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CRA Turns Its Focus to Cryptocurrency Transactions

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The Federal Court (FC) recently authorized the Canada Revenue Agency (CRA) to issue an "unnamed persons requirement" (UPR) to Coinsquare Ltd. for information and documentation relating to users of Coinsquare, a cryptocurrency exchange operating in Canada. This UPR is part of an on-going CRA project, led by the CRA's specialized "Cryptocurrency Section" of the CRA's Digital Compliance and Audit Support Division, which, according to publicly available information from the Canadian government, may have up to seven team members. The project is aimed at taxpayers who have failed to properly report income from cryptocurrency transactions. This large scale audit may affect not just those taxpayers who intentionally did not report income from cryptocurrency transactions, but also those taxpayers who unintentionally failed to report such income – even if the omission occurred years ago.

Canadian income tax and sales tax legislation provides that the CRA, with FC authorization, can require any person to provide information and documentation relating to a group of "unnamed persons," provided that (i) the group of persons is "ascertainable," and (ii) the requirement is made to verify compliance by the person or persons in the group with income tax or sales tax legislation.

The FC order (Coinsquare Order), dated March 19, 2021, relates to Coinsquare users who fall into at least one of the three following categories (Coinsquare Users):

- users with accounts with a value of at least $20,000 on December 31 of any year from 2014 to 2020 (inclusive)
- users who have deposited a cumulative sum of $20,000 since opening their Coinsquare accounts, and
- the 16,500 largest user accounts by trading volume in Canadian dollars between 2014 and 2020, and, if not already included, the 16,500 largest user accounts by number of trades between 2014 and 2020.

This UPR, once issued, will require Coinsquare Ltd. to provide three broad categories of documents and information on Coinsquare Users pertaining, to the period from January 1, 2013, to the date of the Coinsquare Order. First, Coinsquare must provide the CRA with a list of Coinsquare Users, as well as "know-your-customer" reports and deposit addresses. Second, Coinsquare must provide a list of all cryptocurrency and fiat currency deposits and withdrawals from Coinsquare Users' accounts, including identifying the source and destination of deposits and withdrawals, respectively, details about the method of funding and withdrawal from the Coinsquare Users' accounts, the date and time of each transfer and all other captured information regarding funding and withdrawals from the accounts of Coinsquare Users. Third, Coinsquare must provide a detailed listing of all trading activity of Coinsquare Users, including information indicating trading pairs, buy/sell orders, date, time, amount, price per unit, fees, transaction identifiers, as well as a list of all known cryptocurrency addresses that were, or may have been, used by the Coinsquare Users during the relevant period.

The CRA indicated that it would use the information gathered to determine whether Coinsquare Users have filed required income tax returns, payroll remittances and GST/HST returns, as well as to ensure that profits earned by the Coinsquare Users engaged in cryptocurrency businesses were properly reported as business income. This suggests that the CRA will be analyzing Coinsquare Users' trading patterns to determine whether they were engaged in a trading business. The CRA also indicated that it would assess whether Coinsquare Users duly collected GST/HST, suggesting it would treat cryptocurrencies occurring prior to 2018 as being subject to GST/HST, notwithstanding proposed amendments to the GST/HST treatment of cryptocurrencies exempting them from sales tax (which are discussed in more detail here).

The CRA's representations to the FC suggest that, given the general anonymity of cryptocurrencies, UPRs aimed at online cryptocurrency exchanges and other third parties will be an important tool in cryptocurrency audits in the future. Though it is possible to contest UPRs at the stage of FC authorization, it may be preferable to limit the scope of the CRA's information request through proactive negotiations with the CRA.

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