

Minister
of National Revenue



Ministre
du Revenu national

Ottawa, Canada K1A 0A6

MAY 29 2019

The Honourable Kevin Sorenson
Chair of the Standing Committee on Public Accounts
House of Commons
Ottawa ON, K1A 0A6

Dear Colleague:

Pursuant to Standing Order 109 of the House of Commons, I am pleased to respond on behalf of the Government of Canada to the recommendations made in the 59th Report of the Standing Committee on Public Accounts entitled: *Report 7, Compliance Activities – Canada Revenue Agency, of the Fall 2018 Reports of the Auditor General of Canada*, tabled in the House of Commons on February 6, 2019.

The Government would like to thank the Committee for its review and recommendations to ensure that the Canada Revenue Agency addresses each of the issues identified in the Auditor General's audit. The Government appreciates the insights and support provided by the Committee.

The Government Response takes into account the Canada Revenue Agency's commitment to apply the *Income Tax Act* consistently during its compliance activities and to accurately report the results of its compliance activities. It also supports my mandate letter priority to make it easier for taxpayers to meet their tax obligations and my overarching goal to ensure that the Canada Revenue Agency is fairer, more helpful, and easier to use.

Please find enclosed a copy of the Government's Response to the recommendations of the Report.

Sincerely,

A handwritten signature in blue ink, appearing to read 'Diane Lebouthillier'.

The Honourable Diane Lebouthillier, P.C., M.P.
Minister of National Revenue

**GOVERNMENT RESPONSE TO THE 59th REPORT OF THE
STANDING COMMITTEE ON PUBLIC ACCOUNTS ENTITLED: REPORT 7,
COMPLIANCE ACTIVITIES – CANADA REVENUE AGENCY,
OF THE FALL 2018 REPORTS OF THE AUDITOR GENERAL OF CANADA**

INTRODUCTION

The Government of Canada is pleased to respond to the 59th Report of the Standing Committee on Public Accounts entitled: *Report 7, Compliance Activities – Canada Revenue Agency, of the Fall 2018 Reports of the Auditor General of Canada*, tabled in the House of Commons on February 6, 2019.

After carefully reviewing the Committee's report, the Government has chosen to respond to each recommendation individually. The Government of Canada appreciates the work of the Committee and welcomes its analysis, views and recommendations.

The government response agrees with the content of the report's 10 recommendations and acknowledges the Committee's recommended reporting schedule. However, in order to maximize efficiency and provide more robust reporting on progress to the Committee, the Government proposes an alternative schedule, which provides all of the requested reports but with less frequent status reporting and more harmonized reporting dates.

The Committee's reporting schedule calls for updates at nine separate dates, while the Government's alternative schedule proposes status updates at four separate dates.

The alternative schedule would provide a more integrated reporting, to clarify the work being done by the Canada Revenue Agency (CRA or Agency).

The following represents the Government initial response, including responses for Recommendation 1 and Recommendation 2 requests for progress on or before May 30, 2019.

ABOUT COMPLIANCE ACTIVITIES

The CRA administers taxes for the Government of Canada and for most provinces and territories. Canada operates a self-assessment system of taxation, whereby taxpayers determine their own tax liabilities under the *Income Tax Act*, and file their own returns to reflect those liabilities.

Part of the CRA's mandate is to ensure that taxpayers comply with the income reporting requirements of the *Income Tax Act*. The Agency aims to protect the integrity of the tax system by identifying and deterring those who do not comply.

Participation in this system of voluntary compliance is contingent to a large extent upon taxpayer confidence in the integrity of the tax system which is, in turn, significantly impacted by the timeliness and fairness, actual or perceived, of CRA's compliance activities.

RECOMMENDATIONS

Recommendation 1: That the Canada Revenue Agency provide the House of Commons Standing Committee on Public Accounts with: (1) a status report on the revisions undertaken on time limits for taxpayers, by 30 May 2019; and (2) a final report outlining its revised policy with a set timeline for all taxpayers to provide information to the Agency in response to compliance activities, by 31 March 2020.

The Government of Canada agrees with this recommendation.

The Government agrees that it is necessary to establish clear guidelines on timelines of when the CRA is expecting taxpayers undergoing audits or reviews to provide requested information to the CRA. These timelines nonetheless should take into consideration the level of complexity of, as well as the specifics of the taxpayer's situation. The CRA should ensure that the guidelines are well understood by the taxpayers and the consequences when there is failure to provide the information. These guidelines will still provide CRA auditors with some discretion to take into account the specific circumstances of taxpayers.

Timelines given to taxpayers to comply with information requests from the CRA depend on the taxpayer's type of business activity and the type of audit conducted by the CRA, so there can be significant variations in the amount and complexity of information requested and the effort required by taxpayers to comply with the requests. For example, providing a receipt to substantiate a single expense on a personal income tax return requires much less time than providing the full records from the full revenue stream of a taxpayer's foreign affiliate. The CRA will ensure to provide timelines that take these circumstances into consideration.

If a taxpayer requires more time to comply with a request to provide information, they can contact the CRA and explain their circumstances. The Taxpayer Bill of Rights requires that the CRA take individual circumstances into account when granting extensions to taxpayers to respond. In complex cases, when taxpayers do not willingly comply with those requests, the CRA may resort to obtaining information from third parties, through judicial processes, or from foreign tax administrations; all of which contribute to substantial delays and also may be dependent on the availability of Department of Justice resources to initiate the judicial process. The Agency will clearly outline the parameters of addressing cases in which the time limits are not respected, and ensure that it communicates these expectations clearly with affected taxpayers.

Because auditors need to use judgement to determine the best strategy for obtaining the necessary information from taxpayers, the Agency is reviewing internal procedures describing the circumstances and criteria for granting extensions to taxpayers that take into consideration the complexity of the information request and the impact on the taxpayer. The CRA is also considering more formal internal deadlines after which it would move to the courts to compel the required information.

With respect to the report requested by the Committee by May 30, 2019, the CRA would like to report that it has established an internal working group, and has started consultations with key stakeholders, including developing an Agency-wide questionnaire to collect information on the current practices for handling information requests that will inform its analysis and recommendations.

With respect to the second part of the recommendation, the Agency will provide the Committee with a final report on its efforts to improve the consistency of enforcing timelines on audit information requests by June 30, 2020. This will allow the Agency to gain a better understanding of the impact that these changes have made, and to conduct a more thorough environmental assessment to report on.

Recommendation 2: That the Canada Revenue Agency provide the House of Commons Standing Committee on Public Accounts with: (1) a report on the review of the proactive relief criteria and procedures, by 30 May 2019; and (2) a report on the new guidelines regarding the definition of undue delay, by 30 June 2020.

The Government of Canada agrees with this recommendation.

With respect to the report requested by the Committee by May 30, 2019, the CRA would like to report that it has drafted a new governance agreement and memoranda of understanding related to the administration of the taxpayer relief provisions. The agreement identifies responsibility for the administration of the various provisions. During this process, the CRA reviewed the current policy and procedures for the consideration of proactive relief, including the feasibility of the application of proactive relief in the conduct of various compliance activities.

The CRA will also conduct a review and analysis of the various compliance activities by the end of March 2020 and, where reasonable, define the appropriate criteria to determine what it considers to be an "undue delay." The development of any guidance will also ensure that all relevant factors continue to be considered in accordance with the legislation.

With respect to the second part of the recommendation, the Agency agrees to provide the Committee with a report on the new guidelines by June 30, 2020.

Recommendation 3: That the Canada Revenue Agency provide the House of Commons Standing Committee on Public Accounts with: (1) a status report on the consultations with the Agency's stakeholder regarding (a) harmonization of the application and administration of the taxpayer relief provisions; and (b) determination of responsibility for delays (falling to either the Agency or the taxpayer), by 31 October 2019; and (2) a final report on these two matters, by 30 May 2020.

The Government of Canada agrees with this recommendation.

With respect to the first part of the recommendation, the CRA is committed to providing fair relief and to not rewarding non-compliance. In order to mitigate any inconsistent application or administration of the taxpayer relief provisions, the Agency will ensure to harmonize policies, procedures, guidelines, and training materials as committed in the publicly available internal audit report entitled *Internal Audit – Application of the Taxpayer Relief Provisions*.

The CRA will clarify what is considered to be delays attributed to the Agency (within the Agency's control) and delays attributed to the taxpayer (within the taxpayer's control) in the conduct of the various compliance activities by the end of March 2020, considering the discretionary nature of the provision. The Agency will provide the Committee with a status report on its consultations with the Agency's stakeholder branches by December 31, 2019. The additional time will allow the Agency to complete the necessary consultations, allowing for a more robust analysis of this issue.

With respect to the second part of the recommendation, the CRA will provide the Committee with a final report on these two matters by June 30, 2020. As the Agency will be reporting on other matters on this date, it will provide the Committee with a more complete picture of where the Agency stands regarding its analysis and implementation of recommendations.

Recommendation 4: That the Canada Revenue Agency provide the House of Commons Standing Committee on Public Accounts with: (1) a report describing the reasons for regional variations in the time required to complete its compliance activities, by 30 September 2019; and (2) a report outlining the measures in place to reduce or eliminate these variations, including a reallocation of resources, so that two taxpayers with a similar profile and files of similar complexity are dealt with in the same manner by the Canada Revenue Agency, no matter where their files are processed, by 30 April 2020.

The Government of Canada agrees with this recommendation.

With respect to the first part of the recommendation, the CRA is committed to treating taxpayers fairly and in adherence to the Taxpayer Bill of Rights and completing audits within the legislated timelines. The sectors of activity and structure of the business communities vary across the country and CRA's tax service offices are modeled

according to the differences in industries found in different regions. There may be a perceived regional difference in the audit completion. However, these differences can often be found because different tax centres in different regions have different expertise and process files of specific sectors of the economy. The extent and nature of non-compliance can vary considerably due to variations in schemes used by taxpayers to pay less or no taxes. Nonetheless, the CRA recognizes that there may be factors within its control to fix, so it is conducting a review to identify the main reasons for regional variations and will create a plan to address any problematic issues identified by the review. The Agency will provide the Committee a status report with the reasons for regional variations by December 31, 2019.

With respect to the second part of the recommendation, the Agency will provide the Committee a final report on the measures in place to reduce variations by June 30, 2020. As the Agency will be reporting on other matters on this date, it will provide the Committee with a more complete picture of where the Agency stands regarding its analysis and implementation of its plan.

Recommendation 5: That the Canada Revenue Agency provide the House of Commons Standing Committee on Public Accounts with: (1) a report establishing targets for average and maximum processing times for assessments resulting from compliance actions, by 31 December 2019; and (2) a first monthly follow-up report on processing times for assessments resulting from compliance actions, by 31 March 2020.

The Government of Canada agrees with this recommendation.

With respect to this recommendation, the CRA is developing service level agreements to establish and track the time it takes to process assessments resulting from audit programs which will enable the CRA to improve the timeliness of the reassessment processes. The Agency will provide the Committee with a status report by December 31, 2019 and a final report on its efforts to establish and track service levels for (re) assessments arising from its audit programs by June 30, 2020. This additional time will allow the CRA to conduct its ongoing internal quality assurance activities on the data that will go into the report following the end of the fiscal year.

Recommendation 6: That, by 30 April 2020, the Canada Revenue Agency, after determining the impact of past disclosures made under the Voluntary Disclosures Program, provide the House of Commons Standing Committee on Public Accounts with a report detailing the results and recommendations to enhance its risk assessment processes.

The Government of Canada agrees with this recommendation.

With respect to this recommendation, the CRA is conducting a review of past voluntary disclosures to determine if taxpayers have remained compliant in the tax areas where they provided corrected or more complete filings. The aggregated results of this review will be used to enhance the risk assessment methodologies over

time. Importantly, following a recommendation made by the Offshore Compliance Advisory Committee, the CRA reviewed and limited the Voluntary Disclosures Program. Since March 1, 2018, taxpayers who intentionally avoided their tax obligations are no longer able to benefit from the same level of relief as taxpayers who apply for relief to correct an unintentional error. In addition, the CRA has created the Offshore Voluntary Disclosures Program Section to provide an in-depth review of high risk disclosures involving offshore issues.

The Agency will provide the Committee a report with how it plans to follow up on taxpayers who have used the Voluntary Disclosures program to verify future compliance by June 30, 2020. As the Agency will be reporting on other matters on this date, it will provide the Committee with a more complete picture of where the Agency stands regarding its analysis and recommendations to enhance its risk assessment processes.

Recommendation 7: That, by 31 December 2019, the Canada Revenue Agency provide the House of Commons Standing Committee on Public Accounts with a report that reviews and clearly documents its methodology to set targets for tax earned by audit.

The Government of Canada agrees with this recommendation.

The Agency does agree that documentation can always be improved, so it is reviewing and will more clearly document the process used to establish revenue projections. This analysis will be completed by March 2020. Because our new performance measurement framework will impact how the Agency sets targets for additional revenues, the CRA will address this issue in its final report for Recommendation 10, by June 30, 2020.

The CRA puts considerable care into setting the projections for tax earned by audit (TEBA) each year. TEBA projections factor in past results, the type and location of compliance risks, the experience level of auditors and budget for available resources, and key priorities such as commitments for Budget priorities.

Establishing projections requires in-depth program expertise and experience to be able evaluate previous results, trends and factors that go into setting projections. Program and administrative changes need to be known and understood in order to predict their impact on future projections. Determining an annual target is more than a simple quantitative exercise; it is also a qualitative process that requires informed judgement and validation with regional offices across the Agency.

Recommendation 8: That, by 31 December 2019, the Canada Revenue Agency provide the House of Commons Standing Committee on Public Accounts with a report on the work it has undertaken to share information on objections and the associated results with taxpayers.

The Government of Canada agrees with this recommendation.

The CRA agrees to provide the Committee a report on the work it has undertaken to share information on objections and the associated results with taxpayers by December 31, 2019.

Information on objections is currently available on the CRA website. There are three levels of complexity for objections – low, medium, and high. Every month, the CRA updates how many days it will take on average to assign and resolve objections of low and medium complexity.

Recommendation 9: That, by 30 April 2020, the Canada Revenue Agency provide the House of Commons Standing Committee on Public Accounts with a report on the results of its research and evaluation of measures to track additional tax revenue generated from increased budgetary funding; and a final report by 31 October 2022.

The Government of Canada agrees with this recommendation.

The Agency does track the results of incremental budgetary funding, and the concern raised by the AG was over the methodology for attributing the incremental impact from the increased resources. The Auditor General's concern relates to how the Agency attributes its results to the source of funding of the activity type (core budget versus new funding from Federal Budget initiatives) rather than the soundness of the data. While the CRA's current reporting methodology for tracking additional revenue generated from Federal Budget funding satisfies the requirements of the Treasury Board Secretariat and the Department of Finance, the CRA accepts this recommendation. The CRA is analyzing the accuracy of its performance measures for return on investment of budget investments and will include any proposed new measures in the performance measurement framework to be developed by March 2020.

The CRA will provide the Committee with a report on the results of its research and evaluation of measures to track additional revenue from Budget investments by June 30, 2020. The additional time will permit it to be integrated with its other work on performance reporting. The Agency will also provide the Committee with a final report by October 31, 2022.

Recommendation 10: That, by 30 April 2020, the Canada Revenue Agency provide the House of Commons Standing Committee on Public Accounts with a report on its new performance measurement framework for compliance activities and the actual collected tax revenues.

The Government of Canada agrees with this recommendation.

The CRA has already started working on new horizontal performance measures to provide a more comprehensive overview of program outcomes, following recommendations from a recent internal evaluation. However, the CRA does not have the tools to calculate the actual dollar amount collected from audit assessments, due to the complexity of the calculation and current system limitations.

The actual amount collected from an audit assessment is impacted by partial payments made over many years, and in some cases decades, offsets from other related tax accounts, daily compounding interest that increases the debt, and the application of non-cash credits/debits, such as loss carry forwards, changes to depreciation allowances or capital dividend accounts. This level of complexity and limitations of the CRA's current accounting systems prevent the Agency from providing the Committee with the requested information. The CRA had performed preliminary analysis of the cost of a new system to track the amounts collected on audits, and this proved cost-prohibitive. The CRA proposes to respond to this recommendation to the extent feasible, using manual estimates.

The CRA will be developing additional strategic measures that will estimate the impact of litigation, collections and deterrence using estimates or ratios to fill in any areas that defy an exact count. The CRA is developing a performance management framework and implementation plan for its compliance programs, including measures that factor litigation and collections, by March 2020.

The Agency will provide the Committee with a final report on the new performance measurement framework for compliance activities by June 30, 2020. This alternative date will allow for the integration of impacts of the new performance measurement framework on how the Agency sets its TEBA targets, as well as any new measures to track additional revenue from Budget initiatives.