

Taxpayers Rights During an Audit

I recently attended a tax seminar put on by CRA auditors. I don't know if anyone not in the business can fully appreciate the energy level created by 6 auditors in a room at one time. Luckily the audience was all made up of accountants, who are used to that type of electric atmosphere, so nobody actually fell out of their chairs, although I did see a few nodding heads.

One topic that did generate some discussion, however, was that of taxpayer's rights vs. the rights of CRA. Until they are involved in a full-blown audit review, most people are unaware of the powers of CRA, and of their own rights during an audit.

For those who believe that in every circumstance under Canadian law, you are innocent until proven guilty, an audit can make you feel like you're living in a foreign country, assumed to be guilty and forced to prove otherwise. That isn't really what is happening, however. Under Canadian tax law, each person is assigned a certain amount of tax owed based upon their income and the marginal tax rate that applies. There are, however, certain allowable deductions which will serve to lower your taxes owed. When you are undergoing a compliance audit, you are being asked to prove that the deductions you have claimed are legitimate.

The Canadian tax system relies upon self-assessment, which means, in essence, that you are trusted to be honest in your reporting, and that you will maintain good books and records to support your claim. In most cases, CRA simply checks the mathematical accuracy of the return, cross-references to supporting documentation and issues a quick assessment, usually within eight weeks. Occasionally they will send out a letter requesting verification of a receipt or slip of some kind. For the majority of taxpayers, that is the end of it.

A small percentage of taxpayers each year, however, will for some reason pop up on the CRA radar-screen, and those individuals will be subject to a routine compliance audit, under which an auditor has the right to enter a taxpayer's business, and demand that the taxpayer answer his or her questions. They also have the right to obtain information from third parties, such as your bank or suppliers.

Non-compliance with the auditor's requests can result in significant penalties and problems for the taxpayer. CRA has tremendous powers to ensure tax compliance, which include the right to audit, investigate, demand and search for information into your financial affairs.

It is important to understand, should you be the target of a full tax audit, that as a taxpayer you do have rights as well, and while it may be a very Canadian trait to simply sit back and take what's coming to you, during an audit is not the time to do so. You must stand your ground and demand your rights.

At the start of an audit, you should ask the CRA auditor for ID, for the purpose of his or her visit, and for the nature of the audit, thereby establishing the guidelines under which they will conduct the audit. If you are unclear on a question that is asked, request that the auditor clarify it for you in writing, so that you can review it carefully and get back to them. Ask your accountant or other advisors for help. They are familiar with the process and can often prevent a small problem from growing into a big one.

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Taxpayers Rights During an Audit (cont'd)

Always remember, if you are the subject of an audit, that you have the right to fair treatment, you have the right to be dealt with on a timely basis and you have the right to object to any audit findings resulting from a re-assessment.

The prospect of an audit can be a very scary thing, but as I often tell my clients, the keeping of good books and records is your best defense. Under Canadian tax law, it is, in fact, a requirement that you keep good books and records, which is for your protection as well as for the benefit of the auditor. If you cannot support a deduction with documentation, that deduction will be disallowed. If you have documentation, however, and it is a legitimate deduction, then you will have proved your case. The principle is basically the same under tax law as it is under criminal or civil law; You will win or lose, based upon the evidence you provide.

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