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Eight things that can trigger a tax audit by CRA

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If you're self-employed, your tax filing deadline is just around the corner on June 15 (unless you have a balance owing from 2015, in which case you missed your deadline of April 30—uh oh!).

You're busy enough at this time of year, so the last thing you need is the Canada Revenue Agency (CRA) wrapping you up in its auditing tentacles.

Thankfully, you may be able to avoid an audit entirely if you play it safe and smart.

In this blog, tax expert David J. Rotfleisch shows you a few areas that are likely to raise a red flag with the CRA.

(https://mystartupcanada.files.wordpress.com/2016/05/auditor.png)"Help! I'm being audited," are dreaded words uttered by Canadians. They are especially dreaded by business owners because an audit means extra work and extra accounting costs.

Have you ever wondered what triggers a tax audit by the CRA in the first place?

Once an income tax return has been filed, it is subject to both computer and human review. Some tax returns will be audited on a random basis, but most audits are caused by what is in the tax return: the information you supplied and the way you supplied it.

Here is a list of eight "red flags" that are likely to trigger an audit by the CRA.

1. **Claim unreasonable expenses**
   The best way to ensure an audit is to be greedy with expenses claimed. The amount of any category of expense has to be reasonable, both compared to revenues and compared to other similar businesses. Claiming $10,000 in car expenses against $50,000 in sales will likely trigger an audit. Don't claim such a high percentage unless you supply a mileage log and you're willing to be audited.Another basic CRA review technique is to compare expenses claimed to the amount deducted in previous years. Any discrepancy will be flagged for audit. So, if travel expenses increased from $3,000 to $12,000, expect questions and very possibly an audit.
2. **Use all "rounded-off" numbers in your tax return**
   The CRA likes to see exact amounts in both the dollars and cents columns. Rounded-off numbers (for example, $2,500 or $10,000) signal to the CRA that you have likely not been keeping accurate records and are estimating everything at the end of the year. It also tells CRA that you are not likely to have receipts. Put in exact amounts, such as $2,486.32 and $9,742.56, and you are less likely to trigger an audit.
3. **Forget to include a T-slip**
   It's easy to forget a T-slip, but the CRA has a matching program that will pick up any missing slips and will charge you a 10% penalty for the first time, rising to 20% for subsequent occurrences. And you will increase your audit risk: was it inadvertent, or are you not reporting all of your income?A tax return preparation tip: compare everything on this year's tax return to last year's T1, to ensure that you haven't missed anything.
4. **Certain sectors are on the CRA's watchlist**
   Restaurants, construction, and small retail outlets have been identified as part of the "cash economy" and stand a good chance of being audited.
5. **Being self-employed or an independent contractor**
   If you own a business or are an independent contractor, you increase the chance that CRA will audit, either to make sure you are declaring all of your income, or that you are, in fact, an independent contractor and not an employee looking for more tax breaks.
6. **Over-paying salaries to spouse and children**
   Paying spousal or child salaries is proper for services rendered and if the amount charged is market rate. But expect a CRA audit to check for services not rendered, overpaying for services that were provided, and not documenting amounts paid. This is an especially tricky area because the audit reassessment will deny the expense (or part of it) for the taxpayer, but it remains taxable to the recipient resulting in double taxation.
7. **Reporting business losses for years and years**
   Small business owners can expect the CRA to come knocking if they report losses for several consecutive years in a row — why would anyone continue to operate an unprofitable business?
8. **Big discrepancies in income for your industry, neighbourhood**
   The CRA compares what you report on your income tax return to the statistics for your industry, your profession, and your neighbourhood.For example, if you're declaring

$50,000 a year in income and you live in a neighborhood where the average reported is $130,000, that is a noticeable difference. CRA is going to audit to see how you can continue living beyond your means.

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