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Law Reform Commission
of Canada

Commission de réforme du droit
du Canada

search and seizure under the *Income Tax Act*

CRIMINAL LAW SERIES

SUMMARY OF STUDY PAPER

Canada

SEARCH AND SEIZURE
UNDER
THE *INCOME TAX ACT*

Criminal Law Series

Summary

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Summary of a Study Paper
prepared for the

Law Reform Commission of Canada

by

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I.

Introduction

A. Revenue Enforcement Legislation: The Problem Identified

The principle of voluntary self-compliance lies at the heart of the administration of the federal income tax system. A self-compliance system of collecting tax is both more efficient and less intrusive than other methods. However, its efficacy depends upon two important factors: on the one hand, the ability of the revenue agency to investigate the accuracy of filed information; and, on the other hand, the willingness of the great majority of taxpayers to support the system by accurately reporting their income. These factors are related. The public's willingness to adhere to the principles of voluntary self-assessment and compliance depends, in part, not only upon its perception of whether Revenue Canada's enforcement powers are sufficient to ensure that it can obtain the information it needs to administer effectively the *Income Tax Act* (S.C. 1970-71-72, c. 63, as amended), but also upon its perception of whether the powers are necessary and are fairly administered.

In this first section of the Introduction we suggest that much of the current concern over Revenue Canada's enforcement practices and the resulting public cynicism about the tax system can be traced to the legal framework underlying Revenue Canada's enforcement powers, in particular, its broad powers of search and seizure. Consequently, restructuring these enforcement powers to provide taxpayers with greater procedural due process should not impair Revenue Canada's ability to police our self-assessment system, but ultimately should enhance it.

This perception, that generally Revenue Canada agents' powers of search are too broad, has been shared by many law reform organizations. The various recent reports and legislative enactments that have addressed the issue are reviewed in the Paper. Solutions that provide greater protection to the privacy interests of taxpayers, but at the same time provide for effective monitoring and enforcement of revenue-raising legislation have been sought in all these reform efforts.

B. Purpose of Study Paper

The Paper is related to the Law Reform Commission's work on police powers and in particular the police's powers of search and seizure. For a number of reasons, an

evaluation of the search powers outside the *Criminal Code* is a necessary part of the comprehensive study of police powers of search and seizure in criminal law enforcement. First, if the search powers contained in these other statutes are considerably broader than those contained in the *Criminal Code* (R.S.C. 1970, c. C-34, as amended), they might be used to defeat the safeguards surrounding the powers of search in the *Criminal Code*. Thus, law enforcement officials might be encouraged, for example, to use the search powers in the *Income Tax Act* to conduct a criminal search of a suspected drug dealer. Second, in the course of the Commission's comprehensive review of the substantive offences of the *Criminal Code*, offences might be transferred into or out of the *Code*. It is conceivable, for example, that tax evasion, at present an offence contrary to the *Income Tax Act*, will emerge from the fundamental review of the criminal law as a variety of fraud and hence as an offence contrary to the *Criminal Code*. If different enforcement requirements are needed for these offences, now found in several federal statutes, the criteria for distinguishing them from offences now in the *Criminal Code* will have to be clearly articulated. The powers the state has for investigating particular offences should not turn on the happenstance of what federal statute the offence is found in. Finally, the proliferation of legislative regimes of search and seizure renders the aggregate of such powers uncertain and indeed unknowable. Thus, the broad objectives sought by the Commission in consolidating, rationalizing and reforming the various search and seizure regimes within the common law, the *Criminal Code* and crime-related statutes will only be partially achieved unless the search powers in other federal statutes are similarly consolidated, rationalized and reformed.

Although the Paper only evaluates in detail the search power contained in the *Income Tax Act*, it develops a framework for the analysis of the nature, scope and extent of all search powers outside the traditional criminal law context.

A review of the general principles of privacy and intrusions reveals that search powers can, in principle, be divided broadly into two types: investigatory, and inspection search powers. Investigatory searches are those searches conducted as a result of a belief that there has been a specific contravention of the law. The person conducting the search is looking for evidence of the offence. A search of a dwelling-place for suspected drugs by police officers is a paradigm of an investigatory search. Inspection searches are searches that are conducted on a routine basis to ensure continual compliance with the law. A routine audit of a taxpayer's books and records by officials of Revenue Canada is an example of an inspection search.

The *Income Tax Act* confers both of these kinds of search powers on Revenue Canada officials. In particular, in section 231 it provides them with the power to:

- (a) obtain a search warrant and conduct a search for a suspected violation of the *Act*;
- (b) enter any premises to examine books, records or property described as inventory; and,
- (c) require any person to provide information or to produce books and records.

The first type of search power is an example of an investigatory search power and is examined in Part II of the Paper. We conclude that there is no justification for the state to have broader powers of search when it is investigating tax evasion or other violations of the *Income Tax Act* than when it is investigating a criminal offence. The other two types of search powers mentioned above are examples of inspection search powers and are discussed in Part III of the Paper, in sections “B” and “C” respectively. Our fundamental conclusion in this part of the Paper is that the state should not have the right to enter premises to inspect books and records: in the absence of the taxpayer’s consent, the state’s only remedy should be to demand that those books and records be produced for inspection. However, in addition to this basic proposal, numerous proposals are made as to how both the present powers to enter premises to inspect books and records (or only property, if our basic recommendation is adopted) and to call for the production of books and records should be reformed.

In addition to these two search powers, there are two related powers in the *Income Tax Act*. First, Revenue Canada officials are given the power to seize property in the course of a search if it appears to them that the property may be required as evidence of a violation. Second, they are given the power to require persons to answer questions during the course of an inspection. These powers are examined in sections “D” and “E” of Part III.

C. General Principles of Privacy and Intrusions

In this section of Part I, the concept of privacy, the nature of the state’s need for information and the interests underlying the traditional notions of procedural due process are briefly reviewed. The point of this review is to establish a theoretical basis for distinguishing between investigatory and inspection searches, and for the various safeguards that we recommend should surround inspection searches.

II.

Investigatory Search Powers in the *Income Tax Act*

A. Introduction

(1) Outline

This Part of the Paper compares the investigatory search powers contained in the *Income Tax Act* with those in the *Criminal Code*. The purpose of the comparison is to determine whether there is any justification for the powers to differ. That is to say, to determine whether there is anything unique about suspected violations of the *Income Tax Act* that justifies the state having broader powers when investigating such suspected violations than it has when it is investigating suspected violations of the *Criminal Code*. Our conclusion is that there is not, and that only the investigatory search powers contained in the *Criminal Code* should be used when suspected violations of the *Income Tax Act* are being investigated.

(2) Other Investigatory Search Powers outside Criminal Law Enforcement

The *Income Tax Act* is not the only federal statute outside the *Criminal Code* that contains investigatory search powers. It has been estimated that approximately twenty-three federal statutes authorize investigative searches in order to assist law enforcement officials to investigate suspected violations of their governing statutes. To place the comparison of the *Income Tax Act* investigatory search powers with those in the *Criminal Code* in a broader context, we briefly review the other federal statutes that contain such search powers. Ultimately, it may be decided that the investigatory search powers in the *Criminal Code* should apply to violations of all federal statutes — that there should be no investigatory search powers outside those contained in the *Code*. Although the Paper does not address this larger issue directly, by examining in detail the search powers in the *Income Tax Act* it does provide a framework for the analysis of the nature, scope and extent of all investigatory search powers outside the traditional criminal law context.

Furthermore, our conclusion that there is no justification for broader search powers in the *Income Tax Act*, suggests that there is likely no justification for investigatory search powers that are broader than those in the *Criminal Code* in any federal statute.

(3) Investigatory Search Powers in the Income Tax Acts of Australia, the United States, and the United Kingdom

The Australian, American and British laws are reviewed in the Paper. In Australia and the United States, only the general criminal search powers are available for investigating income tax violations. This would appear to confirm our conclusion that there is nothing unique about tax violations that justifies search powers that are broader than those available for investigating ordinary criminal offences. In the United Kingdom, on the other hand, there is a separate regime for searches undertaken to obtain evidence of suspected income tax violations. However, this regime has only recently been introduced and has been the subject of criticism.

B. Detailed Comparison of the Investigatory Search Powers in the *Income Tax Act* and the *Criminal Code*

The Paper compares in detail the search powers in the *Income Tax Act* and the *Criminal Code*. Some of the points of comparison are trivial. Other differences arise only because of a difference in wording between the legislative description of the two search powers: the interpretation of, or the practice under, the two provisions may not differ. On only three points of comparison is the difference between the provisions substantial. However, in spite of this, we have compared the provisions on all possible grounds. To support our recommendation that there is no justification for a distinct investigatory search power in the investigation of income tax violations we wanted to be sure that there was no subtle, but important, differences reflected in the particular language used in the income tax provision. The following is a summary of the questions we asked in comparing the provisions. Our basic conclusion with respect to each question was that the differences could not be justified.

(1) For the Violation of What Types of Offences Can a Search Warrant Be Obtained?

Under the *Income Tax Act* an investigatory search warrant can be obtained to assist in the investigation of any suspected violation of the Act or regulations, no matter how trivial. We recommend that it should be available for investigating only serious violations.

(2) Must There Be Evidence That an Offence Has Been Committed before a Search Will Be Authorized, or Can a Search Be Authorized if There Is Evidence That an Offence Is Likely to Be Committed?

At present, under subsection 231(4) of the *Income Tax Act*, an authorization to search can be obtained where an offence "has been committed or is likely to be committed" There is no justification for this preventive search power.

(3) Who May Authorize the Application for a Search Warrant?

Certain designated Revenue Canada officials can apply for a search warrant under the *Income Tax Act*. Although administrative personnel should be allowed to apply for a search warrant, and of course a person with personal knowledge must swear to the facts supporting the application, the official who is empowered to apply for the warrant should be of a sufficiently senior level to ensure uniformity of practice and departmental accountability. At present, this objective appears to be achieved by the regulations promulgated under the *Income Tax Act*.

(4) What Degree of Particularity Is Required with Respect to the Alleged Offence, the Items Sought and the Places to Be Searched?

The standard of particularity is one of the most fundamental protections limiting the scope of criminal investigatory search powers. The *Income Tax Act* does not require the warrant to contain details of either the alleged offence or the evidence to be searched

for. After reviewing the arguments, we conclude that there is no reason why warrants issued in searches for evidence relating to an alleged violation of the *Income Tax Act* should not be as specific on these matters as are warrants issued in searches for evidence relating to an alleged violation of the *Criminal Code*.

(5) What May Be Seized in the Course of a Search?

Under the *Criminal Code*, generally, only evidence relating to a specified crime may be seized. Under the *Income Tax Act*, evidence relating to *any* violation may be searched for and seized. Again, we conclude that there is no justification for giving investigators under the *Income Tax Act* broader powers in this regard than investigators under the *Criminal Code*.

(6) What Procedures Are to Be Followed in Applying for a Search Warrant?

Under both the *Criminal Code* and the *Income Tax Act* the application to obtain a search warrant must be made under oath, and may be presented at an *ex parte* hearing.

(7) Who May Issue a Search Warrant?

Here, the *Income Tax Act* is stricter than the *Criminal Code*. Under the former Act, a search warrant must be approved by a superior or county court judge; under the latter, a justice of the peace may issue a warrant.

(8) Must the Issuer Have Reasonable Grounds for Believing That an Item to Be Searched for Is Related to an Alleged Offence, and Is to Be Found in a Specified Place before Issuing a Search Warrant?

The purpose of having an independent arbitrator to issue the warrant is to ensure that the grounds justifying the search have been impartially determined. Under *Criminal Code* subsection 443(1), before a search warrant is issued, a justice must be satisfied that "there is reasonable ground to believe" that the items sought are linked to the alleged offence and will be found in the locations to be searched. Subsection 231(4) of the *Income*

Tax Act provides only that before a warrant is issued “the Minister [must have] reasonable and probable grounds to believe” that a tax violation has been committed. The courts have construed this wording to mean that the justice authorizing the warrant must have reasonable grounds for believing there has been a violation. However, there is no requirement that the justice have reasonable grounds for linking the items to be searched for with the alleged violation or the places to be searched. Following from our conclusion that a search warrant issued for evidence of an income tax violation should be specific with respect to those matters, the standard of reasonable belief should also apply to their linkage.

(9) What Procedures Must Be Followed in Executing the Warrant?

Although the *Income Tax Act* is largely silent on these matters, there is no reason why investigating officers conducting a search for evidence of a suspected tax violation should not be required to: display the warrant to the persons whose premises are being searched; execute the warrant, except in extraordinary circumstances, by day; execute the warrant within a specified period of time after its issuance; and, only be allowed to use a reasonable degree of force in executing the warrant. An issue unique to searches outside the *Criminal Code* is whether the investigative officers of the relevant administrative agency, such as Revenue Canada, should be required to be accompanied by police officers when executing a search warrant. For a number of reasons reviewed in the Paper we conclude that they should have to be so accompanied.

(10) What Procedures Are Provided for Obtaining Access to Items Seized in the Course of a Search?

Who may authorize access? Who may obtain access? What conditions may be imposed for obtaining access? Both the *Criminal Code* and the *Income Tax Act* provide procedures for obtaining access to seized items. However, the procedures differ in some details. We conclude that there is no justification for these differences. The Commission has recently recommended some changes in the procedures relating to access of things seized in the *Criminal Code* in its Working Paper 39 on *Post-Seizure Procedures* (Ottawa: Supply and Services, 1985). Very briefly, the Commission recommends that access should normally be obtained by consent, but that a hearing before a justice should be available to a person who claims an interest in the things seized in cases where access is denied. All persons with an interest in the things seized should be entitled to examine them and photocopy them at their own expense.

(11) What Procedures Are Provided for Disposing of Items Seized in the Course of the Execution of the Search Warrant?

Must a court order be obtained to allow officials to retain custody of the items seized? For what period of time is such an order valid? Can the party whose items are seized challenge the validity of the custody order and, if successful, obtain restoration of the items? If the items seized are documents that the party needs in the conduct of his or her business or to prepare his or her defence to a criminal action, who must bear the cost of copying them? The *Criminal Code* contains a comprehensive scheme for processing items seized pursuant to a search. The *Income Tax Act*, by contrast, makes no provision for processing items seized other than to authorize their detention until they are produced in any court proceedings. There is no reason why the *Criminal Code* procedures for disposing of seized goods should not apply to goods seized in relation to an income tax offence. The Commission has recently recommended some changes in the procedures for disposing of items seized in criminal cases in its Working Paper 39 on *Post-Seizure Procedures*. Briefly, the Commission recommends that inventories of things seized should be prepared in all cases by the officers effecting seizure (Recommendation 2(3)). A copy of the inventory should be given to interested parties. The officers should also, as soon as practicable, be required to present the inventory (along with the endorsed search warrant or a post-seizure report) to a justice (Recommendation 2(4)). The justice would issue a "custody order" in relation to the things seized. Where no criminal proceedings have been instituted, the custody order should terminate within three months (Recommendation 5(1)). The Commission also recommends that a person from whom things have been seized should have the right to apply to a judge to have the things restored to him or her (Recommendation 7). Among other grounds for ordering that things be restored, the judge is to have regard to "any alternatives to detaining the things for use as evidence (Recommendation 9(1)(b))." The Commission goes on to recommend that where an order for restoration of things seized is made, the judge should be empowered to order further that an accurate record be made of the things seized and that such record be admissible at trial in place of the original (Recommendation 11(a)). The Commission's recommendations contained in its recently released Report 22 entitled *Disclosure by the Prosecution* (Ottawa: Supply and Services, 1984) would entitle the taxpayer, once charged, to request and receive photocopies of exhibits where it is practical and to receive, without charge, copies of various classes of enumerated documents relevant to the case against him or her.

(12) What Procedures Are Provided for Reviewing the Search Warrant and the Manner in Which the Search Was Executed?

Although not specifically provided for in the *Criminal Code*, the method for obtaining such a review is certain and well known under the *Code*. By contrast, the procedure for obtaining review, the forum for lodging an application for review, and the type of relief available are uncertain for a search authorized under the *Income Tax Act*. The review procedures ought to be the same.

III.

Inspection Searches

A. Introduction

(1) Outline

The *Income Tax Act* contains two broad types of inspection powers. First, under paragraphs 231(1)(a) and (b), Revenue Canada officials are given the power to enter premises to audit books and records and to examine certain property. Second, under subsection 231(3) Revenue Canada officials are given the power to call for the production of books and records. The significant difference between these search powers is, of course, that under the first power Revenue Canada officials have the power to enter premises, while under the second they do not.

Our basic conclusion is that Revenue Canada should have the right to enter premises only for the purpose of inspecting property. If taxpayers refuse to allow Revenue Canada officials to inspect their books and records at their premises, Revenue Canada's only recourse should be to call for the production of such books and records.

Following the justification for this basic conclusion, we examine in detail both Revenue Canada's present power to call for the production of books and records and its power to enter premises to inspect books, records and property. To assist in evaluating these inspection powers, a number of issues are identified which must be addressed in determining whether the present powers meet the procedural requirements necessary to ensure that the appropriate balance is struck between the state's need for information to ensure compliance with income tax legislation and the individual's right to privacy. Under each of these issues the existing provision and the relevant case-law and revenue practice are discussed, the details of the United Kingdom and United States law are compared, the policy considerations are examined, the shortcomings of the Canadian law are identified, and proposals for amendments, where necessary, are made.

Section "B" of this Part examines the power to require the production of books and records; section "C" examines the power to enter premises and inspect books, records and property. Sections "D" and "E" examine two related powers that the *Income Tax*

Act provides Revenue Canada officials: the power to seize property in the course of a search if it appears that the property may be required as evidence of a violation; and, the power to require persons to answer questions during the course of an inspection.

(2) General Principles

Inspection searches are those conducted on a routine basis to ensure continual compliance with the law. They are contained in many federal statutes. In the main, this Paper examines only the inspection search powers contained in the *Income Tax Act*.

The evaluative issues addressed in this Part are whether these inspection powers are necessary to ensure compliance with income tax legislation, and if so, whether their present form provides sufficient procedural safeguards to protect the privacy interests of individuals.

Different rules are required for regulating inspection searches than for regulating investigative searches because of the differences in the nature of the intrusion, the extent of the intrusion, and the social need for the intrusion. These general principles are reviewed in this section of the Introduction.

(3) Types of Inspection Searches: Requiring Books and Records to Be Produced and Entering Premises to Inspect

The *Income Tax Act* contains two broad types of inspection powers: paragraphs 231(1)(a) and (b) gives Revenue Canada officials the power to enter premises to audit books and records and to examine certain property; subsection 231(3) gives Revenue Canada officials the power to call for the production of books and records. This section of the Paper addresses the question of whether Revenue Canada should be given both these powers.

(4) Income Tax Inspection Powers in the United States, the United Kingdom and Australia

The inspection powers in the Income Tax Acts of each of these countries are briefly reviewed.

B. The Power to Call for the Production of Books and Records

Subsection 231(3) of the *Income Tax Act* authorizes the Minister to require any person to supply information or to produce any documents or records. The Minister may exercise this power for any purpose related to the administration or enforcement of the Act. The following issues are discussed in evaluating this power.

(1) What Officials Should Be Authorized to Require the Production of Books and Records?

There are two competing interests in determining who should exercise these powers. On the one hand, the required level of authority should be sufficiently low so that the power can be exercised conveniently and so that the decisions of lower-level officials are not simply rubber-stamped by the authorizing official. On the other hand, the level of authority required to exercise these powers should be sufficiently high so as to ensure safeguards which result in departmental accountability, and to ensure a degree of uniformity in practice. We conclude that the present law, under which fairly senior officials are specifically identified by regulation, appears satisfactory. We do recommend, however, that normally where the demand for inspection is not being made to the taxpayer personally but to a third party who has possession of the taxpayer's documents, and no taxpayer is identified, a more senior official be required to authorize the demand than the level of official who may authorize a demand made to the taxpayer personally. In the case of third-party demands, the potential for abuse is greater since there is no individual taxpayer directly involved who has firsthand knowledge of, and a personal interest in, Revenue Canada's inquiries.

(2) Should Books and Records in the Possession of Third Parties Be Liable to Be Summoned?

Revenue Canada should continue to be able to summon third parties who have information relating to the tax liability of a taxpayer who is under inspection. Indeed, the class of third parties who can be subject to such a demand should be slightly broadened. However, the present procedures for obtaining information or documents from third parties do not sufficiently protect the privacy interest of the taxpayer. Thus, additional safeguards regarding the issuance of demands to third parties should be enacted. These safeguards are discussed below.

(3) **Where a Third-Party Summons Is Issued, Should Taxpayers Be Informed That Information Relating to Their Tax Liability Has Been Requested?**

Under the present law there is no requirement that the taxpayer be informed when his or her documents are being demanded from a third party. We recommend a fairly elaborate procedure for informing the taxpayer that his or her documents are being demanded in such circumstances and for allowing him or her to contest the demand. We also recommend that prior judicial approval be obtained for the issuance of a third-party summons if the taxpayer cannot be identified.

(4) **Should the Requirement of Production Be Restricted to Books and Records Relating to an Investigation of the Tax Liability of a Specified Person?**

Subsection 231(3) of the Act provides that production or testimony can be required "for any purposes related to the administration or enforcement of this Act." However, in spite of this broad wording, the Supreme Court of Canada has recently held in *James Richardson & Sons Limited v. The Minister of National Revenue* ([1984] 1 S.C.R. 614), that the production of documents can only be required for the purpose of investigating the tax liability of a specified person. In that case, Revenue Canada had called for the production of all the records of a particular brokerage house relating to its clients who traded in the commodities futures market. We conclude that instead of prohibiting Revenue Canada from demanding the production of documents in these circumstances, a more satisfactory way of balancing the conflicting interests would be to require Revenue Canada to obtain prior judicial authorization before it could call for the production of documents where no individual taxpayer was identified or being investigated.

(5) **Should the Books or Records That Can Be Required in a Summons Exclude Some Classes of Documents, Such As Documents Protected by the Solicitor-Client Privilege, or the Tax Working Papers of Auditors?**

We recommend that the procedures in the *Income Tax Act* for claiming solicitor-client privilege be broadened so that they embrace all documents that are protected by the solicitor-client privilege under the common law. We also recommend that no privilege be recognized for tax working papers of accountants.

(6) What Information Should a Summons to Require Books and Records to Be Produced Contain?

Should the authority under which, and the purpose for which, the summons is issued be identified; should the summons contain a description of the mechanism for challenging compliance; and, with what degree of specificity should the taxpayer to whom the information requested relate, and the documents required to be produced, be identified? At present there is virtually no requirement that the taxpayer be notified of the details relating to the demand for production. We suggest that taxpayers be fully apprised of all matters that might be necessary in order to inform them of the scope of the inspection and to enable them to make an informed decision as to whether or not to comply with the summons.

(7) By What Method Should the Summons Be Served?

We recommend a number of safeguards to ensure that the taxpayer or a third party has been fairly served with the summons.

(8) How Much Time Should the Summoned Party Be Given to Comply with the Demand for Production?

Under the present law, Revenue Canada may demand the production of documents almost immediately. We recommend that the summoned party be given a specified minimum number of days for complying with a summons.

(9) Where Should the Books and Records Be Required to Be Produced?

Under the present law, there is some confusion as to where Revenue Canada may demand that a party deliver documents. We recommend that Revenue Canada should be allowed to demand production at any reasonable place, but not at the taxpayer's or the third party's premises unless that person consents to production at his or her premises.

- (10) What Limits, If Any, Should There Be upon the Power to Require the Production of Books and Records to Ensure That Unnecessary Burdens Are Not Imposed on Taxpayers?

At present, there are no limits on Revenue Canada's authority to require a taxpayer to produce records. We recommend that Revenue Canada's authority to audit should be restricted in a number of ways. First, it should be expressly prohibited from engaging in "unnecessary" audits. Second, only one inspection in relation to a particular taxpayer should be allowed each year. Third, a limitation should be placed on the number of past years for which Revenue Canada may demand production without court approval. Fourth, a general standard should be enacted prohibiting Revenue Canada from requiring taxpayers to compile an unreasonable amount of information.

- (11) Should Inspection Searches Be Prohibited If the Taxpayer Is under Criminal Investigation?

Under the present law, it appears that in most cases, even though a taxpayer is under criminal investigation, Revenue Canada may inspect all his or her relevant records by means of an inspection search. Obviously in these circumstances an inspection search can be used to circumvent the procedural protections inherent in the requirement that the police obtain a search warrant to search for the purpose of obtaining evidence of a crime. A statutory restriction should be imposed on the issuance or execution of an inspection summons in aid of a criminal investigation or prosecution.

- (12) Should Taxpayers or Third-Party Recordkeepers Be Reimbursed for the Cost of Complying with a Summons Requiring Them to Produce Books and Records?

The Act contains no provision for reimbursing either the taxpayer or a third party for costs incurred in complying with a summons. We recommend that, subject to certain restrictions, costs be reimbursed in two situations: where the costs of complying exceed what might reasonably be expected as a cost of doing business; and, in the case of a third-party summons.

(13) How Should the Summons Be Enforced If the Summoned Party either Fails or Refuses to Comply with the Summons?

The present method of enforcing the demand to produce is inadequate for several reasons. We recommend that if a person refuses to comply with a summons, or a taxpayer stays compliance by a third party, Revenue Canada should be required to seek enforcement through an adversary proceeding before a judge.

C. The Power to Enter Premises for the Purposes of Inspecting Property

Under paragraph 231(1)(b) of the *Income Tax Act*, any person authorized by the Minister may enter any premise to examine property which "may, in his opinion, assist him in determining the accuracy of an inventory or in ascertaining the information that is or should be in the books or records or the amount of any tax payable under this Act." The following questions are asked in evaluating this search power. If the authority to enter premises to inspect books and records is retained, these questions would be relevant, of course, in assessing that search power as well.

(1) Should the Power to Enter Be Restricted to Any Property, Process or Matter Relating to an Investigation of the Tax Liability of a Specified Person?

The Act provides in subsection 231(1) that entry of premises to conduct an audit of property can be made "for any purpose related to the administration or enforcement of this Act" However, in spite of this broad language, the *Richardson* case has essentially limited this power to investigations of specified taxpayers. With respect to the power to require production, we recommend that the purposes for which the power could be used not be limited to an inquiry into the tax liability of a specified person because the requirement of prior judicial authorization to issue a third-party summons where no taxpayer was identified is sufficient to prevent abuse. Even though the entry of premises is a greater invasion of privacy than the requirement of producing documents, and even though only rarely would Revenue Canada need to inspect property when it would not be investigating the tax liability of a specified person, the same procedure should adequately protect the privacy interests of taxpayers.

(2) Should Revenue Canada Be Able to Inspect the Premises of Third Parties Who Have Custody of Property Relating to the Taxpayer's Tax Liability?

Since taxpayers may have property that is described in their books and records on the premises of third parties, entry into third-party premises should be authorized. This is the present law.

(3) Should There Be Any Restrictions on the Types of Premises That May Be Entered?

Under the present law, there has been some suggestion that only premises where books and records are required to be kept under the Act may be entered. For example, in *Royal American Shows Incorporated v. The Queen ex rel. Hahn* ([1975] 6 W.W.R. 571 (Alta. S.C.)) it was held that a taxpayer's records could not be inspected in a police station where they were being held in custody. We recommend that Revenue Canada be given a broad power to inspect any premises that relevant property may be found in.

(4) Should Notice of the Inspection Be Required, and If So, What Information Should the Notice Contain and Who Should Be Given Such Notice?

Under the present Act, there is no requirement for notifying the occupier of premises about to be entered that an inspection of property is about to take place. Consequently, the occupier has no opportunity to challenge the inspection, short of refusing entry and facing prosecution. We recommend that full and timely notice always be given to the person whose premises are to be entered. In addition, where the taxpayer's property in the custody of a third party is being inspected, the taxpayer should be entitled to timely notice. Although we recommend that notice to the person whose premises are to be entered should never be dispensed with, there is a case for instituting a mechanism, similar to that with respect to a third-party summons to produce documents, permitting Revenue Canada to dispense with notice to the taxpayer where there is a reasonable cause to believe that the taxpayer will destroy, alter or conceal the property to be examined if notice of the examination is given.

(5) Should There Be a Procedure for Challenging the Notice of an Inspection?

At present, the *Income Tax Act* does not provide a mechanism for challenging an inspection of property. If the person whose premises are to be entered decides not to comply, he or she must refuse the request for entry, thus running the risk of prosecution. We recommend a procedure for challenging the notice, and an enforcement proceeding that essentially mirrors the procedures that we recommend for challenging and enforcing the notice for production.

(6) Who Should Be Authorized to Issue a Notice for Inspection?

See the discussion of the first question in section “B” above with respect to the notice for production.

(7) Should the Person Executing the Inspection Notice Be Required to Display the Authorization?

At present the Act makes no provision as to how authorization to enter to conduct an inspection is to be effected. We recommend a procedure to ensure that the person whose premises are being inspected can verify the authority of those who demand the power to inspect.

(8) Should Entry to Conduct an Inspection Be Limited to Certain Specified Times?

Subsection 231(1) of the *Income Tax Act* provides that entry may be made “at all reasonable times.” We recommend that the Act should be more explicit as to what are reasonable times. For example, perhaps the Act should provide that entry can be effected only during conventional business hours.

(9) Should Persons Whose Property Is Being Inspected Be Required to Give Assistance to Those Conducting the Inspection?

Paragraph 231(1)(c) of the *Income Tax Act* entitles an authorized person conducting an audit to "require the owner or manager of the property or business and any other person on the premises or place to give him all reasonable assistance with his audit or examination" This provision appears adequate.

(10) Should Force Be Permitted if a Person Refuses to Allow an Inspection of Premises?

Under the present provision authorizing an inspection of property, Revenue Canada officials are prohibited from using force to effect an audit. If the person whose premises are to be entered refuses to allow the audit, he or she may be prosecuted for failing to comply with the authorizing section. Under the procedure for challenging a notice of inspection which is recommended in the Paper, the taxpayer or the person whose premises are to be entered will be able to stay the audit by issuing a notice to that effect. If the Minister decides to enforce the notice, enforcement proceedings may be instituted, and if the Minister's application for enforcement is successful, the court will order the challenging party to allow entry. Thus, there is no need for Revenue Canada officials to resort to force.

D. The Power to Seize Property during the Course of an Inspection

(1) Should Revenue Canada Officials Be Authorized to Seize Property during the Course of an Inspection, and If So under What Circumstances?

At present, Revenue Canada officials may seize property in the course of an inspection if it appears to them that there has been a violation of the Act and that the property to be seized is evidence of this violation. We recommend that the telewarrant provisions recommended by the Law Reform Commission in Recommendation 19 of its Working Paper 30, *Police Powers — Search and Seizure in Criminal Law Enforcement* (Ottawa: Supply and Services, 1983), or similar procedures, should be complied with before a seizure in the course of an inspection is made.

(2) Should a Seizure in the Course of an Inspection Be Able to Be Used to Further an Existing Criminal Investigation?

We recommend a rule similar to the one we recommended for the production of documents so that these powers are not used to side-step the requirement of obtaining a search warrant where a violation of the Act is suspected.

(3) Should a Seizure Made in the Course of an Inspection Be Reviewable?

At present the procedures for reviewing a seizure are unsatisfactory for a number of reasons. We recommend a procedure similar to the one for reviewing a seizure made pursuant to a search warrant.

(4) What Procedures for Obtaining Access to Seized Items Should Be Provided?

Subsection 231(6) of the *Income Tax Act* permits access to items seized in the course of a search “at all reasonable times and subject to such reasonable conditions as may be determined by the Minister” Again, we recommend that the same procedures that apply for obtaining access to property obtained pursuant to a search warrant should apply here.

(5) What Procedures for the Disposition of Items Seized in the Course of an Inspection Should Be Provided?

Subsection 231(2) of the *Income Tax Act* provides that within 120 days the Minister shall, on an *ex parte* basis, apply for continued retention of the property seized in the course of an audit. This procedure is inadequate for a number of obvious reasons and we recommend that the procedures for disposing of items seized pursuant to a search warrant should apply.

- (6) Is the Power to Seize in the Course of an Inspection Consistent with the Protection against Unreasonable Search and Seizure in Section 8 of the *Canadian Charter of Rights and Freedoms*?

Aside from the policy reasons for abolishing the power to seize in the course of an inspection, there is a strong likelihood that such a power will be held invalid under the *Canadian Charter of Rights and Freedoms*.

E. The Power to Require Persons to Answer Questions during the Course of an Inspection

- (1) Should Revenue Canada Have the Power to Require Persons to Answer Questions Relating to Their Own or Someone Else's Tax Liability?

Revenue Canada officials at present have this power, and we suggest that they ought to retain it.

- (2) What Procedures Should Be Followed in Compelling Persons to Answer Such Questions?

The *Income Tax Act*, in paragraph 231(1)(c), authorizes a Revenue Canada official to "require the owner or manager of the property or business and any other person on the premises or place ... to answer all proper questions relating to the audit or examination" either orally, in writing, on oath or by statutory declaration. Because compelling a person to answer questions constitutes such a serious intrusion on privacy, we recommend that a more formal procedure — a summons procedure similar to the summons procedure we recommended for the production of books and records — should be enacted for requiring persons to answer questions.

- (3) Does the Power to Require Persons to Answer Questions Offend the *Canadian Charter of Rights and Freedoms*?

Although no cases have been decided directly on this point, we suggest that it does not.

IV. Conclusion

The state needs sufficient intrusion powers to enable it to determine whether all taxpayers are paying their legal tax liabilities. In addition to simply securing the revenues necessary to maintain government expenditures, these powers are necessary so that all taxpayers can be assured that the burden of taxation is evenly spread. If taxpayers generally perceive that some are able to escape their obligation, their dissatisfaction with the tax system will increase and enforcement will become more difficult, perhaps requiring increased coercive powers.

On the other hand, to be acceptable, the state's coercive powers should be exercised so that the individual's invasion of privacy is minimized. Also, the state should be required to exercise its powers pursuant to clearly defined rules.

The proposals in the Study Paper attempt to strike a better balance in the present law between the state's need to gather information in monitoring and enforcing the income tax laws and the citizen's right to privacy. They should result in greater protection for taxpayers but at the same time ensure increased tax compliance.