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The CRA Cannot Compel Oral Interviews During an Audit

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In *Minister of National Revenue v Cameco Corporation*, the Federal Court of Appeal (FCA) dismissed the Minister of National Revenue's appeal and held that the Canada Revenue Agency's (CRA's) audit powers under the *Income Tax Act* (ITA) do not extend to compelling taxpayers to be subjected to oral questioning. We expect this judgment to have a significant impact on the conduct of audits.

The CRA's Audit Powers

As was confirmed by the Supreme Court of Canada almost 30 years ago in *McKinlay Transport Ltd.*, the CRA's audit powers are, generally speaking, quite broad. Taxpayers are required to keep books and records at their places of business or residence, and auditors may at any time "inspect, audit or examine" them, under paragraph 231.1(1)(a). To that end, auditors may, at all reasonable times, and for any purpose related to the administration and enforcement of the ITA, enter businesses where such books and records are kept and require taxpayers or their agents to provide "all reasonable assistance and to answer all proper questions" regarding those books and records, in accordance with paragraphs 231.1(1)(c) and (d). If taxpayers fail to comply, the CRA may bring an application to the Federal Court to compel them to provide "any access, assistance, information or document."

Though the ITA focuses on the CRA's power to access books and records, and to request documents and information, it is a long-standing CRA practice to interview taxpayers and their agents in the course of an audit, which is commonplace in transfer pricing audits. This practice was the subject of the recent FCA decision in *Cameco*.

Background

Cameco Corporation (Cameco) has been under a lengthy transfer pricing audit. In the course of this audit, the CRA requested that Cameco make available for questioning 25 of its employees, spanning several offices worldwide, so that it may better understand the impugned transactions between Cameco and its foreign subsidiaries. At this stage of the audit, the CRA had already interviewed several Cameco employees. Cameco refused the CRA's request, but agreed to answer questions in writing.

The Minister of National Revenue (Minister) applied to the Federal Court (FC) for a compliance order asking that Cameco be compelled to comply with the request for oral interviews. The FC dismissed the application, finding that the Minister's request was unreasonable.

The Minister appealed the FC decision to the FCA, arguing that the power to "inspect, audit or examine" under paragraph 231.1(1)(a) is broad enough to encompass the authority to compel oral interview of taxpayers or their employees, including the employees of the taxpayers' foreign subsidiaries. The appeal, therefore, turned on the interpretation of the words "inspect, audit or examine."

The FCA's Decision

Applying the modern approach to statutory interpretation, Rennie JA, writing for the majority of the Court, found that a textual, contextual and purposive analysis of paragraph 231.1(1)(a) leads to the conclusion that it does not permit the Minister to compel oral interviews of a taxpayer or its employees (concurring reasons were given by Woods JA, who would have disposed of the appeal on narrower grounds).

The FCA first engaged in a textual analysis of the provision, making a number of important findings:

- On a plain reading, the power to "inspect, audit or examine" does not include oral examination, and the word "audit" does not imply oral examination.

- That provision obligates taxpayers to assist the Minister only with respect to the inspection, search, examination or review of books and records – that is, documentary information. Indeed, the Minister may ask compellable questions to taxpayers, but only with respect to the origin and location of books and records that are the subject of an audit. Taxpayers' obligation to assist the Minister does not encompass non-documentary information, such as any information that would be gathered by means of general questions.
- Taxpayers cannot be compelled to explain what they did or to provide explanations with respect to the facts, assumptions and other considerations taken into account in preparing their returns. In so holding, the FCA reiterated its earlier finding in *BP Canada* that auditors “cannot compel taxpayers to reveal their soft spots.”
- If the requirement to answer questions was implied in the power to “inspect, audit or examine,” as argued by the Minister, then paragraph 231.1(1)(d) – which states that taxpayers must provide “all reasonable assistance and to answer all proper questions” during on-site audits – would be redundant.

Next, the FCA considered contextual factors. It noted that the purpose of section 231.1 and the preceding section is to allow the Minister to independently verify taxpayers' records that are kept at their places of business. Further, comparing the ITA to other statutes, the FCA found that when Parliament wants to compel a person to answer questions, it does so expressly.

Then, turning to a purposive analysis, the FCA found that its interpretation does not undermine the Minister's ability to verify information received from taxpayers in the context of a self-reporting system, because the Minister may still draw inferences when no answers are given and make assumptions to support assessments.

Finally, the FCA examined the legislative history of the provision. It observed that the previous version of the provision contained the phrase “answer all proper questions relating to the audit or examination either orally or, if he so requires, in writing,” which language was deleted when the provision was last amended. This deletion suggests an intention to limit the scope of the provision, which is consistent with the Technical Notes to the amendment.

Takeaway

The FCA's approach showed careful attention to the text and context of the ITA and, significantly, an unwillingness to extend audit powers absent explicit statutory authority. This restrained analysis diverges from the CRA's historically broad interpretation of its audit powers, on which it has relied to compel taxpayers to provide oral answers to its questions. By refocusing the CRA's audit power on the inspection of books and records, this judgment is likely to have widespread repercussions on the way audits are conducted.

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