



# TaxNewsFlash

Canada

## Get Ready for New Mandatory Reporting Obligations

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Canadian individuals and businesses should prepare now to report certain transactions under expanded new mandatory disclosure rules. These expanded rules generally require individuals, corporations, trusts and partnerships to promptly disclose certain “reportable transactions” and “notifiable transactions” to the CRA, among other new obligations. Finance recently updated the rules for these transactions with new relieving amendments, including to extend the disclosure deadline to within 90 days (from 45 days) of entering into the transaction and narrow the scope of reportable transactions. These rules will apply to transactions entered into on or after the date the legislation to enact these changes receives Royal Assent, which is expected soon. Certain corporate taxpayers will also have to disclose information about uncertain tax treatments reflected in their financial statements for taxation years that begin on or after January 1, 2023.

In light of these reporting requirements, taxpayers need to quickly assess whether they may have new reporting obligations under these rules. In particular, taxpayers should identify any planned transactions that may occur once these rules come into effect and implement a process to identify and track all transactions and uncertain tax treatments that must be reported. Taxpayers who fail to make the proper disclosures may be subject to onerous penalties as well as extended reassessment periods. Taxpayers should also be aware of Quebec’s disclosure rules that may apply to their situation.

### **Background**

Finance originally announced measures in the 2021 federal budget to expand Canada’s existing mandatory disclosure rules for reportable transactions and introduce new reporting requirements for notifiable transactions and uncertain tax treatments. These changes follow recommendations from Action Item 12 of the OECD’s Base Erosion and

Profit Shifting Project. For details, see *TaxNewsFlash-Canada* 2021-21, “[2021 Federal Budget Highlights](#)”.

Finance first released draft legislation to introduce these changes for public consultation on February 4, 2022. At the same time, Finance released specific examples of notifiable transactions that would be required to be reported under the new rules. Finance released revised draft legislation on August 9, 2022 to address several comments received during the consultation process, including to narrow the application of certain reportable transaction hallmarks and clarify certain adviser reporting obligations, among other issues. Alongside the 2022 Fall Economic Update, Finance announced that it would delay the revised reporting requirements for reportable and notifiable transactions until these changes receive Royal Assent (instead of for transactions after 2022). Bill C-47, which includes the legislation to enact these new reporting requirements, received first reading in the House of Commons on April 20, 2023.

Note that, under the new mandatory disclosure rules, certain corporate taxpayers must also disclose uncertain tax treatments for taxation years beginning on or after January 1, 2023 (although the penalty doesn't apply to taxation years that begin before the date the legislation receives Royal Assent). These rules have not been amended from the draft legislation released on August 9, 2022.

For details, see *TaxNewsFlash-Canada* 2022-48, “[Highlights of the 2022 Federal Fall Economic Update](#)”, *TaxNewsFlash-Canada* 2022-43, “[Prepare Now for Upcoming Mandatory Disclosure Rules](#)” and *TaxNewsFlash-Canada* 2022-05, “[Finance Issues Outstanding Interest Expense Rules & More](#)”.

## Reportable transactions

Under the new mandatory disclosure rules, taxpayers will soon be required to disclose certain transactions where it can reasonably be considered that one of the main purposes of entering into the transaction (or series of transactions) is to obtain a tax benefit, and any one of the following generic hallmarks is present:

- Contingent fee arrangements (other than fees related to Scientific Research and Experimental Development (SR&ED) claims)
- Confidential protections (related to the tax treatment of an avoidance transaction)
- Contractual protections (other than standard professional liability insurance and certain indemnity clauses in arm's-length purchase and sale agreements).

This is a change from the current rules, which provide that a transaction is reportable when two generic hallmarks are present and it constitutes an “avoidance transaction” under the general anti-avoidance rule (GAAR) (which has a primary purpose test). These broader

disclosure requirements apply to reportable transactions entered into after the legislation receives Royal Assent.

#### **KPMG observations**

In its latest revisions to the mandatory disclosure requirements, Finance clarifies that certain contingent fee arrangements and contractual protections will not give rise to reportable transactions. In particular, taxpayers should not be required to disclose transactions because of contingent fees for SR&ED claims (which are separately reported to the CRA), standard professional liability insurance or certain indemnity clauses in purchase and sale agreements between arm's-length parties if certain conditions are met.

Further, Finance's explanatory notes now include examples of common billing practices and fee arrangements that would generally not result in a reporting obligation (absent another hallmark being present), including:

- "Value-billing" by tax professionals based on criteria other than the value of a tax benefit resulting from the transaction or series of transactions
- A contingent litigation fee arrangement related to an appeal of a tax assessment implemented after the completion of the transaction or series of transactions subject to the appeal.

However, Finance further advises that taxpayers and advisers may have to report a transaction where a contingent litigation fee arrangement is put in place prior to the completion of the transaction or series.

The explanatory notes also include several examples specific to financial institutions, where the collection of a standard fee (i.e., generally available to the public under normal commercial terms and in comparable circumstances) would not generally result in a reportable transaction.

In addition, the revised rules no longer include a joint and several liability clause where more than one person is liable for a penalty for failure to disclose a reportable transaction.

#### **Notifiable transactions**

Taxpayers will also have new notifiable transaction reporting obligations where they enter into certain transactions that the CRA has found to be abusive, as well as transactions identified as transactions of interest (i.e., where the CRA requires more information to determine if a transaction is abusive). Under this reporting obligation, taxpayers will have to report transactions that the CRA designates as notifiable transactions as well as substantially similar transactions. The CRA can designate a transaction as a notifiable

transaction with the agreement of Finance. These reporting obligations apply to notifiable transactions entered into after the legislation receives Royal Assent.

Based on Finance's notifiable transactions released to date, taxpayers will need to report:

- Certain transactions to avoid Canadian-controlled private corporation (CCPC) status
- Certain "straddle-loss" transactions where they enter into two or more financial instrument positions concurrently that are expected to generate substantially equal and offsetting gains and losses, including through the use of partnerships
- Certain transactions in which they transfer trust property to capital beneficiaries on a tax-deferred basis before the 21-year deemed realization date
- Certain transactions in which they are temporarily assigned into bankruptcy before settling or extinguishing a commercial debt obligation in order to reduce a forgiven amount of the obligation to nil under the debt forgiveness rules
- Certain transactions in which the taxpayer argues that there is no deemed acquisition of control under the corporate loss trading rules because certain purpose tests are not met
- Certain transactions involving indirect financing arrangements from arm's-length non-residents where they file, or anticipate filing, their income tax return on the basis that the debt and related interest is not subject to the thin capitalization rules
- Certain transactions involving indirect financing arrangements from non-resident persons where their income tax reporting reflects, or is expected to reflect, the assumption that related interest is not subject to withholding tax or is subject to a lower rate of withholding tax than the rate that would otherwise apply (as well as similar arrangements for rents, royalties or other payments or to effect a substitution of the character of the payment).

#### **KPMG observations**

The 2022 federal budget also proposed new rules for "substantive CCPCs" to address transactions to avoid CCPC status that have not yet been included in a bill. For details of the budget announcement, see *TaxNewsFlash-Canada 2022-24*, "[2022 Federal Budget Highlights](#)".

Under the reporting requirements for notifiable transactions, taxpayers are not subject to these requirements where they have exercised due diligence in determining whether the transaction is a notifiable transaction. Previously, the draft rules had a due diligence defence that was only available where taxpayers were subject to a penalty for failure to disclose a notifiable transaction.

Similar to its changes for reportable transactions, Finance has removed the joint and several liability clause for notifiable transactions included in previous draft legislation, that would have applied where more than one person is liable for a penalty for failure to disclose a notifiable transaction.

Although the CRA has designated several notifiable transactions so far, taxpayers should also be aware that the CRA can add to this list with the concurrence of Finance.

### Reporting deadline and penalties

A taxpayer must inform the CRA of a reportable or notifiable transaction by filing an information return within 90 days of the earlier of:

- The day the taxpayer becomes contractually obligated to enter into the transaction, and
- The day the taxpayer enters into the transaction.

This requirement also applies to other persons who enter into these transactions for the taxpayer's benefit.

Persons who fail to disclose reportable or notifiable transactions as required face a penalty of \$500 per week for each failure, up to the greater of \$25,000 and 25% of the tax benefit. Corporations that do not disclose reportable or notifiable transactions and have assets with a total carrying value of \$50 million or more face a higher penalty of \$2,000 per week, up to the greater of \$100,000 and 25% of the tax benefit.

Under the new rules, where a taxpayer has a reportable or notifiable transaction in a taxation year, the taxpayer's normal reassessment period for that year does not begin until the taxpayer has complied with the mandatory disclosure reporting requirement (i.e., the year for that transaction would not become statute-barred).

#### **KPMG observations**

The revised legislation extends the reporting deadline for taxpayers (or other persons) so that they are required to notify the CRA of reportable or notifiable transactions within 90 days (from 45 days).

### Disclosing uncertain tax treatments

Certain corporate taxpayers that are required to file a Canadian income tax return are also required to report uncertain tax treatments reflected in their financial statements to the CRA under these rules. Specifically, these rules may affect corporations with at least \$50 million in assets that have reflected an uncertainty with respect to a particular tax treatment in their audited financial statements, or the audited consolidated financial statements of a group of

which the corporation is a member, that are prepared in accordance with International Financial Reporting Standards (IFRS) or certain other country-specific GAAP. A reporting corporation must file an information return to report its uncertain tax treatments on or before the date that its Canadian income tax return for the particular year is due. Reporting corporations must disclose these uncertain tax treatments for taxation years that begin or after January 1, 2023.

Reporting corporations that fail to disclose uncertain tax treatments as required may be subject to a penalty of \$2,000 per week for each uncertain tax treatment, up to a maximum of \$100,000. The penalty does not apply to taxation years that begin before the legislation receives Royal Assent.

For a full explanation of these rules, which have not changed from the draft legislation released August 9, 2022, see *TaxNewsFlash-Canada* 2022-43, "[Prepare Now for Upcoming Mandatory Disclosure Rules](#)".

### Special rules for promoters and advisers

The mandatory disclosure requirements for reportable and notifiable transactions, including the reporting deadlines, also apply to promoters and advisers (as well as persons who do not deal at arm's length with the promoter or adviser and who are entitled to receive a fee with respect to a transaction) except where solicitor-client privilege applies. However, the adviser reporting obligation will generally not apply to persons solely because they provided clerical or secretarial services in respect of a reportable or notifiable transaction. In addition, under the revised legislation for notifiable transactions, advisers and promoters (and non-arm's length persons entitled to a fee) will not have a reporting requirement for a transaction unless the person knows or should reasonably be expected to know that the transaction was a notifiable transaction.

Separate penalties also apply to promoters and advisers (and non-arm's length persons entitled to a fee) who do not disclose under these rules as required for each failure to report.

#### **KPMG observations**

The revised legislation has expanded reporting relief for promoters and advisers that do not know, or should not reasonably be expected to know, that the transaction was a notifiable transaction. Previously, this relieving rule was only available to certain financial institutions.

### Quebec mandatory disclosure regimes — Reminder

In addition to the federal mandatory disclosure rules, taxpayers residing in or operating in Quebec may also have to disclose information about certain transactions, under similar provincial reporting requirements. Under these rules, taxpayers may be required to disclose:

- Transactions involving conditional remuneration
- Confidential transactions
- Transactions with contractual coverage
- Nominee agreements
- “Specified transactions” including:
  - Avoidance of the deemed disposal of trust property
  - Payment to a non-treaty country
  - Multiplication of capital gains deduction
  - Tax attribute trading.

### We can help

Your KPMG adviser can help you assess the effect of the mandatory disclosure rules. KPMG has developed a global technology tool to assist organizations in assessing whether a particular arrangement meets the definition of a transaction which must be reported to tax authorities and to assist with the reporting process, if required. KPMG has developed a full-service approach in order to ensure organizations remain compliant under these complex rules.

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