the notifiable transaction. Subsection 237.4(6) then states that "for greater certainty, … if subsection (4) applies to a person in respect of each transaction that is part of a series of transactions that includes a notifiable transaction, the filing of the information return by the person that reports each transaction is deemed to satisfy the obligation of the person under subsection (4) in respect of each transaction so reported."

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[5] Subsection 248(10) expands any reference in the Act to "a series of transactions or events" such that any related transaction completed in contemplation of the series is included. In the context of GAAR, the Supreme Court in *Copthorne Holdings*, 2011 SCC 63, commented that "contemplation" applies both prospectively and retrospectively such that where an avoidance transaction takes place after a transaction that did not contemplate avoidance at the time, the two still form a series.

[6] In particular, refer to the designated transactions regarding avoidance of deemed disposal of trust property which describe situations where another trust or a corporation is or may become a beneficiary of "Old Trust" and may receive property from "Old Trust" at some future time before the 21-year anniversary of "Old Trust." Until that transfer occurs, or an agreement is signed to effect that transfer, arguably a notifiable transaction has not occurred. Yet, based on the court's comments in *OSFC Holdings,* 2001 FCA 260, a preliminary transaction can form part of a series of transactions, even though at the time the taxpayer had not determined all the important elements of the later transactions.

Although not clear, it appears that the taxpayer, advisors and promoters may have to report before a series is completed. This can lead to the taxpayer, advisors, and promoters being unfairly penalized as they would not have known they had a notifiable transaction until later on in the series of transactions and hence may miss the 45-day deadline.

***Recommendation***

*As it may not be known at a point in time if something is notifiable or if something might become designated within an existing series, subsection 237.4(5) should consider when the actual tax benefit is realized to avoid this problem. Alternatively, the notifiable transaction designation should specifically identify when reporting is required in respect of a series of transactions.*

## PENALTY PROVISIONS

### Joint and Several Liability

The penalty provisions for failing to file an information return for reportable transactions and notifiable transactions each include a joint and several liability provision where there are multiple persons who have to file (in subsections 237.3(9) and 237.4(11) respectively). As the persons referred to in the rule are facing their own penalty and an unpaid penalty of another person is not akin to an amount of unpaid tax escaping collection, it is unclear why the penalties in question are subject to a joint and several liability rule.

***Recommendation***

*The use of a general joint and several liability rule should be reconsidered if subsection 237.3(4) is repealed as proposed and a similar rule is not included for notifiable transactions under section 237.4. The potential application of multiple penalties along with joint and several liability is unfair.*

### Due Diligence Rule

Both sets of reporting rules contain an identical due diligence rule which states that a person is not liable for a penalty "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."

Further information will be needed to clearly communicate the care, diligence and skill that should be exercised to avoid a penalty. As discussed elsewhere in the submission, we believe that it will be possible to inadvertently require a filing obligation due to a number of different circumstances such as inadvertently triggering the application of a hallmark, providing routine advice to others without full knowledge of a larger plan, preparing legal documents to give effect to transactions without full knowledge of a larger plan or simply the lack of knowledge around tax generally in the case of non-tax advisors.

***Recommendation***

*Additional guidance and examples should be provided of what will be considered to satisfy the due diligence requirements.*

**Proportionality of the Penalties**

As noted in the Appendix, the OECD recommends that monetary penalties have a strong deterrent value without being overly burdensome or disproportionate.

For a taxpayer, the fixed portion can be large in situations where the amount of the tax benefit is small. Similarly for an advisor, the structure of the penalty is such that up to $110,000 of the total penalty amount is determined without regard for the quantum of the fees charged by the advisor. The fixed portion of the penalty could be disproportionately large when compared with the nature of the work done. This will adversely affect those advisors who are providing relatively minor assistance as they may be subject to the same fixed penalty that applies to an advisor that devises the plan.

For example, an accountant who provided a safe income calculation and invoiced $5,000 and who failed to file an information return would be liable for a penalty of $110,000 plus their fee, while a promoter who charged $250,000 in respect of the same transaction and who failed to file an information return would be liable for a penalty of $110,000 plus their fee. The penalty is disproportionately punitive for the advisor who is less culpable and less integral to the realization of the tax benefit and who is less likely to know that they have a reporting obligation.

***Recommendation***

*Whether through a more focused approach to the rules generally or the penalty proposals specifically, the rules should be reviewed to ensure that the penalties are not disproportionate.*

## APPENDIX: COMPARISON TO OECD RECOMMENDATIONS

The proposed amendments to the reportable transaction regime in section 237.3 and the notifiable transaction regime in proposed section 237.4 are clearly based on recommendations from the OECD's BEPS Action 12 final report (the OECD Report).[7] We assume that the decision to adopt the OECD's recommended best practices was a political or policy decision and we will therefore not provide comments on the wisdom or efficacy of the OECD's suggestions.

Nevertheless, there are areas where the proposed amendments diverge from the OECD's model mandatory disclosure rules. These departures from the model rules contribute to many of the issues raised elsewhere in this submission. In our view, amending the proposed legislation to follow the OECD's recommendations more closely would eliminate or reduce these concerns.

### 1. Definition of Advisor

| Draft Proposals | OECD Report |
| --- | --- |
| The definition of "advisor" in subsection 237.3(1) means "each person who provides … any assistance or advice with respect to creating, developing, planning, organizing or implementing the transaction or series…". This is a very broad definition that, in the context of a commercial transaction, could include investment bankers, auditors, corporate-commercial lawyers, investment advisors, etc. There are no proposed amendments to this definition, but its breadth, when combined with the shift to a one hallmark approach and the imposition of separate reporting obligations on all advisors, is now a source of concern. The effect of the existing definition may be to impose reporting obligations on advisors who have no knowledge of those obligations or no meaningful ability to comply except through coordination with other advisors. | The OECD's recommendation was that the concept of an "advisor" should include persons who provide advice or assistance relating to the *tax aspects of a transaction that causes the transaction to be a reportable transaction*.[8] The OECD also stipulated that persons who provide services incidental to the transaction or series ought not to be burdened with reporting obligations where they did not have knowledge of the tax elements of the transaction or series. |
| Conclusion:<br>Adding a limitation of the nature suggested by the OECD to the definition of "advisor" in subsection 237.3(1) and subsection 237.4(1) should exclude advisors who provide advice or assistance in respect of the series of transactions that is incidental or unrelated to any tax benefit. These advisors are unlikely to ever provide useful disclosure that furthers the objectives of mandatory reporting rules, so their exclusion is reasonable from a cost-benefit and administrability standpoint. | |

[7] OECD (2015), *Mandatory Disclosure Rules, Action 12 - 2015 Final Report*, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris.
[8] *Ibid*., at 35 (box 2.2).

## 2. Definition of Confidential Protection

| Draft Proposals | OECD Report |
|---|---|
| The definition of "confidential protection" in subsection 237.3(1) means "… anything that prohibits the disclosure to any person … of the details or structure of the transaction or series…" except a disclaimer or restriction of an advisor's liability. Again, no changes to this definition have been proposed by the Department of Finance, but its scope is concerning with the shift to a single hallmark approach.<br><br>For example, many professional services firms will provide opinions on the basis that they are not to be disclosed, even where those opinions are non-controversial and do not relate to aggressive tax planning. The rationale for doing so is to prevent the opinion from being circulated as free tax advice to persons who are not the firm's clients, even if the non-clients cannot rely on that opinion and would not have any claim against the firm if the opinion is incorrect. The same considerations apply for other tax services more generally.<br><br>This limitation on disclosure could constitute confidential protection and, with a single hallmark approach and the proposed expanded definition of "avoidance transaction" in subsection 237.3(1), could cause many routine tax planning transactions to become reportable transactions. | As observed by the OECD, confidential protection is concerning when its purpose is to permit a promotor or advisor to sell the same aggressive tax plan to multiple taxpayers without tax authorities or competitors becoming aware of the plan.[9] Other countries, notably the United Kingdom, have excluded confidentiality clauses in opinions from the scope of confidential protection where the subject matter of the opinion is reasonably well-known in the tax community. Confidential protection in those circumstances is non-problematic given the purpose of the confidential protection hallmark. |
| Conclusion:<br>The definition of "confidential protection" in subsection 237.3(1) should be amended to exclude confidential protection obtained where the details of the transaction or series are reasonably well-known in the tax community. Practically, this exclusion could be phrased as an objective purpose test. For example, that it is reasonable to conclude that none of the main reasons for the confidential protection was to prevent the Minister or a competitor from becoming aware of the details or structure of the transaction or series. | |

[9] *Ibid*., at 40 (para. 95) and 42 (box 2.4).

## 3. Contingent Fee Concept

<table>
<tr><th>Draft Proposals</th><th>OECD Report</th></tr>
<tr><td>Paragraph (a) of the “reportable transaction” definition in subsection 237.3(1) hallmarks an avoidance transaction as a reportable transaction if an advisor or promoter charges a fee that is: (i) based on expected tax benefits; (ii) contingent upon tax benefits being obtained; or (iii) attributable to the number of participants in the avoidance transaction. No amendments to this definition have been proposed, but ambiguities in the text of the definition are concerning given the shift to a single hallmark.<br><br>Professional services firms are concerned that charging a flat fee for standardized tax planning services could hallmark the series of transactions; clients would only choose to pay the flat fee if they perceived that the tax benefit would be large enough to justify the fee. Many firms are choosing to market their skills and know-how by billing for the value of the service and not by direct reference to time.<br><br>As a further example, a large commercial transaction may require the filing of dozens or hundreds of T2057s for the purpose of deferring capital gains, and an accounting firm would likely bill for the preparation of the T2057s on a per-transferor basis. These are not aggressive transactions, but one of their main purposes is to obtain a tax benefit and therefore the transactions would be avoidance transactions under the proposed avoidance transaction definition.</td><td>The OECD observed that the United Kingdom has avoided these issues by stipulating factors that may be considered in setting a fee which will not create a contingent fee.[10] For example:<br>• The location of the advisor;<br>• The urgency of the advice;<br>• The size of the transaction;<br>• The skill or reputation of the advisor; or<br>• The scarcity of expertise in a particular area of tax.</td></tr>
<tr><td colspan="2">Conclusion:<br>Section 237.3 should be amended to provide that, for greater certainty, a fee is not described in paragraph (a) of the definition of “reportable transaction” in subsection 237.3(1) where enumerated factors such as those used in the United Kingdom above are considered in setting the fee. Alternatively, the Department of Finance could work with the CRA to create updated administrative guidance concerning the existence of a contingent fee. This administrative guidance should be coupled with statements in the updated Explanatory Notes to clarify that fees based on efficiencies, urgency, skill, or importance are not intended to create reportable transactions.</td></tr>
</table>

[10] *Ibid*., at 44 (para. 112), citing HMRC (2014), *Disclosure of Tax Avoidance Schemes: Guidance*, 14 May 2014, p. 46.

### 4. Absence of a De Minimis Threshold for Notifiable Transactions

| Draft Proposals | OECD Report |
| --- | --- |
| The notifiable transaction regime in proposed section 237.4 does not include a monetary threshold for the tax benefit that must be realized before disclosure is required.<br><br>On the impact that a *de minimis* threshold can have, the OECD states:<br><br>"A de-minimis filter could be considered as an alternative to, or in addition to, a broader threshold test and could operate to remove smaller transactions, below a certain amount, from the disclosure requirements. It would therefore narrow the ambit of the mandatory disclosure regime and reduce the risk of over-disclosure. It may also enhance the usefulness of the information collected because the focus would be on more significant transactions and excessive or defensive filings could be reduced. This could reduce the costs and administrative burden for certain taxpayers and for the tax administration."[11] | As observed by the OECD, adopting a monetary threshold for specific hallmark-based disclosures may reduce costs to taxpayers and avoid diluting the relevance of information received; this is the approach taken by the United States in some comparable instances, with respect to both the quantum of the tax benefit that must be realized and with respect to the fees that must be charged before an advisor has acquired a reporting obligation.[12] |
| Conclusion:<br>As currently proposed, there is no size test for the proposed application of the notifiable transaction rules. It would be up to the Department of Finance to determine what *de minimis* threshold is appropriate, but it should be possible to set a tax benefit and fee threshold to reduce over-reporting and simplify the application of the rules for smaller transactions. | |

[11] *Ibid*., at 38 (para 87).
[12] *Ibid*., at 37-39 (paras. 85 and 90).

## 5. Quantum of Penalties

| Draft Proposals | OECD Report |
| --- | --- |
| Proposed paragraph 237.3(8)(b) and proposed paragraph 237.4(8)(b) would impose a penalty on an advisor or promoter who fails to file an information return in respect of a reportable or notifiable transaction as and when required. The maximum penalty is $110,000 plus the fee charged by that promoter or advisor and would apply if the promotor or advisor's non-compliance continued for 100 or more days. The minimum penalty is $11,000 plus the fee charged and would apply if the promotor or advisor's non-compliance was limited to one day.<br><br>The structure of the penalty is such that up to $110,000 of the total penalty amount is determined without regard for the quantum of the fees charged by the advisor. So, for example, an accountant who provided a safe income calculation and invoiced $5,000 and who failed to file an information return would be liable for a penalty of $110,000 plus their fee, while a promoter who charged $250,000 in respect of the same transaction and who failed to file an information return would be liable for a penalty of $110,000 plus their fee. The penalty is disproportionately punitive for the advisor who is less culpable and less integral to the realization of the tax benefit and who is less likely to know that they have a reporting obligation. We believe this is unfair. | The OECD recommends that monetary penalties have a strong deterrent value without being overly burdensome or disproportionate.[13] Any fixed penalty or daily penalty will be disproportionate to fees charged or to the extent of an advisor's involvement, so the Department of Finance's objective should be to avoid an overly disproportionate fixed or daily penalty. |
| Conclusion:<br>We submit that the amount of the fixed or daily penalty should be reduced or, in the alternative, should be made proportionate to the fee charged by the advisor or promoter. The impact of this issue will depend on whether the final proposals are more focused or subject to a *de minimis* test. | |

[13] *Ibid*., at 57-58 (para. 183).