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# Understanding TAX Audits

Does the thought of your income tax return being selected for audit concern you? Outlined are some facts about audits that you should know.

## What is a Quick Assessment?

After you file your return, it usually takes from two to six weeks to receive your Notice of Assessment and any refund that you may be entitled to. Canada Revenue Agency (CRA) will perform a Quick Assessment of the numbers on your return and ensure that they are arithmetically correct but they will not address any deductions in detail. This means CRA has not investigated your return beyond what you have filed; they are not necessarily allowing your claims. Any claims you have made are still open to review in detail in the future.

## The Next Step

After the peak period for filing has passed, CRA performs their "Processing Review Program". This is the process where your return is reviewed more thoroughly. It usually occurs between June and November each year.

## Reassessments

If you are reassessed, your taxes payable will change; which will result in a tax refund or a tax liability. Reassessments cannot normally be issued more than three years after the date of the original Notice of Assessment. However, in cases of fraud or misrepresentation attributable to "neglect, carelessness or wilful default", a reassessment can be issued at any time.

## How Are Tax Returns Selected for Audit?

The main reasons tax returns are selected for audit are:

- Random selection
- New information comes to the attention of CRA (an example would be unfiled T-slips)
- Due to the type of income earned or deductions claimed
- Due to the individual's review history (previously audited)
- For the purpose of comparison to third party information sources

## What Happens In An Audit?

In an audit, your receipts will be examined and your expenses scrutinized to ensure they are allowable. An audit should not be a cause for concern unless you have engaged in tax evasion. You don't have to deal with the auditor personally; you can avoid some of the stress of the audit process by having an accountant handle the audit. During the audit, the auditor will identify issues and discuss them with you or your

accountant. Any proposed adjustments will be explained and the auditor will give you a reasonable amount of time (usually 30 days) to respond to their proposal. Before finalizing the audit and issuing a Notice of Assessment or Reassessment, the auditor will consider any explanations you provide regarding their findings.

## Two Types of Audits – Desk Audits and Field Audits

**Desk Audits.** Most audits of individuals are desk audits. The auditor will ask you to supply supporting documentation for the claims you have made. This usually takes place by mail, phone or fax. You will not have to meet the auditor. These "spot-checks" are designed to verify claims such as RRSP contributions, tuition fees, and medical expenses. In some cases, you may be asked to complete a questionnaire.

**Field Audits.** In a field audit, the auditor will meet with you or your accountant to review all your records and verify the amounts claimed on your return. For individuals, this may take anywhere from a few hours to a few days.

**Tax Tip.** Keep your tax return and all supporting documents in one place. In the event of an audit, you will be able to find everything to support your claims. Unsupported claims will normally be disallowed.

## What Happens In a Business Audit?

Initially, the auditor will ask for the supporting documentation for your revenue and expense claims. This will include sales invoices, expense receipts and possibly business and personal banking records. In some cases, they will request that you tape your expenses. This refers to a calculator tape stapled to your expense receipts. If you have a formal accounting system, they will also want to see the financial statements, general ledger and related information.

## What Happens If You Disagree With Your Reassessment?

If you disagree with the Notice of Assessment or Reassessment, you have 90 days from the date of issue to file a Notice of Objection.

## Be Prepared If the Auditor Comes Knocking...

You have just received a letter from the CRA. They have selected your tax return for review. Can your return stand up to scrutiny? Since it is your responsibility to apply the tax rules correctly, you will be held accountable for any errors. To avoid being levied a fine, penalty and/or interest charges, ensure that you have a competent advisor so that your return is completed properly and that you pay the "correct" amount of tax. A competent tax advisor will enable your return to stand up to scrutiny.

This information is current to January 2008. It is of a general nature and is not intended to address the specific circumstances of a particular individual. You should not act on this information without appropriate professional advice after thorough examination of a particular situation. E&OE