

Vote 9. - Office of the Revenue Commissioners

6. Revenue Account

Basis for Audit

An account showing all revenue received and paid over to the Exchequer by the Revenue Commissioners is furnished to me annually. I am required under Section 3 of the Comptroller and Auditor General (Amendment) Act, 1993, to carry out such examinations of this account as I consider appropriate in order to satisfy myself as to its completeness and accuracy and to report to Dáil Éireann on the results of my examinations. The results of my examinations have been generally satisfactory, except for the matters referred to in paragraphs 15 and 16.

I am also required under Section 3 of the Comptroller and Auditor General (Amendment) Act, 1993, to carry out such examinations as I consider appropriate in order to ascertain whether systems, procedures and practices have been established that are adequate to secure an effective check on the assessment, collection and proper allocation of the revenue of the State and to satisfy myself that the manner in which they are being employed and applied is adequate. Paragraphs 13 to 17 refer to matters arising from this examination.

Revenue Collected

Revenue collected under its main headings was as follows

	1997 £m	1996 £m
Income Tax	5,208	4,579
Value Added Tax	3,707	3,109
Excise	2,523	2,304
Corporation Tax	1,697	1,428
Stamps	424	332
Customs	180	163
Capital Acquisitions Tax	89	82
Capital Gains Tax	132	84
Residential Property Tax	3	14
	£13,963m	£12,095m

The amount paid into the Exchequer was £13,976m leaving a balance of £11m prepaid to the Exchequer compared to a balance of £2m owing at the end of the previous year.

7. Write-Offs

The Revenue Commissioners have furnished me with details of taxes written off during the year ended 31 December 1997. The total amount written off is made up as follows

Tax	1997 £,000	1996 £,000
Value Added Tax	73,702	38,244
PAYE	61,625	29,998
Corporation Tax	40,801	12,237
Income Tax	47,343	8,781
Health/Social Insurance- Self employed	55,183	-
Other Taxes	2,495	1,473
	281,149	90,733

The distribution according to the grounds of write-off is

	1997 £,000	1996 £,000
Liquidation/Receivership/Bankruptcy	152,008	43,501
Ceased Trading	20,855	37,940
Uneconomic to pursue	77,806	-
Unfounded Liability	19,594	-
Cannot be traced/Outside Jurisdiction	4,889	6,101
Compassionate Grounds	2,938	2,643
Examinership	3,059	548
	281,149	90,733

The large increase in the amounts written off is due to a revision of the Commissioners' write-off policy with a view to deleting from their records the large amount of debts which are old and regarded as uncollectable and, in the case of estimated assessments likely to overstate the actual liabilities. The objective of the programme, which will take a number of years to complete, is that the debt showing on the books will be more realistic and in large measure collectable, and enable resources to be better targeted and more effectively deployed in collecting arrears. The additional amount written off in 1997 under the programme was approximately £194m *viz.*

- £97.4m was written off on an automated basis comprising Income tax (Estimated Liability) £19.6m, Income Tax (Declared Liability) £18.7m, Corporation Tax £3.9m, and pre-1988 Health Charges and Social Insurance contributions for the self employed £55.2m.
- £8.9m was written off as a result of the change in policy whereby amounts owing by companies in liquidation are written off at the beginning rather than at the end of liquidation proceedings.

- Enhanced efforts were also put into the task of reviewing the debt showing in respect of companies in liquidation and arising from this an additional £88m was written off in 1997. An amount of approximately £95m still remains on the books in respect of amounts owing from companies in liquidation which is intended to be written off over a number of years.

Details of taxes automatically written off amounting to £42.2m were retained by Revenue in paper copy rather than computer format and because of the volume of such write-offs it would be difficult to determine with accuracy the number of cases involved without extra work being undertaken. For this reason, the number of items making up the amounts written off is not presented in the Report, unlike previous years' Reports. Revenue have agreed to my request that such automated write-offs will be retained in computer format in future years.

I have made a test examination of the cases and I am satisfied with the action taken.

8. Outstanding Taxes and Levies

Table 4 was prepared on the basis of information furnished by the Revenue Commissioners and reflects the activities and transactions in the twelve month period ended 31 May 1998 - the latest date for which data was available at the time of finalising my Report.

Table 4 - Outstanding Taxes and Levies

	Balance at 31 May 1997 £m	Charges/ Estimates Raised ^a £m	Paid £m	Discharged £m	Balance at 31 May 1998 £m	Estimate of amount likely to be collected £m
Income Tax (Excluding PAYE) ^b	673	1,145	1,182	81	555	249
VAT (Declared Liabilities Net of Repayments)	159	3,184	3,245	-	98	38
VAT (Estimates) ^c	172	68	89	-	151	15
PAYE (Declared Liabilities)	123	4,059	4,091	-	91	59
PAYE (Estimates) ^c	71	71	98	-	44	11
PRSI (Declared Liabilities)	143	2,012	2,050	-	105	55
PRSI (Estimates) ^c	51	13	31	-	33	7
Corporation Tax	231	1,887	1,788	146	184	74
Capital Gains Tax	56	125	124	9	48	13
Capital Acquisitions Tax	3	106	95	-	14	7
Abolished Taxes	8	1	1	2	6	3
Total	1,690	12,671	12,794	238	1,329	531^d

Notes:

- Net of write-offs*
- Includes Deposit Interest Retention Tax, Withholding Tax, PRSI for the Self-employed, Health Contributions and Levies.*
- Net of discharged estimates.*
- The estimate of the amount likely to be collected takes into account factors such as :*
 - anticipated reductions of estimated amounts included in balances brought forward from previous years.*
 - the level of liquidations and business closures.*
 - historical collection patterns.*

9. Sheriffs and other Enforcement Measures

The Revenue Commissioners have supplied the following information regarding the collection of taxes from recalcitrant taxpayers in 1997:

Sheriffs

Tables 5 and 6 summarise the results of enforcement action taken by Sheriffs on foot of certificates issued under Section 962 of the Taxes Consolidation Act, 1997 (formerly Section 485 of the Income Tax Act, 1967).

Table 5 - Certificates

		No of Certificates	
		1997	1996
On hands of Sheriffs at 1 January		35,097	40,293
Referred to Sheriffs during the year		63,057	82,234
		98,154	122,527
Returned paid	21,265		
Certificates withdrawn - alternative agreements with Revenue	22,164		
Returned unaccompanied by payment	32,153 ^a	75,582	87,430
On hands of Sheriffs at 31 December		22,572	35,097

^a *These arise where*

- *tax returns or claims for repayment are later submitted*
- *companies have ceased trading or have left the address*
- *no distrainable goods are available*

Table 6 - Analysis under tax heads of certificates on hands

	No of Certificates	Value £m
Value Added Tax	9,191	26
PAYE/PRSI	6,654	28
Income Tax	6,159	18
Corporation Tax	446	1
Others	122	1
	22,572	74

The amount paid over to the Collector-General in 1997 by the Sheriffs was £58m compared to £60m in 1996. The Commissioners attribute the continuing diminishing return from sheriffs to changes in debt collection strategy introduced during the past five years. One of the main changes introduced was the Active Intervention Management (AIM) system in 1995 which placed an emphasis on caseworking rather than a computer driven process approach.

Under this strategy sheriff action is regarded as a final enforcement option after all other measures have failed, and the former practice of routinely and repeatedly referring cases to sheriffs has been discontinued. A key objective of the new caseworking approach is to pursue cases to finality through making the defaulting taxpayers compliant or, in the event of this not being possible forcing them out of business. This approach means that the sheriffs are now used much more selectively than in the past and is the main reason for the significant drop in the numbers of cases referred to sheriffs and in the revenues collected by them.

Solicitors

Two firms of solicitors are retained by the Revenue Commissioners to pursue cases which are deemed unsuitable for sheriff enforcement. In 1997 a total of 4,018 items (3,893 items in 1996) were referred to the two firms and the yield was £9m (£8.6m in 1996). The Revenue Solicitor also pursues certain cases for recovery of tax. 161 items (112 items in 1996) were so referred in 1997 and the yield was £0.9m (£0.3m in 1996).

Attachment Orders

In 1997, power to attach amounts owed by third parties to tax defaulters was successfully used in 186 cases (148 cases in 1996) resulting in a yield of £2.9m (£1.4m in 1996).

10. Taxpayer Compliance with Self Assessment Requirements

The rate of taxpayer compliance with the requirements of the self assessment system in terms of returns submitted up to 31 May 1998 was :

Year ended 5 April				
Income Tax	1993/94	1994/95	1995/96	1996/97
No of Returns issued	241,353	258,046	266,163	272,787
% Received 31/5/95	82%	*	*	*
% Received 31/5/96	92%	79%	*	*
% Received 31/5/97	96%	91%	84%	*
% Received 31/5/98	98%	94%	93%	86%

Year ended 31 December				
Corporation Tax	1993	1994	1995	1996
No of Returns issued	69,047	71,671	73,131	74,518
% Received 31/5/95	70%	*	*	*
% Received 31/5/96	79%	73%	*	*
% Received 31/5/97	82%	79%	74%	*
% Received 31/5/98	83%	82%	81%	77%

*- not applicable

Details of prosecution action in 1997 for failure to file Income Tax and Corporation Tax returns is as follows :-

	Income Tax	Corporation Tax	Total
Cases awaiting court hearing 1 January 1997	493	161	654
Legal proceedings instituted	<u>591</u>	<u>329</u>	<u>920</u>
	1,084	490	1,574
Cases heard	<u>223</u>	<u>68</u>	<u>291</u>
Cases awaiting court hearing 31 December 1997	861	422	1,283

Fines were imposed in all cases heard to a total value of £174,060 in 1997.

11. Revenue Audit Programme

An effective tax system must incorporate procedures for verifying the validity of the returns submitted by taxpayers. This involves the desk checking of returns for completeness, accuracy and reasonableness and on-the-spot inspection of documents and records.

The majority of audits carried out by the Revenue Commissioners are specific to taxheads, like VAT and PAYE, but a significant number of comprehensive audits are also carried out which may focus on all or any taxes payable but in practice are primarily aimed at Income Tax, Corporation Tax and Capital Gains Tax. There is also a body of work which comes under the general category of Revenue audit arising out of the activities of the investigation and anti-avoidance branches.

Revenue audit activity is a key element of the tax collection system and in this context I noted that the number of audits completed by Revenue had fallen from 19,767 in 1996 to 18,762 in 1997 while there was a reduction in the tax yield from £141m to £131m. In 1995, 23,294 audits were carried out yielding £148m. The outcome of the Revenue audit programme is summarised in Table 7.

I was informed by Revenue that the reduction in the number of audits and the audit yield in 1997 compared to 1996 was mainly due to:

- A reduction of 13 in the number of staff conducting Comprehensive, VAT and PAYE Employers audits. These staff were re-deployed to the Compliance and Criminal Assets Bureau areas.
- A learning period for the 11 newly trained auditors who carry out audits on computer systems to identify areas of Revenue risk.
- The re-deployment of 9 staff in Investigation Branch from investigative duties to a dedicated Prosecution Policy Unit.
- The temporary deployment in the last quarter of 1997 of 12 Relevant Contracts Tax auditors to man Revenue's nationwide operation to monitor tax compliance in the construction industry.

Table 7 - 1997 Revenue Audit Programme

(i) Audits Completed

Audit Type	1997		1996	
	No. of Audits Completed	Yield £m	No. of audits Completed	Yield £m
Comprehensive Audits	3,635	60.10	3,969	69.21
Value Added Tax	7,764	38.93	8,424	33.04
PAYE Employers	5,095	14.10	5,358	19.54
Capital Acquisitions Tax	315	3.30	315	2.60
Relevant Contracts Tax	1,856	8.10	1,582	7.99
Investigation Branch	77	3.71	90	5.95
Anti - Avoidance	20	2.40	29	2.42
Total	18,762	£130.64m	19,767	£140.75m

(ii) Comprehensive Audit Results

As part of the self assessment system comprehensive audits are carried out following review of returns made for Income Tax and Corporation Tax purposes. The result of this audit activity is as follows:

Audit Activity	Total		Income Tax Returns		Corporation Tax Returns	
Audits in progress at 1/1/97	2,087		1,237		850	
Audits initiated in 1997	<u>3,387</u>		<u>2,440</u>		<u>947</u>	
Total		5,474		3,677		1,797
Returns accepted	808		525		283	
Cases closed with additional liability	<u>2,827</u>	3,635	<u>2,059</u>	2,584	<u>768</u>	1,051
Referred to Investigation Branch		31		21		10
Audits in progress at 31/12/1997		1,808		1,072		736

(iii) Yield from Comprehensive Audits

Income Tax Returns		No.	As % of Total	Yield £	As % of Yield
Returns Accepted - No additional tax payable		525	20	-	-
<i>Agreed Settlements</i>					
£1 - £5,000	930		36	2,209,679	8
£5,000 - £50,000	983		38	14,299,145	51
£50,000 - £100,000	57		2	3,959,974	14
Over £100,000	<u>23</u>	1,993	1	6,961,318	25
<i>Referred to Collector General for enforcement action (a)</i>		20	1	317,882	1
<i>Settled by Restriction of Losses Carried Forward to Future Years (b)</i>		46	2	410,812	1
Totals		2,584	100	28,158,810	100

Corporation Tax Returns		No.	As % of Total	Yield £	As % of Yield
Returns Accepted - No additional tax payable		283	27	-	-
<i>Agreed Settlements</i>					
£1 - £5,000	264		25	754,474	2
£5,000 - £50,000	377		36	7,026,908	22
£50,000 - £100,000	51		5	3,438,167	11
Over £100,000	<u>42</u>	734	4	16,727,617	53
<i>Referred to Collector General for enforcement action (a)</i>		6	1	429,843	1
<i>Settled by Restriction of Losses Carried Forward to Future Years (b)</i>		28	2	3,562,340	11
Totals		1,051	100	31,939,349	100

- a. Where the Inspector is unsuccessful in collecting the additional tax and interest arising on audit adjustments, the amounts are referred to the Collector General. It is likely that the amounts eventually collected by the Collector General will be significantly less than the full amounts shown.
- b. A number of audit settlements involve the restriction of losses available for carry forward against future years' profits, thereby providing higher tax yield in those years. The yield shown assumes that taxable profits in future years will fully absorb the losses. This may not always be the position and hence the yield figure may be less than the figure shown.
- c. The amount of the highest individual settlement in 1997 was £3,374,495 and arose in respect of a Corporation Tax audit.
- d. Interest charges of £7.63m and penalties of £4.22m are included in the yield from agreed settlements.

(iv) Random Audits

As part of the 1997 Audit Programme, a total of 68 random audits were completed. Additional liabilities of £115,435, including £32,057 in penalty and interest charges, were assessed in 25 cases while the returns of the remaining taxpayers were accepted as originally submitted.

(v) Arrears of Tax collected by Auditors

In addition to the yield collected by auditors on adjustments made to tax returns, they also collect any arrears of tax already on record with interest. This amounted to £22.2m in 1997.

12. Investigation Branch Settlements and Prosecutions

Audits carried out by Revenue staff on taxpayers may reveal underpayments of tax due to inaccurate records, incorrect application of taxation rules and regulations and other factors. A settlement in relation to the taxes underpaid and interest and penalty charges arising is generally reached on audit between the taxpayer and Revenue staff. However, where evidence of systematic or widespread evasion of tax comes to the attention of Revenue, either through audit or from other sources, the cases are referred to their Investigation Branch. Where such investigation reveals that a taxpayer has failed to disclose relevant information, resulting in an underpayment of tax, legal proceedings may be instituted against the taxpayer. Alternatively, the Revenue Commissioners may agree to accept from the taxpayer a sum in settlement of the tax outstanding with the addition of interest and penalty charges.

Early in 1997 the Revenue Commissioners completed a reorganisation of the Investigation Branch, concentrating the preponderance of the staffing resource in pursuing a prosecution strategy in contrast to the previously prevailing policy of accepting monetary settlements in virtually all cases. The continuing reduction in both the number of investigations completed and the yield therefrom is a direct consequence of this change in emphasis.

During 1997, investigations were completed in 77 cases, 24 of which resulted in back-duty settlements amounting to £3,712,897 (90 cases in 1996 of which 47 yielded £5,949,172) becoming collectable inclusive of £1,462,818 (£1,043,743 in 1996) in penalty and interest charges.

The Accounting Officer supplied me with the following information in relation to prosecutions in 1997:

Cases on hands at 1 January 1997	14
Cases referred for consideration for prosecution in 1997	18
Cases dropped due to lack of evidence	6
Cases brought to Court in 1997	3
Cases on hands at 31 December 1997	23

Of the 23 cases on hands at the year end, 20 were still being examined and decisions to prosecute had been made in three cases.

Of the cases brought to Court in 1997 all three resulted in successful convictions. A fine of £500 was imposed in one case and disqualification to act as a director of a company as well as a suspended prison sentence of six months was imposed in a second case. In a third case a fine of £12,000 was imposed on a company and a two years suspended prison sentence imposed on a director of the Company.

13. PAYE Audit

Following a review by my staff of PAYE audit arrangements, a number of matters were raised with the Accounting Officer.

Case Selection for Audit

Screenings of taxpayers' returns for possible audit by Revenue were all performed manually. It would appear that the screening process could be more efficient and effective if computer power was harnessed to process the vast amount of computerised information held on taxpayers. The development of appropriate computer programmes to automatically identify taxpayers falling within predetermined selection criteria would release for other tasks the significant amount of manpower currently employed in carrying out this work manually.

The Accounting Officer stated that the computerisation of the screening process was desirable and that this was being actively considered as a development to the Common Registration System and the Active Intervention Management (AIM) system. In the meantime, a computerised system was being put in place to record the results of further in-depth secondary screening carried out before final selection for audit. The feasibility of introducing a computer assisted risk rating system for audit case selection had been under active consideration for some time. The internal research had been completed and the compatibility of such a system with existing developments in the Consolidated Tax Project was currently being evaluated.

Recording Audit Results

There appeared to be scope for improving the way details of audits were recorded and classified as a means of refining audit selection strategy.

The Accounting Officer informed me that as a development under AIM, a proposed computer analysis facility would, when available, record the basis for case selection and the causes of underpayments identified on audit. It would then be possible to analyse the audit results and to identify the circumstances which occur most frequently and which give rise to the highest yields as a means of better informing audit strategy. However, because of pressure on computer development for Year 2000 and the Euro it would be some time before the facility would be available countrywide.

Imposition of Penalties

Where underdeclarations of taxes are discovered on audit, mitigated penalties of £120 are usually imposed under Section 987 of the Taxes Consolidation Act, 1997, (previously Section 128 of the Income Tax Act, 1967), on the grounds that taxes had not been paid when due. Whereas tax legislation provides for significant penalties in respect of underdeclarations in respect of Income, Corporation and Value Added Taxes amounting to 100% of the tax where the underdeclarations are attributed to negligence and 200% if they are fraudulent, no such penalties are provided for in relation to underdeclarations of PAYE and PRSI.

The Accounting Officer stated that the Tax Acts provided for a wide range of penalties for non-compliance and tax evasion. Some of these were civil penalties and others were criminal in nature under which a person found guilty could be subjected to a fine or imprisonment or both. Because the civil penalties in relation to the various taxes were developed at different times some inconsistencies had emerged which would be considered in the context of the 1999 Finance Bill. Criminal penalties were, by contrast, more consistent and applied to a range of taxes including PAYE/PRSI, and they were for the most part covered by Section 1078 of the Taxes Consolidation Act, 1997, and could only be applied by the Courts and be pursued under Revenue's prosecution programme in appropriate cases.

Duration of Audits

As the average duration of a PAYE/PRSI audit is about two to three days, I sought assurances from the Accounting Officer that the audits were of sufficient depth and penetration to afford a reasonable chance of detecting any significant tax evasion that may be taking place, and that the level of resources committed to PAYE and PRSI audits, and Revenue audits generally, was adequate.

The Accounting Officer informed me that a majority of businesses were small family-owned enterprises, and experience had shown that a 2-3 day audit was sufficient for the normal low risk that such cases presented, but that the duration of the audit would be extended for periods of up to 10 days approximately where significant risks were identified. He stated that where there was a likelihood of significant evasion, the case would be referred for a comprehensive audit to examine the risks under all taxheads. He was satisfied that the length of audits was adequate to deal with the tax risks.

He also stated that approximately 6% of taxpayers had their returns examined under at least one of the main audit programmes - Comprehensive, VAT, RCT and PAYE/PRSI - in both 1996 and 1997 and that most employers with any significant PAYE/PRSI exposure had been audited. He was satisfied with this level of audit coverage.

14. PAYE Compliance

Employers are required to pay to the Revenue Commissioners the net amount of PAYE and PRSI deducted for the relevant income tax month by the following nine days. The income tax month runs from the sixth day of a calendar month to the fifth day of the following calendar month. Section 987 of the Taxes Consolidation Act, 1997, (previously Section 128 of the 1967 Income Tax Act), provides for the imposition of a £1,200 fine for the failure to pay over the monthly amounts of taxes due by the statutory dates. Compliance has been improving in recent years as Table 8 indicates.

Table 8 - Monthly Returns Compliance - All Cases

	1993	1994	1995	1996*	1997*
	%	%	%	%	%
Due Month	31	37	41	43	49
Due month + 1	52	56	57	58	61
Due month + 2	61	65	66	65	67

* Data in respect of 1996 and 1997 are not directly comparable with the data from earlier years. The basis of measuring compliance was improved in 1996 to take account of taxpayers paying by Direct Debit and of returns received on the last day of the month.

The percentages for compliance are much higher for large liability employers as Table 9 indicates.

Table 9 - Monthly Returns Compliance - Large Liability Cases

Payment Case Size	1996			1997		
	Due Month %	1 Month late %	2 Months Late %	Due Month %	1 Month Late %	2 Months Late %
>£25,000 per month	84	95	97	87	96	98
£10,000 - £24,999 per month	73	89	93	80	92	94
£7,000 - £9,999 per month*	n/a	n/a	n/a	74	89	n/a

* Caseworking was extended to these cases in 1997.

The Accounting Officer attributes the high level of compliance for large liability employers to the success of Revenue's caseworking approach and it is intended to extend this approach to further groups of cases as resources allow. He informed me that the general improvement in compliance also reflects:

- the raising of interest charges and ensuring such charges are paid, which is facilitated by the caseworking approach.
- ongoing initiatives to promote voluntary compliance through Revenue's customer service approach.
- significant investment in information technology and in staff training.

In response to my inquiries the Accounting Officer stated that:

- The Commissioners were generally satisfied that the procedures and legal powers in relation to the collection of PAYE/PRSI were adequate.
- The charging of interest was regarded as the most efficient and effective deterrent to late payment, and that any proposal to give the Commissioners powers to levy penalties directly for late payments rather than having to prosecute through the Courts would require careful consideration.
- Varying the level of penalties in line with the amounts of tax outstanding was currently under review with regard to the submission of end of year PAYE/PRSI Returns.
- The Commissioners considered that interest should be applied where possible to late payers, but that the application and collection of interest charges was resource-related. However the levying of interest charges was being progressively extended through the various case sizes.
- Revenue now had the necessary management information tools to identify at an early stage employers who continuously or regularly defaulted. The action taken against such employers was determined by the frequency and extent of default, and the revenue at risk and would include, where appropriate, stringent enforcement action.
- Although no employers had been prosecuted in 1997 for late payment of their monthly PAYE/PRSI, a significant number of employers had been prosecuted each year for failure to file their end of year P35 Returns. However, prosecution would not be practicable as the general method of countering late payment for any sizeable number of cases, as neither Revenue or the Courts could cope with such an approach.
- The question of putting the monthly return on a more formal legal footing would be kept in mind in the context of future changes to the tax system.

15. Value Added Tax (VAT)

The VAT ledger records the VAT receipts due from taxable persons and the amount received in respect of this liability.

In the course of audit many accounts were noted where the amount received from the taxpayers exceeded the liability recorded. The total value of these account surpluses was £73.8m. In several cases the apparent overpayments were long standing. The audit findings indicated that a significant proportion of the total did not represent actual overpayments but may have been due to repayments or returns not having been posted to the ledger, accounting adjustments not having been made in respect of offsets against other taxes, and other bookkeeping errors.

In response to my inquiries the Accounting Officer informed me that:

- The detailed requirements for a control account which would reconcile all input transactions for tax charges and payments to the total changes on taxpayer accounts were currently being examined so as to consider the feasibility of including this feature when VAT was being incorporated into the integrated taxpayer computer system.
- Resource levels prevented a systematic review of all apparent overpayments on record, but cases were reviewed on a day to day basis as they were encountered through normal caseworking and, in addition, all large apparent overpayments were reviewed on a regular basis. While he was satisfied that this approach represented the most effective use of available resources, he accepted that there was a need to try and identify genuine overpayments more systematically and accordingly he was making the necessary arrangements to carry out a review of procedures to deal with the issue.
- Where a taxpayer submits an application for a refund of an overpayment, the application was processed and the circumstances of the case examined, and a refund would be made where appropriate. However, if there were doubts as to the validity of the claim, the Inspector of Taxes would be requested to carry out an inspection and certify that the refund was in order.
- While it was impossible to say how much of the apparent overpayments were genuine, he was satisfied that the vast majority of cases did not represent actual overpayments.

16. Capital Acquisitions Tax (CAT)

Capital Acquisitions Tax (CAT) is a composite term which covers Probate Tax, Inheritance and Gift Tax and Discretionary Trust Tax. In 1997 the yield from CAT was £89m. The following matters noted on audit were brought to the attention of the Accounting Officer:

Administration Controls

Up to 1995 the administration of CAT was manually based but in that year a computer system was installed to keep a record of each individual payment in respect of any new case opened after mid June 1995. The system was primarily designed as an enquiry and cash accounting system, as

well as a management information tool. It was never intended to replace the paper files as records of individual cases. The volume of transactions and numbers of users have grown since 1995 and a more sophisticated system is now required.

The Accounting Officer informed me that the CAT computer system is an RSI number based system. Prior to its introduction there was no requirement to furnish the RSI numbers of donors and taxable beneficiaries. It was not feasible given the resources available at the time to convert old files into RSI computer-based records, which would also have required correspondence with taxpayers or agents. In any event, the number of cases opened pre-1995 which remain active is decreasing.

The overall aim is a fully integrated networked computer system, serving the whole of Capital Taxes Division. It was recognised, however, that such a project in its entirety would take some time to develop especially in the light of the pressure on resources from more urgent requirements. Therefore, it was decided to develop the system on an incremental basis. To this end, the processes of the Division were examined in detail, and those areas which had the heaviest volumes of work, and which had to put most manual effort into keeping track of outstanding cases and producing management information, were identified as the areas which would benefit most from interim computer support. The fact that these areas were also the areas in which most cases started and finished their life cycle served to reinforce this decision. As and when resources become available, it is intended that the final stage of the integrated system will be added.

He was satisfied that the current system had been a useful development and met the purposes for which it was introduced.

Assessment and Collection Procedures

A review of the assessment and collection procedures for CAT revealed some shortcomings including:

- lack of supervisory checks on closed cases
- control weaknesses over the refund of tax
- inadequacies in controls over certificates of discharge i.e. certification that all due capital taxes have been paid on particular properties
- lack of assurance that all receipts issued are in respect of amounts received.

In response to my inquiries the Accounting Officer stated that:

- Cases are dealt with by different officers at various stages of the processing system which of itself provides for an element of control and allows for discrepancies to be identified and acted upon. It is accepted that a more rigorous control and checking procedure at supervisory level in relation to closed cases is desirable. Random supervisory checks were carried out in the past, but lapsed due to increased work pressures, mainly arising from the move to an RSI number based filing system. These random supervisory checks of closed cases have now been reintroduced. In addition, the use of the CAT computer system to allow for more focused quality control checks will be investigated. A detailed case by case supervisory check of closed

cases would be resource intensive and could not be justified on cost grounds. Random supervisory checks are considered to be the better value for money approach.

- For every case for which a refund is required a warrant is completed and approved by an official with the necessary authorisation. It is sent to the Accountant General's Office which issues the payment order directly. Under the arrangements Capital Taxes Division are not notified when refunds are actually paid, but following my audit these arrangements will be reviewed. Since the audit all the refund warrants are being sequentially numbered, monetary limits for the authorisation of refund warrants are being strictly adhered to and a direction has issued to all staff in this regard.
- While he recognised that there were some inadequacies in the certificates of discharge area, he considered the controls in place generally to be adequate. Nevertheless, a full review of the entire system of certificates of discharge, including security aspects, is scheduled to commence shortly.
- More systematic checks on unaccounted for receipts are being introduced and the result of such checks will be recorded.

Cash Controls

In general the post was opened by personnel who were also involved in the maintenance of the taxpayer ledger records. After recording in the taxpayers' ledger accounts the cheques are taken to the cash office for lodgment to Revenue's bank account. No records were kept of the number and amount of cheques received at the post opening stage for reconciliation with the number and amount of cheques processed and lodged at the bank.

As it was my view that the procedures represented a control risk, particularly bearing in mind the large amount of moneys received, (£89m in 1997) I sought the views of the Accounting Officer.

The Accounting Officer stated that the current policy was to process payments received in a secure and timely fashion in order to maximise same-day value for the Exchequer, while maintaining a timely and accurate updating of the taxpayer record. He considered that recording the number and amount of cheques in the post room would impede productivity and delay lodgment to the Exchequer. He stated that a balance had to be struck between the timely processing of payments and the extent of the checking and recording procedures, and that in his view the current supervisory controls and procedures had, generally speaking, got the balance right. However, he also stated that the matter would be given further consideration in the proposed review of procedures.

Revenue Audit

Underdeclared tax (including interest, penalties and surcharges) of £3.4m was discovered by the three person audit unit in 1997. While no precise figures were available, my staff were informed that there were underpayments in 70% to 80% of cases audited.

In view of the high level of underdeclarations discovered, I asked the Accounting Officer if he was satisfied that an adequate number of staff were employed on audit to ensure an acceptable level of tax compliance.

He stated that the high yield for audit cases was a reflection of the fact that the audit selection was primarily targeted rather than random in nature, and on that basis it was considered that the number currently engaged on this work was adequate, considering overall resources and demands on the Office. The number and grade of staff working on audit and investigation activities was regularly reviewed.

Penalties

The Capital Acquisitions Tax legislation provides for severe penalties for not submitting CAT returns or for making incorrect returns.

I sought information from the Accounting Officer as to the circumstances under which penalties were applied, the level of penalties imposed in 1997, and inquired if he was satisfied that full use was made of the Commissioners' powers to impose penalties to ensure that there was a real and effective deterrent against the evasion of CAT.

The Accounting Officer stated that penalties were applied in clear cases of negligence, and that such cases, which were few in number, mainly came to attention during audit and investigation work. In practice, when reaching a settlement with the taxpayer, a compromise figure was agreed which included the full tax and interest together with an amount for penalties. A number of such settlements have been reached in the past but none in 1997. He assured me that the level and application of penalties would be kept under review.

He also stated that the general practice had been to use the threat of Court proceedings as a means of securing compliance and this had proved to be largely effective. Legal proceedings would, of course, be instituted if necessary.

17. Excise Duty - Wines and Spirits

During 1997, £208m was received in excise duties relating to Wines and Spirits. The following matters were noted by my staff during the course of an audit of these duties and were brought to the attention of the Accounting Officer:

Revenue Audit

The Commissioners have traditionally relied on bonded warehouses to ensure the collection of the great bulk of excise duties. Under this system, excisable goods are required to be stored in bonded warehouses and the movement of goods into and out of the warehouses is monitored by Customs and Excise staff to ensure that the correct duty is paid on all product released from the warehouses on to the open market. Products are monitored by physical checking of goods and by checks against shipping and customs documentation. Heretofore it has not been considered necessary to have any cross checks performed against the commercial and accounting records of

traders or their audited accounts. The system was very effective in an era when tight controls could be operated at ports and along the border, and when the relatively low volume of trade permitted significant checks to be carried out on goods entering the country. However, since 1993 with the advent of the Single Market in the EU and the dismantling of trade barriers, the Irish customs authorities are severely constrained in the physical checks they can carry out on goods being imported from other EU member states. Moreover, there has been a huge increase in the volume of imports both from other EU states and from countries outside the EU. These developments have somewhat weakened the effectiveness of the bonded warehousing system as traditionally operated to ensure the collection of all due excise duties on certain goods such as wines and spirits. For these reasons the Commissioners have recently decided to introduce an audit based system, whereby the commercial and accounting records of warehousekeepers would be periodically examined and cross checked against warehouse records and excise returns.

The Accounting Officer supplied me with the following information in relation to the prospective audit based system:

- The process of moving to an audit based system was well under way, the working arrangements for the new system had been specified and the task of meeting the warehousekeepers to outline the new requirements had commenced. These meetings would initiate the process of assessing, in collaboration with warehousekeepers, the extent to which their existing systems needed to be modified to meet the new requirements. The existing control regime in warehouses would only be removed when their accounting and other control systems and procedures were satisfactory from a Revenue perspective. Because some warehousekeepers would be better placed than others to meet the requirements, it was not possible to state when all warehousekeepers would be ready for the new procedures, but it was intended that they would all be ready by December 1998.
- The staffing requirement had been identified and arrangements were in hand to provide the appropriate training.
- It was not considered appropriate to introduce a methodology for extrapolating sample audit findings. In a situation where audit results suggested that a full examination of all transactions was warranted then that would be done, particularly if there was any suggestion that duty liabilities had been underdeclared. Procedures would be kept under review in the light of audit experience.

Checking of Goods

It was noted that the level of checks on goods entering warehouses provided for in the procedures were not being carried out in a warehouse examined by my staff and satisfactory evidence was not maintained of the checks actually carried out. Furthermore, the guidelines in relation to some checks were somewhat unclear and ambiguous.

The Accounting Officer stated that it had been recognised for some time that the level of checks, particularly in the case of intra-EU movements, should be reduced. The imminent changeover to an audit-based system would, in any event, mean that much less emphasis would be placed on such checks, although they would not be dispensed with entirely. As it had been planned for some time

to introduce audit based controls, piecemeal changes to existing staff instructions had been avoided pending the issue of new audit and administration guidelines. These guidelines, which were being prepared, would require that details of any checks carried out were recorded.

Consolidation of Legislation

As the legislation relating to excise duties is contained in a number of different statutes dating back to the early 19th century, I asked the Accounting Officer if the Commissioners would see any merit in reviewing and consolidating the legislation to ensure it was appropriate and effective in current circumstances and to facilitate staff in its application.

The Accounting Officer stated that the consolidation of legislation, including Excise legislation, had already been identified by Revenue as a key strategy in its corporate plan 1997 - 1999. A planned programme, which would include updating, was underway but it was likely to be at least three to four years before the process was fully completed. The plan provided for consolidation and modernisation of the hydrocarbon oil primary and secondary legislation for enactment in 1999, followed by general excise law in the year 2000, and alcohol law in 2001. He also stated that as an essential step, the various provisions of general excise law were being consolidated into a computer record, under a range of headings, and when this work was completed the information would be circulated for use as a reference source by staff.

Penalties and Interest

While Customs and Excise legislation provides for severe penalties in relation to underpayments of excise duties where the underpayments are considered to be fraudulent, no substantial penalties are provided for where underpayments are attributed to negligence, unlike the legislation relating to some of the main taxes such as VAT and Corporation Tax. Furthermore, existing excise legislation does not provide for the charging of interest for late payments of excise duty unlike tax legislation.

As I felt that penalties and interest could have an important deterrent effect against evasion and late payment I asked the Accounting Officer why they had not been provided for in legislation and if there were any plans to do so.

The Accounting Officer stated that the issue of civil penalties to deal with minor breaches of either the law or approval conditions, where there was no deliberate intent, had been considered. Such penalties would have application even where there was no late payment or underpayment of duty, and might deal with matters such as late submission of reports, or failure to keep adequate records. The charging of interest would be another option where an underpayment was involved. While there were arguments in favour of civil penalties and interest charges, it was considered that the introduction of such provisions should, if required, be proceeded with in the context of the planned review and updating of excise law over the next number of years.

Security Bonds

Warehousekeepers are obliged to pay their excise duties monthly and to furnish bonds to the Commissioners to guarantee payment of amounts outstanding. In response to my inquiries regarding the calculation of bond amounts the Accounting Officer stated that recommendations as to the size of bonds were made by highly experienced and expert officers. The primary concern

was to ensure that the bond was adequate to cover any potential risk. The Commissioners were satisfied that there was consistency in this procedure, having regard to the fact that no two warehouses presented identical risks. However, staff guidelines were being drafted which would codify the various factors to be taken into account in the calculation of bonds.