



## **IVI Audits - SME**

### **Situation**

I have just heard that as of this summer CRA has a new term for SME (small to medium enterprises) audits. The term is 'IVI', which means Independent Verification of Income.

What exactly is an 'IVI' audit? How should I be recommending my clients prepare for an 'IVI' audit? What can I, as the accountant, do to minimize my risk?

### **Response**

The Auditor General, Sheila Fraser, considers the Small and Medium Enterprises (SME) tax base to be very 'high risk' and suggested increases in compliance enforcement. View her recommendations at <http://www.oag-bvg.gc.ca/domino/reports.nsf/html/20040305ce.html>.

CRA is apparently taking these recommendations seriously. New audit procedures for independent verification of income could include:

- ratio analysis
- audit of key input costs
- quantity as compared to sales
- examination of all personal bank and credit card accounts for all family members
- net worth assessment
- household budgets with comparison to Statistics Canada

### **Recommendations:**

Business owners should keep a file with each personal bank, investment, RRSP and credit card statement for all family members with their business records for each year.

### **Why?**

CRA will request these records and it is very expensive to request these records on demand.

Business owners should also document all deposits and transfer for all bank, investment and credit card accounts as well.

### **Why?**

It has been my experience that clients/taxpayers frequently remove cash from one bank to deposit to another bank across the street, rather than employing a traceable means of transfer like a cheque or electronic funds transfer.

It's really easy for an auditor to chalk up that cash deposit as more income rather than transfers, gifts or repayment of loans.

A business owner should have a financial file for all assets, liabilities, investments, debts and a budget. There are three reasons for doing this:

1. CRA will require it during an audit;
  2. It shows that you care about your business success by measuring and monitoring these items;
  3. It minimizes your risk and generates an effective audit trail for CRA.
  4. Ensuring the foregoing procedures will decrease the residual effect of an IVI Audit on the client.
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### **Did you know?**

- Federal personal income tax revenue in 2003: **\$90 billion**  
Percentage of that amount accounted for by the self-employed: **almost 10%**
- Federal corporate tax revenue in 2003: **\$22 billion**  
Percentage of that amount accounted for by corporations with annual gross revenues of less than \$15 million: **36.5%**
- Net GST/HST revenue (other than that collected by Customs on imported goods) in 2003: **\$14 billion**

Percentage of that amount attributable to small and medium enterprises: **over 60%**

The underground economy results in tax evasion and represents an estimated annual loss of federal and provincial tax revenues of \$12 billion. Promoting compliance with tax legislation in such a large and diversified group of taxpayers is a challenge for CRA.