



## **Audit Angst And How to Prepare So There is None**

Although audits are all part of the fun for me, to most of you reading this, the thought of an audit scares you deep down in places you don't like to talk about. I get it. I also know that most of the angst you feel is a fear of the unknown. 'What are they after?' 'What will they find?' 'Did I keep good enough records?' 'Can I get in trouble?' 'Will I be tossed into the bowels of some secret CRA gulag while they seize my assets and slave out the family dog to pay for all the fines and penalties they've assessed?'

Relax. I'm about to give you the tools to breeze through the process like it's nothing at all. It will be like shining a flashlight in that deep down place and seeing there was nothing there the whole time. We'll start by taking a closer look at audits and what you need to have on hand in case the CRA wants to take a peek at your books. It's time to take a little of the unknown out of your fear.

### ***Why me?***

Audits are assigned by the CRA using risk assessment. If the CRA determines that you have made frequent errors in your revenue reporting, or there is a high likelihood that errors have been, or will be made, they may want a review of your books.

By law, you are required to keep adequate records to determine your taxes owing or entitlements owed to you. You have to disclose these records to the governing body (Canada Revenue Agency) when requested. Non-compliance is a 'red flag' for the CRA and may also trigger an audit.

The burden of proof is on you (the taxpayer) to prove intent to produce income. That means if you don't properly keep or disclose your records (i.e., accurate figures!) then the buck stops with you - not the CRA, and not your wonderful accounting professional. Remember, it's my job to make sure that your taxes are compiled and submitted according to federal guidelines, but I can only work with the figures you give me!

### ***What happens during an audit?***

If the CRA selects you for an audit, the auditor will contact you by phone, letter, or both. If possible, they will come to where you keep your books. That may be your house, office, or your accountant's office.

The auditor is looking for inconsistencies in what you've reported versus what your records show. They may look at previous tax returns, credit bureau searches or asset records. They may also want to see your personal bank and credit card statements, and your mortgage docs. If you own a business, they will likely want to see your ledgers, business bank statements, invoices, receipts, etc.



You should know that a CRA auditor is not limited to you and your records. They also have the right to examine the personal or business records of people and businesses not being audited. In other words, they can examine the records of your spouse, family members, business associates, or trusts.

### *What are my responsibilities?*

#### *Receipts*

You are expected to keep all receipts that you've used to calculate income or deductions. NOTE: You need to keep the actual invoice or receipt that itemizes the purchase and not just the credit card slip or bank statement! The receipts you present must be legible (not faded) and the reason for the receipt must be self-evident or documented on the receipt.

Now, wait! Before you start cursing under your breath and rifling through that Longo's bag full of crumpled receipts, you should know that there are scanning apps available that will help you keep organized. At the end of each work day (or week) you simply scan the receipts, and the app will create an organized and searchable database that the auditor will appreciate. And frankly, so will I!

Scanning apps come in several types. There are PC-based apps, cloud-based apps, and mobile apps. Basic apps are free while others with more features require you hand over a few dollars. TechRepublic does a good job summarizing five of the top apps:

<http://www.techrepublic.com/blog/five-apps/five-apps-for-managing-your-receipts/>

If you are claiming GST/HST for a business, the vendor's business number (BN) and business name must be on the receipt. Any invoices or receipts you report as a business expense will need to be in your name, and not someone else's for a valid claim. A receipt in the name of your spouse is sometimes allowed but not always. As well, make sure you categorize your expenses correctly between assets and supplies.

As a business owner, you are allowed to claim business-related meals and entertainment, but you need to document those claims properly. Record on the receipt (or in your new handy-dandy scanning app) the reason for the dinner or event and the name of the person you were wining and dining (e.g., Your favorite accountant!).

Generally speaking, the CRA expects you to keep your records for six years. Records for any asset you purchase (and claim), however, must be kept until the asset is fully depreciated. That means you will need to keep those records in a permanent folder. It's a good idea, then, to sort your receipts by how you pay for them. See below for a checklist of documents required for bookkeeping.

#### *Vehicles*

If you are claiming vehicle expenses, you need to keep a vehicle log. 'But Debbie', you say, 'there is case law that says a log is not required but that a reasonable amount of vehicle expenses is acceptable.' That is true, my learned friend. But here's the rub. During an audit, you may need to *prove* that your



expenses were ‘reasonable,’ and if your definition of reasonable differs from the CRA’s ... well, you can guess who would win that tug-of-war. Bottom line: keep a vehicle log.

A vehicle log will record the reason for the usage, mileage, gas and oil expenses, repairs, and depreciation over the year. You will need to keep business and personal mileage separate. If you don’t use a vehicle log yet, try this one from PWC: <http://pwc.to/2nJDyZO>.

Finally, make sure your receipts total the line items reported on your tax return. That’s it. Now you know why you might be the subject of an audit, what the CRA would need to see, and what to keep year-to-year to prevent any issues.

### ***Summary***

So, if you build a few good habits into your bookkeeping regime, an audit would be nothing more than a quick peek and an approving nod. Below is a summary for reference. Good luck and happy scanning!

- ✓ Scan receipts to keep them organized.
- ✓ Sort receipts by how you've paid.
- ✓ For GST/HST claims, make sure vendor's name and BN is on the receipt.
- ✓ Ensure invoices and receipts show your name or your business name.
- ✓ Keep a vehicle log.
- ✓ Keep all records for six years and asset records until asset is completely depreciated.
- ✓ Make sure receipts and tax return line items agree.

Want to know more? The article you just read sources information distributed by the CRA. For more details, try these links:

*“What you should know about audits”*

<http://www.cra-arc.gc.ca/E/pub/tg/rc4188/rc4188-e.html>

*“Books and records – Retention/Destruction”*

<http://www.cra-arc.gc.ca/E/pub/tp/ic78-10r5/README.html>

*“Keeping records”*

<http://www.cra-arc.gc.ca/records/>