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Say goodbye to bank secrecy and tax havens... The good old days are gone!



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As you have probably heard, there has been increasing pressure from industrialized countries to force foreign banks to disclose financial information regarding their foreign clients.

Through the OECD, mechanisms have been put in place to ensure that key information be disclosed to governments by financial institutions (especially those doing business in tax havens) about their foreign clients. Governments participating in these programs have agreed to mutual cooperation agreements, in order to facilitate the exchange of information.

These mechanisms ensure that financial institutions in each country disclose to their respective government information about their foreign clients, including their name, address, nature of their income as well as the nature of their investments. The exchange of information from the institutions to the government is done automatically, on an annual basis. Subsequently, this information will be exchanged between governments.

We would like to reiterate that this disclosure mechanism is both automatic and annual, and is already in effect in certain countries.

The vast majority of tax havens have announced that they will participate in these tax cooperation agreements. Some countries have already started to provide financial information regarding foreign clients of local financial institutions, while others have announced that they will comply in 2017, and others in 2018. Accordingly, the clients' information held by the financial institutions of most tax

havens (including Switzerland) will be communicated to the governments of the account holders' resident country.

For Canadian taxpayers, owning foreign bank or investment accounts is not illegal in and by itself. However, the holders of such accounts must disclose annually to the Canadian tax authorities the existence of these accounts as well as the income generated therefrom.

The above mentioned cooperation agreement will ensure that Canadian authorities are informed of the existence of accounts held abroad by Canadian residents.

That being said, what are the options for Canadian residents owning undisclosed foreign bank accounts?

These taxpayers are at risk of being audited or charged with tax evasion....given the existence of these new cooperation agreements, the risks associated with an eventual audit become increasingly high.

Alternatively, foreign account holders could apply for a voluntary disclosure to the Canadian and Quebec authorities. The voluntary disclosure programs ensure that holders of foreign accounts, if they qualify for the program, will not have to pay the penalties associated with unreported income and may benefit, under certain circumstances, from interest relief on their tax bill. It should be noted that specific conditions must be met in order to qualify for a voluntary disclosure.

The Voluntary Disclosure Program

The Voluntary Disclosure Program (the "VDP") gives Canadian and Quebec taxpayers the opportunity to correct inaccurate or incomplete information on their tax returns, or

to provide information they failed to report to the tax authorities.

The VDP applies to taxable income, employees' source deductions as well as sales taxes.

Accordingly, a taxpayer who holds a bank or investment account in a tax haven, and who failed to disclose the existence of this account and to report the income generated therefrom (dividends, interest, etc.) can benefit from the VDP.

Since it is not illegal to hold a bank account abroad, a taxpayer who wishes to use the VDP may wish to keep this bank account in a foreign jurisdiction.

For a taxpayer to be entitled to the benefits of the VDP, the disclosure must be "spontaneous", that is, there cannot be a tax audit, a review or an investigation impending or in progress. Furthermore, the disclosure must be "complete". Therefore, a taxpayer who holds more than one foreign account must disclose the existence of all of his foreign accounts.

A VDP application begins by sending a written request to the Canada Revenue Agency (the "CRA"), and to Revenu Québec ("RQ"). The request can be sent anonymously, but must contain certain information (ex. age, occupation, the value of the investments held in the account abroad, etc.). At this stage, the information transmitted to the tax authorities does not lead to the identification of the taxpayer. Rather, it allows the tax authorities to determine whether or not the taxpayer qualifies for the VDP.

Upon reception of the application, the tax authorities issue a disclosure number. This number essentially protects the taxpayer throughout the process, in the event that an audit or tax investigation is undertaken against the taxpayer thereafter.

As long as the taxpayer's identity is not disclosed by his representative, the taxpayer is always free to withdraw from the VDP, without cost, and above all, without having to justify his decision to the tax authorities. When an agreement has been reached between the taxpayer's representative and the tax authorities, the taxpayer's identity may then be revealed.

Subject to a few exceptions, the approximate cost of a disclosure for a Quebec resident is between 20% and 35% of the portfolio's market value. This estimate includes both the CRA and RQ tax bills, as well as the accrued interest. The taxpayer's tax bill can be reduced considerably if the latter is able to prove that some of the funds held abroad are not taxable (ex.: money from an inheritance, funds held before the taxpayer immigrated to Canada, funds that have already been taxed in Canada, etc.).

Once the taxpayer agrees to disclose his identity to the tax authorities, he must then file the amended tax returns for each taxation year (maximum of 10 years) for which he has failed to report the income earned on the foreign account.

The taxpayers' amended tax returns are then processed by the tax authorities, following which notices of reassessment showing the additional income tax and interests resulting

from the disclosure, are issued. The income tax and interests must be paid immediately.

Contrary to popular belief, taxpayers who decide to take advantage of the VDP are not "blacklisted" by the tax authorities, and are no more likely than anyone else to be the subject of a tax audit.

It is important to remember that all communications and discussions between an attorney and his client are confidential and protected by the professional secrecy privilege, even in such matters.

For more information regarding the VDP, please do not hesitate to contact any member of our tax law group.

The content of this newsletter is intended to provide general comment only and should not be relied upon as legal advice.

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