

POWERS V. DUTIES

Dealing with Revenue Canada's Investigative Arm

This paper examines the investigative powers of Revenue Canada and the role and duties of a tax or accounting advisor when confronted with the exercise of those powers.

The source of Revenue Canada's investigatory powers is, with small exception, the Income tax Act (*Act*). The *Act* has been placed under the microscope of judicial analysis since its inception but in particular from the time of enactment of the Canadian Charter of Rights and Freedoms in 1982. At issue has been the struggle between enforcing the terms of a voluntary reporting system designed for the overall public benefit and the prized protection of privacy of the individual. Unfortunately for some, the *Act* and the powers conferred by it have largely, subject to some notable recent exceptions, withstood a barrage of Charter challenges.

Until recently, Revenue Canada had four types of investigative powers:

- inspection
- requirement for documents and information
- search and seizure
- inquiry

The power to conduct an inquiry was struck down by the Federal Court of Canada and will not form part of this discussion (*Del Zotto et al v. The Queen et al* (1997) 147 DLR (4th) 457)

INSPECTION

I.T.A. s. 231.1

This is the section relied upon by Revenue Canada Auditors to visit taxpayers, accountants and others to assemble information about the affairs of those taxpayers. It allows:

“an authorized person”

- persons authorized by the Minister of National Revenue under Part IX of the Regulations to the *Act*. That authority is evidenced by a plasticized authorization card (T3000) evidencing the authorizing signature of the Deputy Minister.

“at all reasonable times”

- this is usually during business hours and seems to contemplate some reasonable notice but not necessarily so.

“for any purpose related to the administration or enforcement of the *Act*”

- an inquiry to determine the tax liability of specific person(s) or to verify compliance with the *Act* by identifiable persons. The person(s) must be named and may not be referred to simply as members of a class.

“to enter any premises or place where business is carried on, property, books or records are kept, or anything is done in connection with the business”

- the books and records referred to are undoubtedly those mentioned under s. 230 of the *Act*.
- If the premises are a “dwelling house” (the whole or any part of a building kept or occupied as a permanent or temporary residence (s.231)), entry may not be gained without consent of the occupant or under the authority of a warrant of a Queen’s Bench or Federal Court Judge. Before granting the warrant pursuant to s. 231.3 of the *Act* the Judge must be satisfied (a) the premises are where business is carried on, property books or records are kept, or anything is done in connection with the business; (b) entry is necessary for any purpose relating to the administration or enforcement of the *Act* and; (c) entry has been or will be refused. As an alternative the Judge may order the occupant to provide reasonable access to Revenue Canada to the records or items sought.

“to inspect, copy, audit or examine the books and records of the taxpayer or of any other person that relates or may relate to the information that is or should be in the books or records of the taxpayer or to any amount payable by him under the *Act*”

- “document” includes money, a security and a record (s. 231)
- “record” includes an agreement, a book, a chart or table, a diagram, a form, an image, an invoice, a letter, a map a memorandum, a plan, a return, a statement, a telegram, a voucher and any other thing containing information, whether in writing or in any other form (s. 248)
- This definition was enacted in its present form in 1998 to eliminate the argument that tax planning memos weren’t produceable. The only position left to avoid production of those memos is that they are not required “to determine a taxpayer’s liability or verify compliance with the *Act*”.

“to examine property in the inventory of a taxpayer or any property or process of or matter relating to the taxpayer or any other person an examination of which may assist the authorized person in determining the accuracy of the inventory of the taxpayer or in ascertaining the information that is or should be in the books or records of the taxpayer or any amount of any tax payable by the taxpayer under the *Act*”

“to require the owner or manager of the property or business and any other person on the premises to:

- a) **give reasonable assistance**
- b) **attend at the premises or place with the authorized person(owner or manager only)**
- c) **answer all proper questions relating to the administration or enforcement of the *Act*.**

- a taxpayer or any other person must comply unless unable to do so (231.5(2)). Reasonable assistance is such assistance as is reasonable in the circumstances to enable the authorized person to carry out the audit and may include obtaining records or explaining procedures or documents but does not include the creation of new documents. Proper questions are those which are relevant and which relate only about the taxpayer regarding the administration and enforcement of the *Act*.
- the duty of confidentiality does not generally override the duties imposed by this section
- failure to comply is an offence under s. 238 calling for fines between \$1,000 and \$25,000 or fines and imprisonment up to 12 months.

REQUIREMENT FOR DOCUMENTS OR INFORMATION

I.T.A. s. 231.2 & 231.6

Instead of or in addition to the quasi-criminal sanctions for noncompliance with the inspection requirements, Revenue Canada make seek to force compliance with requests for documents or information by serving taxpayers, practitioners or third parties with a “requirement”. Section 231.6 allows for the service of a “requirement” for relevant information or documents located outside Canada.

“The Minister or persons authorized under the *Act*”

- a limited number of persons defined under Part IX.

“may, for any purpose related to the administration or enforcement of the Act, by notice served personally or by registered or certified mail”

- service may be proved by an affidavit of an officer of Revenue Canada. Such affidavit is prima facie evidence of the demand and its service.

“require that”

- the language used is mandatory. Failure to comply is an offence under s. 238. The time period for compliance is “such reasonable time as may be stipulated in the notice” Although the section does not contemplate a minimum reasonable time, Courts have held that “10 days” or “without delay” were both unreasonable provisions. Revenue Canada is usually content to allow 30 days for a response.

“any person”

- this obviously extends to accountants, lawyers and former employees or associates. The requirement is enforceable even though it may cause a great deal of inconvenience or expense.(CIBC v. The Queen 62 D.T.C. 1014)

“provide any information or additional information, including a return or a supplementary return or any document”

- includes money, securities, and whether computerized or not, books, records, letters, telegrams, vouchers, invoices, accounts and statements.
- in response to Court rulings prohibiting “fishing expeditions” s. 231.2(2) and (3) were enacted. These subsections allowed in certain limited circumstances, for the Minister to apply for Judicial authorization to impose upon any person the requirement to provide information or document(s) relating to one or more unnamed persons. Before being granted authorization, the Minister had to prove:
 - a) the person or group is ascertainable
 - b) the requirement is made to verify compliance with any duty or obligation under the Act
 - c) it is reasonable to expect based on any grounds, information or past experience that the person or group or any person of the group may have or may be likely to fail to comply with a duty or requirement under the Act
 - d) the information or document is not otherwise more available

- In June of 1996, c) and d) above were repealed. To extend the metaphor, Revenue Canada can now use drift nets. One would expect a significant Charter challenge to the provisions as they presently stand.

“notwithstanding any other law to the contrary (231.5(2))”

- to the extent that the Federal *Act* stands in paramountcy to other statutes this will be the case.

SEARCH AND SEIZURE

I.T.A. s. 231.3

Revenue Canada may, in pursuit of evidence of an offence under the *Act* apply under the *Act* or under the Criminal Code of Canada for a search warrant. The exercise of this power is not taken lightly and is often followed by assessments and prosecutions.

“A Judge may, on exparte application by the Minister, Deputy Minister, Asst. Deputy Minister or other persons listed in Part IX of the Regulations”

- the application is made to a Queen’s Bench or Federal Court Judge without notice to any other party
- the application must be supported by information on oath establishing the facts upon which the application is based
- the judge must be satisfied there are reasonable grounds to believe
 - an offence has been committed
 - evidence of the commission of the offence is likely to be found
 - the building, place or receptacle is likely to contain such evidence

“issue a warrant in writing authorizing any person named therein”

- the person(s) authorized must be named in the warrant but may addressed as a group (ie. a police force)

“to enter and search any building, receptacle or place for any document or thing that may afford evidence as to the commission of an offence under this *Act*”

- the warrant must specify the places that are to be searched and the evidence sought

- no person can be searched. However, once arrested a person may, for security reasons, be searched and the results of that search may be used against the person.
- the issuance of the warrant does not confer an obligation on the occupants to answer questions. Refusal does not constitute obstruction.
- in third party premises there can be no examination of files that have no relation to charges set out in the warrant.
- execution of the warrant by “night” is invalid unless authorized on the face of the warrant
- where the warrant specifies a time period, the entry, search and seizure activities must be concluded during that period.
- the occupant of premises is entitled to resist or eject the officer engaged in a search which is “unauthorized” having regard to the validity of the warrant, method of entry, time of entry, and propriety of the seizures.

“and seize the document or thing, and any other document or thing the person believes on reasonable grounds affords evidence of the commission of an offence under this Act”

- unlawfully obtained evidence is admissible under the Common Law. This rule has been altered by the Charter and the exception is that unlawfully seized evidence is inadmissible if its admission would bring the administration of justice into disrepute.

“the Judge shall, where any document or thing seized or report of it is brought before him, unless the Minister waives retention, order that it be retained by the Minister who shall take reasonable care to ensure it is preserved until the conclusion of any investigation or until it is produced for the purposes of a criminal proceeding”

- upon seizure, a report of the items seized must go to the Judge
- the Judge may, on his own motion or on the motion of an interested party order some or all property improperly seized or seized but not required for the investigation or proceeding, returned

STOPPING THE FLOW

I.T.A. s. 232

Aside of the provisions allowing for noncompliance with a “requirement” notice when a taxpayer is “unable to do so” (231.5(2)), there is little relief from compliance with the *Act*. As stated earlier, challenges to the *Act* based on the Charter have not generally met with great success. Our Courts have, however, been sympathetic to arguments based on solicitor and client privilege. A method of dealing with solicitor client privileged documents is prescribed in section 232 of the *Act*. Additionally, certain confidential communications have been held inadmissible in Court. Those include some “without prejudice” communications.

Confidentiality v. Privilege

Confidentiality arises generally as a result of a duty imposed by law or contract or convention not to disclose information or facts. A perfect example is the duty imposed upon professionals such as doctors, lawyers or accountants by their respective professional associations not to disclose, without the waiver of their clients, information obtained from or about such clients.

Not all confidential communications are privileged. Privilege involves the right of a person and the duty of some witnesses to withhold evidence, which would otherwise be relevant and admissible, from a Court of Law.

Traditionally, privilege has existed only in the context of solicitor client communications. However, the right was extended a notch by our Supreme Court of Canada in *Slavutych v. Baker* [1976] 1 S.C.R. 254. In that case the University of Alberta was unable to use confidential communications provided to it to support a charge of misconduct against the author of the communications. The Court enunciated a four part test:

1. the communication must originate in confidence;
2. the element of confidentiality must be essential to the full and satisfactory maintenance of the relationship between the parties;
3. the relationship must be one which in the opinion of the community ought to be sedulously fostered;
4. the injury that would inure to the relationship by the disclosure of the communications must be greater than the benefit thereby gained for the correct disposal of litigation.

In the twenty years since this case, the veil of privilege has not been broadened significantly.

Another type of confidential communication which has received Court protection from disclosure is “without prejudice” communication. In Tax Court, the communications protected are the letters and communications exchanged by taxpayers or their representatives and Revenue Canada in furtherance of a settlement or expressing a view of the writer on the matters in dispute. The existence of the words “without prejudice” on the correspondence is of little relevance except as evidence of an intention. The admissibility of the correspondence is dependent upon the intentions of the parties, the existence of a dispute and the contents of the communication. Without prejudice communications may be admissible, notwithstanding the intentions of the author, if the factual context under which the communication is made does not fit the rule, if the offer made in the communication is accepted, if the communication contains veiled threats or if the communication is prejudicial by its very nature.

Solicitor Client Privilege

“Where legal advice of any kind is sought from a professional legal adviser in his capacity as such, the communications relating to that purpose, made in confidence by the client, are at his instance permanently protected from disclosure by himself or by the legal adviser, except the protection be waived”

“The privilege protecting from disclosure communications between solicitor and client is a fundamental right -- as fundamental as the client to counsel itself since the right can exist only imperfectly without the privilege. The Courts should be astute to protect both”
(Descoteaux v. Mierzwinski (1982), 141 D.L.R. (3d) 590 S.C.C.)

Privilege belongs to the client. It can be claimed at the lawyer’s office, the client’s premises or in certain circumstances at the office of a third party such as an accountant. The communications must be made in confidence and for the purposes of obtaining legal advice. Earlier jurisprudence treated communications for advice differently from legal documents prepared in contemplation of litigation however such distinctions are no longer made.

All solicitor client communications, oral and written, regardless of originator, and whether or not litigation is contemplated are privileged.

However, privilege can be lost. Communications seen or heard by a third party are no longer in confidence and thus no longer privileged. Although only the client may waive the privilege, the waiver can be express or implied. If a person such as a tax adviser authorized to act on behalf of a client discloses privileged information to Revenue Canada in the course of a voluntary disclosure, during negotiations with Appeals Division, or in the audit process privilege will be waived.

Accountants Privilege

“It is not at all strange that solicitor-client communications are privileged insofar as compellable evidence before the Courts concerned while those between an accountant and client are not. The purpose of the solicitor-client privilege is to ensure free and uninhibited communications between a solicitor and his client so that the rendering of effective legal assistance can be given. This privilege preserves the basic right of individuals to prosecute actions and to prepare defences ... I do not think there is an overriding policy consideration of this nature in the case of an accountant-client communication. An accountant may, as a matter of professional ethics, be required to keep communications and other information concerning his or her client confidential. But this is not founded upon the need to ensure an effective system of the administration of justice” (Baron v. The Queen 91 D.T.C. 5055 (F.C.A.))

It is possible, however, to “create” privilege in the accountant client relationship. Where an accountant is used as a representative or one of a group of representatives for the purpose of placing a factual situation or problem before a lawyer to obtain legal advice or legal assistance, the accountant is in fact the agent of the client and any such communications are privileged. (Susan Hosiery Ltd. v. The Queen 69 D.T.C. 5278(Exch. Ct.); Cineplex Odeon Corporation v. A.G. of Canada 94 D.T.C. 6401(Ont. Gen. Div.))

A warning was issued in the *Cineplex* case, however, that the client’s clear and unambiguous intention of non waiver should be reflected in writing. It seems equally prudent that the agency relationship be established in writing.

Scrupulous care must be taken not to publish or allow agency communications to be seen by outside parties.

- Privileged communications should be kept separate from non privileged, preferably in a separate marked file to which access should be restricted.
- Avoid photocopying of privileged documents. Avoid mixing privileged and non privileged matters within a document.
- Clearly address correspondence as “Privileged and Confidential”.
- Consider retaining sensitive materials with the client’s lawyer.

The maintenance of the agency relationship and concurrent privileged status of communications obviously comes with a cost. The client and tax advisors must consider whether the matters at hand warrant the extra effort.

Claiming Privilege

Solicitors may avail themselves of s. 232(3) to claim privilege. When the officer is about to seize a claimed privileged document he must seize it without looking at it and place it

with any other documents for which privilege is claimed in a package to be sealed, marked and delivered to the Sheriff of the local Judicial District. The client or lawyer must then commence an application within the following 11 days to a Judge to have the Judge determine the character - privileged or not - of the document(s).

KNOCK KNOCK

As the accountant or tax advisor of the taxpayer, what do you do when Revenue Canada shows up at your door?

- Appoint one person to deal with the Revenue Canada Official and funnel all communications through that individual
- Determine the nature and reasons for the visit, call or investigation
- Unless it is for a Seizure or Requirement to Provide Documents or Information, determine if the time is “reasonable”. If not, set a more reasonable time.
- Obtain the names of all Revenue Canada Officials and require them to produce their authorization cards. If possible, photocopy them(the cards).
- Have a second person present.
- Keep careful and detailed notes of all conversations.
- Contact the client.
- Consider consulting with legal counsel familiar with the investigatory powers of Revenue Canada

Routine Audit

- Ask the following questions:
 - What purpose related to the administration or enforcement of the *Act* has prompted the encounter?
 - What books, records, or documents does the Official wish to see?(Revenue Canada is entitled only to documents which relate or may relate to information that is or should be in the books or records (s.230)or which relates to any amount payable by the taxpayer)

- Consider requesting the Official provide his questions in writing and responding in kind.
- Be cognizant of deadlines imposed for responding to “30 day” letters. If more time is needed ask for it before the deadline passes.
- In your contact with the client inform him of your statutory duty to give “reasonable assistance” and answer all “proper questions”
- Be cognizant of the need to provide information which is accurate, not privileged and which will not impair future representation at the Objection or Appeal stages.

Requirement to Provide Documents or Information

- Ask the following questions:
 - What is the purpose related to the administration and enforcement of the *Act* which has prompted the service of the Requirement Notice?
 - What is the name of the person about whom the information is sought?
 - What are the reasons the information or documents are being sought?
- If the persons are unnamed ask for the Judicial Authorization.
- Notify the taxpayer and advise him to notify his lawyer.
- Consider notifying legal counsel in respect of these and privilege issues.
- Be cognizant that you have reasonable time to respond.

Search Warrants

- Contact legal counsel who should attend the search locations (Under s. 232 the lawyer can assert the privilege claim)
- Review the warrant and copy. Check it to verify that it is correct on its face and to determine any limitations to the authority granted.
- Request a copy of the affidavit supporting the warrant (the officials need not have it with them at the time of search and seizure)

- Determine who is the object of the investigation
- If the search is with respect to a client, contact the client immediately to advise of the search and to obtain instructions whether or not to cooperate.
- Unless authorized by the client to cooperate, neither obstruct nor assist the investigation (within reason).
- Ensure that at least two persons are present at all times
- Keep very detailed notes including times of all conversations and lists of all documents seized as well as the names of all investigating officers.

CONCLUSION

Public policy dictates that the powers of Revenue Canada are sufficiently broad so as to enable the enforcement of the *Act*. Revenue Canada refers to taxpayers as their 'clients' and advises that although it prefers to work in harmony with those 'clients' it is prepared to utilize its powers when needed. Our role as professionals is simply to ensure the powers are applied fairly and properly to those clients. We must at all times be courteous and respectful of our colleagues at Revenue Canada for theirs is an unsavoury business, but at all times mindful of our obligations to the law, our clients, and our professions.

Donald P. Mallon
PROWSE & CHOWNE

Case Study

The Queen v. Tex E. Vador Ltd.

Tex (Darth's brother) has embarked on a risky tax planning exercise which, if successful, will result in the payment of no tax on his very significant income. His lawyers, Suitt & Runn, have rendered him a written opinion the contents of which, if known, will expose the significant weaknesses of his tax plan. The opinion was required by his accountants in order to prepare his returns. Revenue Canada has used its seizure powers pursuant to section 231.3 of the Income Tax Act to seize the opinion in the hands of the accountants and Ron Runn has made application to have the opinion declared a privileged document.

Will he be successful?

Consider the effect of the accountants communicating the contents of the opinion to the Corporation's auditors.

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A Review of Dealings with Revenue Canada

Prepared by
Donald P. Mallon

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