

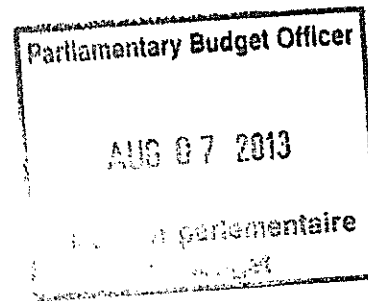


Canada Revenue Agency Agence du revenu
du Canada

Commissioner Commissaire

Ottawa, Canada
K1A 0L5

AOUT
AUG 01 2013



Ms. Sonia L'Heureux
Parliamentary Budget Officer (interim)
Library of Parliament
Parliament of Canada
Ottawa ON K1A 0A9

Re: PBO Information Request IR0102: Tax Gap Estimates

Dear Ms. L'Heureux: -

I am replying to your letter dated June 7, 2013, requesting data from the Canada Revenue Agency (CRA) to support an independent estimate of the Tax Gap by the Parliamentary Budget Office (IR0102).

As you will recall from previous letters dated January 7, 2013 and March 20, 2013, the CRA indicated that it does not currently produce estimates of the tax gap. I would like to take this opportunity to share with you information the CRA has considered on this matter which may be helpful in guiding your decision as to how to proceed.

Most countries do not estimate the tax gap. In fact, according to the Organisation for Economic Co-operation and Development's Tax Administration 2013, 33 of 52 revenue bodies surveyed do not measure the tax gap (please see attached OECD table). Of the countries that do measure the tax gap, estimates are not usually published annually, but every few years, reflecting the high cost of producing such an estimate. The countries that calculate a tax gap do so using different methodologies, and as a result, estimates are not comparable.

The top-down approach – typically used for indirect taxes, such as value added taxes – compares current tax revenues with estimates of taxes, based on broad measures of economic activity, such as gross domestic product. While the top-down approach provides an overall figure for the tax gap for indirect taxes with a reasonable degree of certainty, it does not provide detail for which segments of the taxpaying community are at risk of non-compliance.

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Canada

The bottom-up approach – typically used for direct taxes, such as income taxes – compares current tax revenues with estimates derived from results of compliance actions, surveys and other data, to extrapolate the amount of non-compliance across the full taxpayer population. The bottom-up approach is complex because of the need for random audits and does not necessarily cover all elements of non-compliance or the overall tax gap. Estimates of the tax gap using either approach tend to be undertaken periodically, and for tax years that occurred several years prior to the year of measurement. For this reason, it is difficult to draw comparisons between different jurisdictions. In addition, it is necessary for the tax data to be mostly final (for example, including the results of audits). As a result, tax gap estimates are more reflective of long-term trends than the immediate results of changes to tax policy or tax administration.

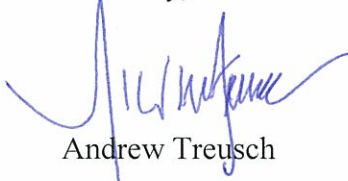
The CRA recognizes the value of detailed analysis of taxpayer behaviour, especially in sectors that are at the highest risk of non-compliance, where analysis can inform our strategies. For example, to increase knowledge and understanding of tax avoidance, the CRA commissioned Statistics Canada to do a study on the Underground Economy (UE) for Canada (a copy is included for your convenience). While the findings of this study confirmed the CRA's previous understanding of unreported income and tax compliance behaviour of certain sectors, the findings also identified other sectors that the CRA should consider auditing. More specifically, it supported the development of CRA's targeted strategies to enhance compliance by directing CRA's resources to focus on specific sectors of the economy that are at the highest risk of engaging in UE activity. There is greater confidence that it is these types of sector-specific strategies that best support the CRA's compliance efforts, as evidenced by the aforementioned UE study which validates CRA's targeted compliance strategy of focusing resources on sectors with the highest risk of non-compliance. Accordingly, the CRA will continue to focus its efforts in these sectors of potential non-compliance.

Regarding your request for tax information, and consistent with section 241 of the *Income Tax Act*, the CRA could provide, under cost-recovery as requested in your letter, initially assessed data and current assessments as of March 31, 2013, for the most recent and complete year available, that is 2008. The difference between initially assessed data and current assessments reflects the difference between reported and assessed amounts that you requested. Current assessments include a large range of changes, not all of which are related to anyone's conception of tax gap.

As examples, changes will include actions such as taxpayer requested adjustments (e.g., when a taxpayer sends additional information and asks to have their assessment updated), reassessments after court decisions or appeals (e.g., for disallowed expenses), applications of losses from other taxation years (e.g., using business losses incurred in a given year to offset profit in a previous year), and reassessments following an audit. The data the CRA can offer would be for the tax filing population as a whole, as creating a representative sample would be costly because of the required effort to select a sample that would truly be representative of the population. The effort required in preparing and delivering the population data is significant and includes the extractions of over 50 million personal income tax records and 4 million corporation income tax records, recreating the original initial assessment files from different source files and reviewing changes at the micro data level to ensure data quality. To initiate this work, your office can contact the Intelligence, Statistics and Data Directorate at 613-957-8706.

In summary, while the CRA can provide you with the requested data, I would like to reiterate that this data will not advance public understanding of the tax gap. As always, the CRA is available to discuss further, should your office need more information about tax data.

Sincerely,



Andrew Treusch

c.c.: Mr. Rick Stewart
Assistant Secretary to the Cabinet
Liaison Secretariat for Macroeconomic Policy
Privy Council Office