TAX

BY JAMIE GOLOMBEK

Missing slips

Evidence of due diligence and a true intention to report all sources of income can save clients from stiff penalties on reassessment.


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Tax slips — whether T4s for employment income, T3s for trust distributions or T5s for investment income — are the CRA's way of ensuring taxpayers don't forget to report all their income under Canada's self-assessment tax system.

Clients generally acknowledge the need to report all income on their slips, but what if a slip goes missing without the client realizing it, or is simply never received?

Most clients may think the risk of innocent non-reporting of income is limited to the tax owing and perhaps some arrears interest. But in some cases, the CRA may decide to also assess a penalty on the unreported income.

Under the *Income Tax Act*, a penalty can be imposed on a taxpayer who fails to report an amount of income that should have been included in his or her tax return for a particular year if he or she also failed to report an amount in any of the three prior years' tax returns.

A recent tax case decided earlier this year (*Thompson v The Queen, 2010 TCC 381*) deals with the imposition of such a penalty.

Failure to report all income

Christina Thompson failed to report $868 of income in her 2006 income tax return, and for 2007, the CRA found she failed to report over $20,000 of dividends and investment income on her return and reassessed her, imposing the non-reporting penalty.

The non-reported income was income that should have been on a T5 slip, yet Thompson testified that she never received a slip for this income. The Judge accepted this testimony, and was left to determine whether she could mount a due-diligence defence to get the penalty reversed.

After Thompson was reassessed the first time for failure to report some investment income on her 2006 return, she wanted to ensure there were no reoccurrences.

An advisor from TD Waterhouse held and managed her investments. When she met with him in November 2007, she expressed concern over the missing T5 slip for 2006, and resulting reassessment. So, to avoid similar situations in the future, her advisor suggested she contact his office in April 2008 to ensure she had all the information slips for the previous year, before she filed her 2007 tax return.

Proof of due diligence

Thompson did just that, sending an e-mail to her advisor in April 2008 in which she provided a detailed schedule showing six T3 slips; two T4RIF slips and two T5 slips with the name of the issuer, the type of income and the amount of income on each. Her advisor confirmed by e-mail that the tax slips all matched up to the investment income she received, and she proceeded to report the total amount on the slips on her tax return.

While Thompson noticed that her 2007 income was about 13% lower than it was in 2006, this did not trigger any alarm bells for her. Rather, she stated she "had assumed that this was because of a decrease in the market."

When TD Waterhouse, which received all her investment income directly into their account, verified she had all the required tax slips for 2007, it essentially confirmed for her that all 2007 investment income was accounted for, and "she would be reporting all of her investment income if she reported the income on these tax slips."

The problem was the missing income wasn't included in the tax slips she had on hand; there must have been additional slips she didn't receive, and thus was unable to confirm with TD Waterhouse.

Based on prior case law, to avoid the non-reporting penalty, a taxpayer needs to establish a due-diligence defence. Fortunately, the Judge concluded Thompson was indeed duly diligent. Having double-checked with TD Waterhouse, it was perfectly reasonable for her to assume she had all her slips and had reported all income.

According to the Judge, her failure to report the income from the missing T5 slip "was innocent and a reasonable person in the same circumstances would have made the same mistake." The penalty was ordered deleted and Thompson was awarded $500 in costs. AER

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