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Tax Alert – Canada

Changes to GST/HST VDP revised

EY Tax Alerts cover significant tax news, developments and changes in legislation that affect Canadian businesses. They act as technical summaries to keep you on top of the latest tax issues. For more information, please contact your EY advisor or EY Law advisor.

On 15 December 2017, the Canada Revenue Agency (CRA) released GST/HST Memorandum 16.5, *Voluntary Disclosures Program*, as well as a separate document relating to the Voluntary Disclosures Program (VDP) for income tax and source deductions, Information Circular IC00-1R6.

These documents follow the CRA's proposed changes released 9 June 2017 and the closing of the consultation period 8 August 2017. See EY's Tax Alert 2017 No. 26 and Tax Alert 2017 No. 27.

Notably, the CRA is separating the VDP policy for disclosures involving income tax and source deductions from the VDP policy for GST/HST, excise tax, excise duties, softwood lumber products export charges and air travellers security charges.

Major changes to the CRA's VDP policy for GST/HST include the following:

- Applications will be processed under three different tracks, and less-generous relief will be available in major cases of non-compliance.
- VDP relief will not be available if a registrant attempts to increase the amount of input tax credits (ITCs), rebates or other credit adjustments without any corresponding increase in tax liability.
- Registrants will be required to pay the estimated tax owing at the time they apply for VDP relief.

There are several significant differences between the June 2017 proposals and those contained in Memorandum 16.5. These changes are discussed in more detail below.

The new VDP policies will apply as of 1 March 2018. For a registrant to qualify for VDP relief under the current regime, the CRA must receive the application, including the applicant's name, on or before 28 February 2018.

Building a better working world

Background

The VDP applies to disclosures relating to income tax, source deductions, GST/HST, excise tax, excise duties, softwood lumber products export charges, and air travellers security charges. Subject to certain eligibility requirements, registrants may correct inaccurate or incomplete information they have previously provided to the CRA or disclose information they have not previously provided. Under the current policy, a registrant that makes a valid disclosure is liable to the taxes owing (plus interest), but is not subject to penalties or prosecution. In some cases, the interest may be reduced, waived or cancelled as well. For GST/HST purposes, section 281.1, section 284, and subsection 284.1(3) of the *Excise Tax Act* provide the legislative discretionary authority to the Minister of National Revenue to waive or cancel penalties and interest.

The CRA released proposed changes to the VDP on 9 June 2017, which were outlined in a draft GST/HST Memorandum (the June 2017 proposals). Submissions were invited over a 60-day online consultation period. During this process, a number of concerns were raised, including whether:

- the proposed multi-tier system of relief was consistent with the VDP policy objective of encouraging tax compliance
- the CRA would administer no-name disclosures in full accordance with current policy
- a registrant should be required to provide the name of its professional advisor as a condition for VDP applications

This alert focuses on the VDP policy for GST/HST, excise tax, excise duties, softwood lumber products export charges, and air travellers security charges.

The CRA has also released Information Circular IC00-1R6, *Voluntary Disclosures Program*, which provides information on the CRA's VDP policy for disclosures related to income tax and source deductions. Refer to our Tax Alert 2017 No. 53 for information on the VDP policy changes for disclosures involving income tax and source deductions.

Introduction of three tracks

The CRA will process GST/HST VDP applications under three tracks:

Track 1 – GST/HST wash transactions: Full interest and penalty relief may be provided for GST/HST wash transactions. Under GST/HST Memorandum 16.3.1, *Reduction of Penalty and Interest in Wash Transaction Situations*, a wash transaction refers to a situation where a supplier has failed to charge and collect GST/HST from a registrant that is entitled to claim a full ITC. A wash transaction may also occur within a closely related or associated group of persons where ITCs are claimed by the wrong entity.

Track 2 – General Program: Track 2 provides relief for applications disclosing non-compliance or errors, including situations involving:

- Wash transactions that are ineligible for a reduction of penalty and interest in accordance with policies set out in GST/HST Memorandum 16.3.1
- Reasonable errors
- Failure to file information returns
- No gross negligence or deliberate tax avoidance
- Over-claimed rebates

Track 3 – Limited Program: Limited relief may be provided for applications disclosing non-compliance where there is an element of intentional conduct on the part of the registrant or a closely related party. This includes (without limitation) situations such as the following:

- GST/HST was charged or collected but not remitted
- Efforts were made to avoid detection (e.g., participation in the underground economy)
- The disclosure is made after an official CRA statement regarding its intended specific focus of compliance or following broad-based CRA correspondence
- Deliberate or wilful default or carelessness amounting to gross negligence

For the purposes of determining the category under which to process a VDP application, the CRA will consider factors such as:

- The dollar amounts involved
- The number of years of non-compliance
- The sophistication of the registrant
- How quickly the registrant took corrective measures after discovering the non-compliance

Notably, VDP applications by "large corporations" (i.e., corporations with gross revenue exceeding $250 million in at least two of their previous five taxation years, and any related entities) will generally be considered under the Limited Program. This measure did not appear in the June 2017 proposals for GST/HST, although it did appear as part of the VDP proposals relating to income tax.

During the consultation process, various stakeholders had raised concerns about limiting VDP relief where large corporations were involved. The grounds for limiting access to the VDP on the basis of a corporation's annual revenues were unclear at best and arguably contravened principles of administrative fairness. Nevertheless, it appears the CRA has opted to extend the large corporation policy to the GST/HST VDP, although it is arguable the CRA will apply a more lenient administration policy in other respects.

For example, the June 2017 proposals indicated the Limited Program would apply for applications disclosing major non-compliance, including any circumstance in which a high degree of registrant culpability contributed to the compliance failure. In contrast, Memorandum 16.5 specifically refers to an element of intentional conduct. Arguably, this change indicates the CRA will require a higher degree of culpability before referring a VDP application to the Limited Program.

In addition, the June 2017 proposals indicated situations involving large dollar amounts, sophisticated registrants and multiple years of non-compliance would generally be viewed as non-compliance suitable for processing under the Limited Program. As noted above, these are now "factors" the CRA will consider in determining the appropriate category for VDP processing.

Conditions of a valid application

In order for a VDP application to qualify for relief, the application must:

- Be voluntary
- Be complete
- Involve the application or potential application of a penalty or interest
- Include information that is at least one reporting period past due
- Include payment of the estimated tax owing

In general, the CRA will not consider an application to be voluntary if:

- The registrant was aware of an enforcement action (e.g., audits or investigations, as well as CRA requests, demands or requirements relating to unfiled returns or unremitted tax) in respect of the information being disclosed to the CRA;
- Enforcement action relating to the VDP application subject matter has been initiated against the registrant, a related person, an associate person, or a third party that is sufficiently related to the application; or
- The CRA has already received information concerning the registrant's (or a related party's) involvement in tax non-compliance.

A registrant's VDP application for a particular issue must be made for taxation years or fiscal or reporting periods where there was previously inaccurate, incomplete or unreported information regarding their tax affairs as follows:

- For Track 1 and Track 2, the four calendar years before the application's filing date; and
- For Track 3, all relevant years.

This differs from the June 2017 proposals, which had indicated that for Track 2 treatment, the application would have to be made for the six calendar years before the application's filing date.

A registrant may submit a written request for additional time to submit required information if extraordinary circumstances prevent the registrant from providing the information. If the applicable books and records no longer exist, the registrant should make all reasonable efforts to estimate the relevant amounts.

Under current policy, a VDP application must involve the application or potential application of a penalty. Memorandum 16.5 states the CRA will consider disclosures involving the application or potential application of interest as well. Registrants may not seek relief through the VDP if neither a penalty nor interest applies, although the CRA suggests submitting the information for normal processing regardless.

VDP applications must include information relating to a reporting period that is at least one reporting period past due. However, Memorandum 16.5 indicates the CRA will consider an application that also includes more recent information.

Registrants will be required to include payment of any related tax when submitting a VDP application. The CRA may consider alternative payment arrangements in certain situations. However, to support the inability to pay, the registrant will be required to make full disclosure and provide evidence of income, expenses, assets and liabilities. The CRA may also require security in certain circumstances.

Interest relief

Where the CRA accepts a VDP application, interest relief in respect of assessments resulting from the application is available as follows:

- For GST/HST wash transactions, 100% interest relief;
- For the General Program, relief for 50% of the applicable interest; and
- For the Limited Program, no interest relief.

The minister may grant interest relief for interest that accrued during the previous 10 calendar years before the calendar year in which the registrant files the VDP application.

Penalty relief

Where the CRA accepts a Track 1 or Track 2 VDP application, full penalty relief will be provided, subject to the 10-year limitation period (consistent with current VDP policy).

Penalty relief is generally not available for a VDP application under the Limited program. However, the CRA will not assess a gross negligence penalty even if the facts establish that the registrant is liable for such a penalty.

Prosecution relief

Where the CRA has accepted a VDP application, it will not refer a registrant for criminal prosecution for tax offences.

Circumstances where no VDP relief will be granted

In general, the CRA will not consider VDP applications in the following circumstances:

- Applications relating to statutory elections
- A registrant is attempting to increase the amount of ITCs, rebates or other credit adjustments without any corresponding increase in tax liability for the relevant period
- The applicant is in receivership or has become bankrupt
- Post-assessment requests for penalty and interest relief

Application form

The CRA recommends that registrants use Form RC199, *Voluntary Disclosures Program (VDP) Taxpayer Agreement*, for all applications made under the new policy. A registrant that does not use Form RC199 should include all of the information requested in that form. This represents a more lenient approach than the June 2017 proposals, which had indicated a registrant must use Form RC199 for VDP applications. The application's effective date of disclosure is the date the CRA receives a completed and signed application.

Where a registrant has received assistance from an advisor with respect to the application, the advisor's name should generally be included in the application. However, if a registrant's authorized representative submits the application, the form must be signed by both the registrant and the authorized representative.

No-name disclosure

Currently, registrants who are unsure if they want to submit a VDP application may engage in informal and non-binding preliminary discussions with the CRA on a "no-name" basis. These discussions occur before the registrant's identity is revealed. On the basis of the preliminary information provided by the registrant, the VDP officer may confirm whether there is anything that would immediately disqualify the registrant from VDP consideration. If all the required information for a complete disclosure (other than the registrant's identity) has been submitted and the registrant so requests, the officer may review the information and advise the registrant on the tax implications of the disclosure, without prejudice.[1]

The CRA has confirmed it will provide registrants with "an opportunity to participate in preliminary discussions… on an anonymous basis," and that such discussions will continue to be informal and non-binding. If complex or technical reporting issues are involved, the CRA

[1] See IC 00-1R5, *Voluntary Disclosures Program*, ¶26 – 30.

may refer a registrant to a CRA official in a specialized audit area for discussion on an anonymous basis. Notably, such discussions do not constitute acceptance into the VDP.

As a result of the information provided in Memorandum 16.5, it is not clear whether the CRA will administer no-name disclosures in full accordance with current policy.

Second VDP application

In accordance with current policy, a registrant will generally be entitled to obtain the benefits of the VDP only once. The CRA will not normally consider a second application unless the circumstances surrounding the second application are beyond the registrant's control and relate to a different matter than the first application.

Objection rights

If a registrant's application is accepted under Track 3, the registrant will be required to waive their right to object in relation to the specific matter that was disclosed in the VDP application, and any assessment (or reassessment) of taxes that specifically relate to that disclosure. This waiver will not prevent a registrant from filing an objection in circumstances involving calculation errors, characterization issues (e.g., taxable vs. exempt supplies), or to an issue unrelated to the matter disclosed in the VDP application.

Learn more

For more information on the proposed changes to the CRA's VDP policy, or any other topics that may be of concern, please contact your EY or EY Law advisor, or one of the following tax professionals:

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