

Tax

New notifiable transactions unveiled: Ignore at your peril

By **Ryan Morris and Michael Ding**

Ryan Morris

(November 23, 2023, 2:21 PM EST) -- Non-tax advisers, particularly corporate/commercial, estates and bankruptcy lawyers, should read this article. Such advisers can easily and unwittingly fall under new notifiable transaction rules requiring them to file an information return with the Canada Revenue Agency (CRA). Financial penalties and other adverse consequences arising on a failure to file the applicable information return can be severe. This includes an adviser being liable for a penalty in excess of their fees (even if a late filing is made).

The notifiable transaction rules are part of a broader set of expanded mandatory disclosure rules that came into effect on June 22, 2023. However, there were no notifiable transactions until the CRA designated the following five notifiable transactions on and effective as of Nov. 1, 2023:

1. Straddle loss creation transactions using a partnership;
2. Avoidance of deemed disposal of trust property;
3. Manipulation of bankrupt status to reduce a forgiven amount;
4. Reliance on purpose tests in section 256.1 to avoid a deemed acquisition of control; and
5. Back-to-back arrangements to avoid the thin capitalization rules or to reduce or avoid Part XIII tax.



Michael Ding

The CRA has provided details of each of the designated notifiable transactions and has recently provided updated administrative guidance.

On Sept. 11, 2023, the Federation of Law Societies of Canada, on behalf of all law societies in Canada, filed an application in the British Columbia Supreme Court, challenging the constitutionality of the amendments to these rules. Following this, the Attorney General of Canada agreed to exempt lawyers, paralegals and articling students from these rules until

the earlier of the court's decision in respect of the federation's application or Dec. 1, 2023. The federation's application was heard on Oct. 20, 2023.

Overview of rules

A notifiable transaction is a transaction or series of transactions that is designated as such by the CRA with the concurrence of the minister of finance as well as transactions and series of transactions that are substantially similar to a designated notifiable transaction. A substantial similar transaction would include any transaction or series of transactions expected to obtain the same or similar types of tax consequences and that is either factually similar or based on the same or similar tax strategy. Further, the legislation specifically provides that "substantially similar" is to be interpreted broadly in favour of disclosure.

In general, the following persons are required to file an information return (Form RC312) with respect to a notifiable transaction:

- every person who will realize a tax benefit from the notifiable transaction or a series of transactions that includes the notifiable transaction;
- every person who entered into the notifiable transaction for the benefit of a person who will realize the tax benefit;
- every adviser or promoter in respect of the notifiable transaction; and
- every person who does not deal at arm's length with an adviser or promoter (acting in that capacity with respect to the notifiable transaction) and who is, or could become, entitled to a fee that is in respect of the notifiable transaction.

"Adviser" is defined *extremely* broadly to capture any person who provides, directly or indirectly in any manner whatever, any assistance or advice with respect to creating, developing, planning, organizing or implementing the notifiable transaction. Given the breadth of the "adviser" definition and the low threshold to report, advisers (including non-tax lawyers) can easily have a reporting obligation under the rules in connection with a particular matter.

For example, a bankruptcy lawyer who assists with filing a corporate bankruptcy may have a reporting obligation if the bankruptcy is part of a transaction designed to reduce a forgiven amount under debt forgiveness rules even if (as would often be the case) the lawyer is just assisting with implementation without having any involvement with the tax planning. Similarly, an estates lawyer who assists with transfers of property from a trust (e.g., trustee resolutions) may have a reporting obligation if the transfers avoid a deemed disposition at fair market value of trust property. These are merely examples.

Where an information return must be filed, the due date is generally the 90th day of the person described at #1 or #2 (the "taxpayer"), as applicable, entering into, or becoming contractually obligated to enter into, the notifiable transaction. The earliest possible deadline for reporting notifiable transactions is Jan. 30, 2024.

Failure to file penalties for the taxpayer is either \$500 or \$2,000 per week to a maximum of the greater of (i) \$25,000 or \$100,000 and (ii) 25 per cent of the tax benefit, with the higher penalty applying to corporate taxpayers with a carrying value of assets of at least \$50 million. Each promoter and adviser is subject to penalties totalling 100 per cent of the fees charged for the transaction or series of transactions plus \$10,000 plus \$1,000 per day of non-compliance to a maximum of \$100,000. Notably, the penalty of 100 per cent of fees plus \$10,000 applies to any late filing (even if only one day late). Furthermore, there may be circumstances where "fees charged" exceed the "fees received."

Accordingly, subject to a due diligence defence, a failure to file an information return when required will cause the adviser to be liable to a penalty in excess of the fees charged by the adviser in respect of the notifiable transaction.

Due diligence defences

Participants can avoid reporting obligations and penalties if they can show that they exercised the degree of care, diligence and skill to determine whether a transaction is a notifiable transaction that a reasonably prudent person would have exercised in comparable circumstances.

Advisers and promoters can avoid reporting obligations and penalties if they can show they did not know and should not have been reasonably expected to know that the subject transaction was a notifiable transaction.

Advisers may wish to consider amending their standard form engagement letters in a manner that would assist them in meeting their due diligence defence. Where a client's tax adviser is involved in a matter (e.g., directly or indirectly providing instructions or advice to the client or lawyer, reviewing documents, etc.), the client and the lawyer may wish to dig deeper as to whether there is a notifiable

transaction. This may include asking the tax adviser whether the mandate is part of a notifiable transaction.

CRA mailing list for future notifiable transactions

The CRA recently released an electronic mailing list to notify subscribers when a new notifiable transaction has been designated by the minister. The CRA indicates that subscribers to this new mailing list may also receive other related updates to the mandatory disclosure rules. To sign up, [click here](#).

The CRA warns that it does not assume any responsibility for the timely delivery of information updates through this service and that the use of this service is not a substitute for regularly checking a pending designated notifiable transaction webpage.

Solicitor-client privilege and the future application to lawyers

Information reasonably believed to be subject to solicitor-client privilege is not required to be disclosed in the information return (and indeed cannot be disclosed in the information return unless the client waives the privilege). This would cover information in the hands of taxpayers, lawyers, and non-legal advisers provided there is a reasonable belief that the information is subject to solicitor-client privilege. There may be some practical uncertainties in the application of solicitor-client privilege and what can be included in the information return. For example, the Supreme Court of Canada previously ruled that in certain circumstances clients' names in lawyer's financial records may be subject to solicitor-client privilege and can be exempt from disclosure to the CRA (*Canada (National Revenue) v. Thompson*, 2016 SCC 21).

The pending decision of the British Columbia Supreme Court (and any subsequent appellate court) on the application of the Federation of Law Societies of Canada discussed above should address uncertainty in this area (and whether lawyers will have reporting obligations under the rules with respect to their clients).

Ryan Morris is chair of the tax law group at WeirFoulds LLP. His legal practice focuses on various areas of domestic and international taxation, including advising on mergers and acquisitions, structured investment products, financings, estate plans, employment tax issues and a broad range of corporate tax matters. Ryan also represents clients with voluntary disclosures, audits and appeals, and he has been lead counsel at every level of court, including the Supreme Court of Canada. Michael Ding is an associate in the tax law group at WeirFoulds LLP with a practice that focuses on various areas of domestic and international taxation planning, advice and dispute resolution. Prior to joining WeirFoulds, Michael practised as counsel at the Department of Justice Canada, representing the Crown before the Tax Court of Canada, Federal Court of Canada, Ontario Superior Court of Justice and the Court of Appeal for Ontario.

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