Accounts of the Public Services 2010

Central Government and Revenue

Report of the Comptroller and Auditor General

Volume 1

Presented to Dáil Éireann pursuant to Section 3 (11) of the
Comptroller and Auditor General (Amendment), Act 1993

September 2011

The report was prepared on the basis of information, documentation and explanations obtained from Government Departments and Offices referred to in the Report.

Drafts of relevant segments of the Report were sent to the Departments and Offices concerned and their comments requested. Where appropriate these comments were incorporated into the final version of the Report.

The report focuses on the accountability of Departments and Offices in respect of their administration of public funds. References to third parties should be read only in that context.

Tá leagan Gaeilge den tuarascáil seo ar fáil freisin A11/1295

Report of the Comptroller and Auditor General on the Accounts of the Public Services – 2010

I am required under Article 33 of the Constitution to report to Dáil Éireann at stated periods as determined by law.

Pursuant to that constitutional provision, I am required under Section 3 of the Comptroller and Auditor General (Amendment) Act, 1993 to report to Dáil Éireann on my audit of the Appropriation Accounts of Departments and Offices and the Account of the Receipt of Revenue of the State not later than 30 September in the year following the year to which the accounts relate.

I have certified each Appropriation Account for the year ended 31 December 2010 and submitted those accounts together with my audit certificates to Dáil Éireann.

Separately, I report on matters arising out of my audit of the accounts of the public services. My report which is in two volumes is set out beneath.

- Volume 1 deals with matters arising out of the audit of Central Government and Revenue and the National Debt

- Volume 2 outlines some matters that arose out of the audit of funds charged to particular Appropriation Accounts.

I hereby present both volumes of my Report for the year ended 31 December 2010 in accordance with Section 3 of the aforementioned Act.

John Buckley
Comptroller and Auditor General

19 September 2011

Report on the Accounts of the Public Services 2010

Volume 1 – Central Government and Revenue

Table of Contents

Chapter 1

Financial Outturn for 2010

Central Government

Financial Outturn for 2010

1.1 The State deficit, representing the excess of payments over receipts, was €18.15 billion in 2010. Certain non-cash outlays arising out of the issue of Promissory Notes of €30.85 billion are not included in that figure.

1.2 The receipts and payments for each of the years 2007 to 2010 are summarised in Figure 1.

Figure 1 Overall Receipts and Payments, 2007 to 2010 [a]

	2007 €m	2008 €m	2009 €m	2010 €m
Receipts				
Tax revenue	47,249	40,777	33,043	31,753
Other current revenues	638	847	838	2,687
Loan repayments	747	749	750	1,043
Other capital receipts	196	161	140	138
Total receipts	**48,830**	**42,534**	**34,771**	**35,621**
Payments				
Issues for voted expenditure	44,609	49,313	47,163	46,434
Share capital acquired in banks	–	–	4,000	725
Service of National Debt	1,676	1,611	2,641	3,619
National Pensions Reserve Fund contribution	1,616	1,690	3,000	–
Contribution to EU Budget	1,572	1,587	1,486	1,352
EU Stability Support	–	–	–	346
Loans issued	740	741	790	972
Oireachtas Commission	114	123	123	103
Other payments	122	183	209	215
Total payments	**50,449**	**55,248**	**59,412**	**53,766**
Deficit for the year	**1,619**	**12,714**	**24,641**	**18,145**

Sources: Finance Accounts 2007 to 2010 and Financial Statements of the National Debt of Ireland

Notes: a The above account is a consolidation of transactions processed through the Exchequer Account and the Capital Services Redemption Account.

b Other payments include €110 million advanced as a working facility to the Social Insurance Fund.

1.3 Receipts into the Central Fund in 2010 totalled €35.6 billion. This represented an increase of €851 million relative to the 2009 receipts of €34.8 billion, but a cumulative 27% decrease from 2007 levels. Within the total income for 2010, taxation receipts fell by €1.3 billion compared with 2009. However, this was offset by an increase in other current revenues made up predominantly of premia under two bank guarantee schemes[1].

1 This is dealt with in Chapter 4.

1.4 Overall State expenditure in 2010 was €53.8 billion, a reduction of 9.5% on the 2009 level. The key features of the 2010 expenditure were

- Following an accelerated Exchequer contribution to the National Pension Reserve Fund (NPRF) in 2009, there were no further payments to the Fund in 2010 (a reduction of €3 billion in cash requirements by comparison with 2009 levels). Chapter 8 outlines the Fund transactions relating to the State's bank stabilisation measures.
- A further €725 million was issued in 2010 to acquire shares in banks, bringing the cumulative cash investment through the Exchequer to €4.73 billion[2]. However, the 2010 outlay by way of direct cash assistance represented a reduction of €3.27 billion on 2009 outgoings.
- Expenditure related to servicing the national debt increased by €979 million or 37%[3]. Chapter 2 outlines the national debt position in more detail.
- Net voted expenditure fell by €729 million in 2010 following a €2.1 billion reduction in 2009.
- Included in 'Other Payments' are amounts totalling €4.8 million paid to political parties under Section 17 of the Electoral Act 1997. The aggregate amount is based on a fixed sum (€3.81 million) indexed in line with pay increases under national wage agreements up to September 2008. No adjustment has been made to take account of downward adjustments in public service pay in recent years.
- Issues of €103 million were made to the Oireachtas Commission in 2010. The expenditure of the Commission is summarised in Figure 2.

1.5 €600 million was transferred to the Capital Services Redemption Account (CSRA) in 2010. This amount was unspent at 31 December 2010. The balance in the CSRA, which is maintained by the National Treasury Management Agency, is subject to guidelines issued by the Minister for Finance (the Minister). The Minister directed that the balance at the end of 2010 should not exceed €601 million. In previous years, the limit on the balance was €1 million.

2 Chapter 4 deals with the financial stabilisation measures taken by the State in the banking sector.

3 This represents the service cost excluding sinking fund payments.

Figure 2 Houses of the Oireachtas Commission Expenditure[a], 2009 and 2010

		2009		2010
		€000		**€000**
Members of the Houses of the Oireachtas[b]				
Salaries [c]		23,782		20,980
Travel expenses		5,174		5,962
Other allowances and expenses		7,236		7,929
Secretarial assistance for non-office holders		19,524		20,493
Grant-in-Aid in respect of Ciste Pinsean Thithe an Oireachtas		**10,340**		**10,000**
Administration Expenses				
Salaries, wages and allowances in respect of staff members	26,076		23,545	
Other administrative expenses	24,253	50,329	14,032	37,577
Other Services[d]		6,821		4,256
Total Expenditure		**123,206**		**107,197**

Source: Accounts of the Houses of the Oireachtas Commission

Notes:
a The issues from the Central Fund differ from the expenditure since funds are advanced on a cash needs basis.
b This includes one MEP. All other MEPs opted to be paid directly by the European Commission.
c Expenditure comprises the salary payment due to the TDs and Senators as elected Members of the Oireachtas. Any additional salary payments for the Taoiseach or ministerial positions are paid directly by the relevant departments.
d ‘Other Services’ include payments in respect of catering and bar staff, televising of Oireachtas proceedings, expenses relating to Oireachtas Committees and a pension scheme for secretarial assistants.

Audit of State Accounts

The summary in Figure 1 is drawn from an account of the Exchequer – the Finance Accounts – that, *inter alia*, show the payments into and out of the Central Fund. The summary also takes account of transactions processed through the CSRA which has been audited and reported upon in the course of the audit of the accounts of the National Treasury Management Agency. The 2010 Finance Accounts have been audited and are due to be presented to Dáil Éireann by 30 September 2011.

State Financial Outturn and GNP

1.6 Gross National Product (GNP)[4] represents the amount of output of the economy attributable to citizens of Ireland regardless of their geographical location. Figure 3 sets out the relationship between the income and expenditure of the State and GNP over the years 2007 to 2010, both in absolute and percentage terms.

Figure 3 Government Funding and GNP

	2007		2008		2009		2010	
	€bn	%	€bn	%	€bn	%	€bn	%
Taxation receipts	47.3	29	40.8	26	33.0	25	31.8	25
Government payments	50.4	31	55.2	36	59.4	45	53.8	42
Gross National Product [a]	**163.4**		**154.7**		**132.2**		**128.2**	

Source: Central Statistics Office

Note: a GNP is stated at current prices i.e. the prices that prevailed in the year.

1.7 The years 2007 to 2010 have seen a decline of 21.5% in Irish GNP. The proportion of this reduced amount that is accounted for by taxation has diminished, with tax receipts declining from a level of 29% of GNP in 2007 to 25% in 2010. State expenditure, as a proportion of GNP, has increased from 31% in 2007 to 42% in 2010. 3.7% of the 2010 expenditure (in terms of GNP) was attributable to the cost of debt servicing, EU stability support and share capital injections into banks.

Voted Expenditure

1.8 Chapter 18 sets out the outturn of vote management by Accounting Officers in 2010. The net voted expenditure for each year comprises expenditure that is classified as current or capital. Figure 4 shows the composition of net voted expenditure over the past four years. Overall, the proportion devoted to capital has declined by 4% over that timeframe with current expenditure increasing to the same extent.

Figure 4 Composition of Net Voted Expenditure, 2007 to 2010

	2007		2008		2009		2010	
	€bn	%	€bn	%	€bn	%	€bn	%
Current	37.0	83	40.7	83	40.3	85	40.6	87
Capital	7.6	17	8.6	17	6.9	15	5.9	13
Total	**44.6**		**49.3**		**47.2**		**46.5**	

Source: Department of Finance, Revised Estimates for Public Services

4 This differs from Gross Domestic Product (GDP), which is a measure of output produced in Ireland. GNP differs from GDP by the net amount of incomes sent to or received from abroad. Historically GDP in Ireland exceeds GNP due to movements associated with foreign investment in Ireland. In 2010, GNP was 18% less than GDP.

Current Expenditure

1.9 The cost of administering central government services was estimated at €2.6 billion in 2010. This represents approximately 4.2% of the total programme expenditure[5]. Around 71% of the administrative costs is made up of the salaries of administrative staff.

1.10 Further salary costs are included in the cost of State services and programmes. In fact, the bulk of public services including teaching, healthcare and security is delivered through staff resources. The overall cost of human resources deployed in central government services in 2010 was of the order of €15.9 billion.

Capital Expenditure

1.11 Gross voted capital expenditure, before taking account of capital receipts, was approximately €6.3 billion in 2010. Most of this gross outlay was incurred on the following

- roads and public transport - €2 billion
- water services investment - €495 million
- social housing and estate regeneration - €746 million
- grants or assistance to private enterprise in the areas of agriculture and industry - €589 million
- building and equipping of education facilities - €616 million.

Movement in State Balances

1.12 The movements in balances associated with the financial outturn are set out in Figure 5.

5 Programme expenditure includes voted expenditure and expenditure from the National Training Fund and from the Social Insurance Fund.

Figure 5 Movements in State Balances, 2007 to 2010[a]

	2007 €m	2008 €m	2009 €m	2010 €m
State balance at 1 January				
Central Bank Exchequer Account	3,587	3,996	21,269	21,026
Commercial Deposits	–	490	790	790
	3,587	4,486	22,059	21,816
Movement in year				
Net Exchequer borrowing in year	2,518	30,287	24,397	12,493
Surplus/(deficit) of receipts over expenditure	(1,619)	(12,714)	(24,641)	(18,145)
	899	17,573	(244)	(5,652)
State balance at 31 December				
Central Bank Exchequer Account	3,996	21,269	21,026	11,399
Capital Services Redemption Account	–	–	–	600
Short Term Notes	–	–	–	3,585
Commercial Deposits	490	790	790	580
	4,486	**22,059**	**21,816**	**16,164**

Source: Finance Accounts 2007 to 2010

Note: a Excludes small balances in the CSRA: €842,000 (end 2007); €434,000 (end 2008) and €452,000 (end 2009).

Major Exchequer Liabilities and Assets

1.13 The State had certain long-term financial liabilities and assets at 31 December 2010 that are reported upon in other chapters in this report. The summary position in relation to key liabilities and assets is outlined below.

National Debt

1.14 The cumulative borrowing by the State at end December 2010 was €109.6 billion (at nominal or redeemable par values). Taking account of related assets of €16.2 billion, including a balance of €600.5 million on the CSRA, the net national debt at that date was €93.4 billion (2009: €75.2 billion).

1.15 During 2010, the Minister issued Promissory Notes to the value of €30.85 billion to three Irish financial institutions. Interest accrues on the amounts outstanding. Under the terms of the Promissory Notes, the State is required to pay the amounts due by way of annual instalments.

1.16 The General Government Debt (GGD) measures indebtedness taking account of all liabilities included in the national debt without offsetting of liquid assets together with other liabilities of the State including those relating to Promissory Notes, non-commercial State agencies and local authorities. At 31 December 2010, the GGD stood at €148 billion.

Financial Commitments Under PPP Contracts

1.17 Central government departments and agencies have entered into long-term public private partnership (PPP) deals for the provision of a range of services and infrastructure. These include commitments to future payments over the terms of the contracts.

1.18 The total value of the future commitments to be met in respect of contracts in place at the end of 2010 is estimated at €4.3 billion (€4.1 billion at the end of 2009). Further PPP projects are in the course of development or procurement, but financial commitments in respect of those projects will not arise until they reach formal contract stage. Part of this commitment represents the rolled up cost of future operation and maintenance, which in projects or services that are conventionally procured, are met on a 'pay as you go' basis.

Public Service Pension Costs and Liabilities

1.19 At end December 2009, a total of €116 billion had accrued in respect of occupational pensions payable to public servants. This is the latest assessment made. Those liabilities represent the estimated present value of the cash payments that fall to be met over the next 60 years in respect of pensions earned at 31 December 2009[6].

Pension Reserves

1.20 The NPRF has been valued at €22.7 billion on 31 December 2010.

1.21 The discretionary investment of the NPRF stood at €15 billion at 31 December 2010. These investments are valued at market prices. An additional €11.3 billion of the Fund's assets, including re-investment of dividends received from Allied Irish Banks Plc and Bank of Ireland, had been devoted to bank capitalisation by the end of 2010. The market value of the investments in the banks was €7.6 billion at 31 December 2010. Additional NPRF funds totalling €10 billion have since been committed towards bank stabilisation.

1.22 The valuation of assets of the NPRF that have been devoted to bank stabilisation payments is dealt with in Chapter 8.

State Commitments and Contingencies

1.23 As outlined in Chapter 4, the State has guaranteed the liabilities of certain Irish credit institutions. The value of the bank liabilities guaranteed at the end of December 2010 was of the order of €113 billion[7].

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6 See Chapter 3 of the Annual Report of the Comptroller and Auditor General on the Accounts of the Public Service 2009.

7 Deposits (up to a maximum of €100,000 per depositor per institution) are covered separately by a Deposit Guarantee Scheme. At the end of December 2010, such deposits with the credit institutions had a combined value of € 72 billion.

1.24 The State has a further commitment to meet any shortfall in the value of collateral under the Exceptional Liquidity Assistance (ELA) scheme. ELA of €49.5 billion advanced by the Central Bank of Ireland (CBI) at the end of 2010 was backed by collateral provided by the credit institutions availing of ELA. Collateral eligible for the purpose of ELA includes Promissory Notes issued by the Minister, loans including residential mortgages and investment or development loans as well as guarantees of the Minister. In addition, the CBI has received letters of comfort from the Minister. These confirm that any shortfall on the liquidation of collateral can be made good by the State.

Conclusion

The State deficit for 2010 was €18.15 billion. The period 2007 to 2010 has seen a decline in taxation receipts of around 4% when expressed as a percentage of Gross National Product (GNP). Over the same period, payments, increased from 31% to 42% of GNP.

At the end of 2010, the General Government Debt stood at €148 billion. In addition, the State had commitments of over €4 billion in respect of public private partnership contracts. Assets held by the State at the end of 2010 included €16.2 billion held as Exchequer assets and €22.7 billion in the National Pension Reserve Fund including €7.6 billion invested in Allied Irish Banks Plc and Bank of Ireland.

The latest estimates of long-term liability for occupational pensions for public sector employees was €116 billion at the end of 2009.

The State also had contingent liabilities arising out of its guarantee of the liabilities of certain Irish credit institutions and in respect of guarantees and letters of comfort issued to the Central Bank of Ireland for Exceptional Liquidity Assistance to banks.

The following chapters in the report deal with some of those issues in more detail

Chapter 2, National Debt

Chapter 3, State Funding Developments 2011

Chapter 4, Banking Stabilisation Measures

Chapter 6, Financial Commitments under Public Private Partnerships

Chapter 8, National Pensions Reserve Fund

Chapter 18, Vote Management.

Chapter 2

National Debt

National Debt

2.1 The net borrowing by the State at redeemable par values amounted to €93.4 billion at 31 December 2010. This liability is reported after taking account of related assets. Figure 6 sets out the gross and net borrowing levels over the past four years.

Figure 6 Net National Debt 2007 – 2010

	2007	2008	2009	2010
	€m	**€m**	**€m**	**€m**
Gross National Debt	42,047	72,457	96,968	109,609
Related Assets	(4,487)	(22,059)	(21,816)	(16,164)
Net National Debt	**37,560**	**50,398**	**75,152**	**93,445**

2.2 While €12.6 billion of the related assets was available to the State immediately or at short notice, €3.6 billion of Housing Finance Agency Commercial Paper cannot be readily realised. The National Treasury Management Agency (the NTMA) continued to purchase this Commercial Paper throughout the first half of 2011 due to the nature of that agency's funding needs.

2.3 The composition of related assets at 31 December 2010 is set out in Figure 7.

Figure 7 Related Assets 2007 – 2010

	2007	2008	2009	2010
	€m	**€m**	**€m**	**€m**
Capital Services Redemption Account	–	–	–	(600)
Housing Finance Agency Commercial Paper	–	–	–	(3,585)
Bank Deposits	(490)	(790)	(790)	(580)
Exchequer Account	(3,997)	(21,269)	(21,026)	(11,399)
Related Assets	**(4,487)**	**(22,059)**	**(21,816)**	**(16,164)**

2.4 The Exchequer balance fell from €21 billion at the end of 2009 to €11.4 billion at 31 December 2010, a drop of €9.6 billion which was accounted for by

- the purchase of €3.6 billion of Commercial Paper from the Housing Finance Agency (HFA)
- the transfer of €0.6 billion to the Capital Services Redemption Account
- the application of €5.6 billion towards funding the State deficit of €18.15 billion[8] offset by the liquidation of €0.2 billion in commercial deposits.

The balance of the State deficit was financed out of borrowing.

8 The gross deficit was €18.75 billion but €600 million of this was accounted for by a transfer to the Capital Services Redemption Account which is held in that account at 31 December 2010.

New Debt Instruments

2.5 As part of the process of bank capitalisation the State has also issued Promissory Notes. The net effect of this measure is to create State debt. The value of notes that had been issued at 31 December 2010 was €30.85 billion. In combination with direct State borrowing by the NTMA, the issue of Promissory Notes brought the overall gross central government debt to €140.46 billion before taking account of the other debt liabilities outlined in Figure 12.

2.6 The State does not have an immediate outlay of cash when it issues Promissory Notes. Interest is accrued annually on the Promissory Notes and is added to the outstanding balances at the end of March each year. Under the terms of the Promissory Notes, payments equal to 10% of the amounts outstanding at 31 December 2010 (€30.85 billion) are made annually on set dates[9], starting in 2011. The annual payments will continue until the principal amounts and all of the accrued interest have been paid.

Profile of National Debt

2.7 Net borrowings[10] by the NTMA in 2010 amounted to €12.5 billion (€24.5 billion: 2009). These were raised mainly through the issue of medium or long-term debt by means of auction and syndication. The cumulative borrowing is composed of a variety of elements with differing maturity profiles. Figure 8 sets out the breakdown of the debt by its major components.

Figure 8 Cumulative Borrowing at Redeemable Par Values

	2008	**2009**	**2010**
	€m	**€m**	**€m**
Government Bonds – maturity more than one year	41,863	70,858	90,102
Other Medium/Long-Term Debt – maturity more than one year	483	670	673
Short-Term Debt – maturity less than one year	21,783	16,261	6,972
Borrowings from other State Funds[a]	2,605	1,783	1,524
Government Savings Schemes – maturity of up to 5½ years	5,723	7,396	10,338
Gross National Debt	**72,457**	**96,968**	**109,609**

Note: a The main element of this borrowing relates to the Post Office Savings Bank Fund.

2.8 Most of the medium and long-term debt is borrowed in the form of government bonds which have differing maturities, the longest of which at the end of 2010 was fifteen years. Figure 9 compares the maturity profile of government bonds at the end of 2008, 2009 and 2010.

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9 The vast bulk of these are made in March each year.

10 The net borrowing, in this context, is the movement in the Gross National Debt.

Figure 9 Maturity Profile of Government Bonds

Duration	2008 €m	2009 €m	2010 €m
Under 5 years	15,931	25,687	28,298
5 to 10 years	11,857	29,296	53,520
Over 10 years	14,075	15,875	8,284
Total	**41,863**	**70,858**	**90,102**

2.9 Short-term debt which is debt with a maturity of less than one year, is comprised mainly of borrowings using Treasury Bills, the NTMA's Euro Commercial Paper Programme and Exchequer Notes. At the end of 2009, the NTMA held around €4 billion in US Commercial Paper. By the end of 2010, the amount held had fallen to around €50 million. Figure 10 sets out the maturity profile of short-term debt.

Figure 10 Maturity Profile of Short-Term Debt

Duration	2008 €m	2009 €m	2010 €m
Less than one month	3,880	4,561	2,186
One to three months	5,518	8,628	3,286
Three to six months	5,803	2,913	1,392
Over six months	6,582	159	108
Total	**21,783**	**16,261**	**6,972**

Debt Service Costs

2.10 The debt service cost disclosed in the NTMA's accounts for 2010 is €4.2 billion (2009: €3.2 billion) when measured on a cash basis. However, when account is taken of a transfer of €617 million (2009: €573 million) from current funds to a sinking fund[11] the current servicing outlay was €3.6 billion (2009: €2.6 billion).

2.11 Measurement of debt service costs on a cash basis masks the effect of servicing obligations which had accrued by year end but remained to be discharged. When the debt service cost is measured on an accruals basis[12], the servicing cost for 2010 was €4.2 billion (2009: €3.2 billion).

2.12 The gross national debt rose by 160% between the end of 2007 and the end of 2010. The cost of servicing the debt, when measured on an accruals basis, rose by approximately the same percentage.

Market Value of Debt

2.13 The net present value of the National Debt at the end of 2010 was €80 billion (€78.4 billion at the end of 2009). The present value of the debt reflects the total of all future cash flows (both interest and principal) discounted using the market rates at the end of the year.

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11 This sinking fund is used to repay debt.

12 The accruals basis recognises the costs incurred rather than those paid and does not take account of sinking fund movements.

General Government Debt

2.14 In addition to central government debt which comprised of borrowings reported in the financial statements of the NTMA and Promissory Notes issued by the State, further debt liabilities arise on foot of other public borrowing and funding activities. Taking account of these additional elements the overall public debt is €148 billion as set out in Figure 11.

Figure 11 General Government Debt 2007 – 2010

	2007	2008	2009	2010
	€m	€m	€m	€m
Gross National Debt	42,047	72,457	96,968	109,609
Promissory Notes	–	–	–	30,850
Other Debt Liabilities[a]	5,350	7,380	7,815	7,615
General Government Debt	**47,397**	**79,837**	**104,783**	**148,074**

Note: a Other debt liabilities are derived mainly from the preliminary return to the EU made in March 2010 under the single currency rules.

2.15 Other debt liabilities comprise a range of borrowings by State bodies and local government, related assets, as well as financial obligations of the State. The extent of those borrowings and obligations at the end of the last four years is summarised in Figure 12.

Figure 12 Other Debt Liabilities 2007 – 2010

	2007	2008	2009	2010
	€m	€m	€m	€m
Non-commercial State Bodies (including voluntary hospitals and HSE)	605	943	875	865
Housing Finance Agency	4,319	4,957	4,932	4,511
Intra Government Balances and Deposits	(2,840)	(3,116)	(2,084)	(1,654)
Post Office Bank Fund Deposits (excluding government bonds)	1,205	1,616	1,580	1,489
Local Government Debt (excluding debt due to central government)	550	599	825	791
Coinage	653	697	674	673
Accrued Interest on Savings Schemes	780	653	346	368
Westlink Buy-Out	–	534	482	433
Adjustment to Nominal Value of Debt [a]	23	489	55	72
National Loans Advance Interest	5	5	127	64
Miscellaneous	50	3	3	3
Total[b]	**5,350**	**7,380**	**7,815**	**7,615**

Source: Department of Finance

Notes: a General Government Debt reported to the EU is stated at nominal values. Where certain debt, such as Commercial Paper, is issued at a discount to its nominal value the General Government Debt figures must be adjusted to the nominal value.

b In addition, the State had future commitments of €4.3 billion in respect of Public Private Partnership contracts in place at end of 2010.

2.16 As a percentage of Gross Domestic Product (GDP)[13] the General Government Debt was 95% at the end of 2010. This is stated without taking account of related financial assets equivalent to 10.4% of GDP at 31 December 2010[14].

Conclusion

Overall, public borrowing increased to €148.1 billion at the end of 2010 with the Gross National Debt accounting for €109.6 billion of that liability. The balance is made up of Promissory Notes issued in connection with bank stabilisation (€30.9 billion) and other miscellaneous public borrowing of €7.6 billion. When account is taken of €16.2 billion in related assets the net public debt amounted to €131.9 billion at 31 December 2010.

The market value of Irish National Debt, on a net present value basis, was around €80 billion at 31 December 2010.

Debt service costs when measured on an accruals basis increased by €1 billion (or 31%) in 2010 principally due to the increase in the amount of the debt.

The State funding developments after 31 December 2010 are outlined in Chapter 3.

13 The ratio of General Government Debt to Gross Domestic Product (GDP) is a standard measure applied for purposes of comparison within the Eurozone.

14 The NTMA continued to maintain the advance funding it built up from 2008 onwards but it reduced to €11.4 billion by the end of 2010.

Chapter 3

State Funding Developments

Central Government

State Funding Developments

3.1 The yield on Irish bonds increased to almost 7% by the end of September 2010[15]. This made funding by way of longer-term borrowing overly expensive for the State.

3.2 The Minister for Finance announced on 30 September 2010 that the National Treasury Management Agency had decided not to proceed with bond auctions scheduled for October and November 2010. No further bond auctions or Treasury Bill auctions have been held since the announcement.

Chapter Focus

This chapter outlines

- the international background to the funding difficulties
- the international arrangements put in place to address Ireland's borrowing requirements
- the updated debt position at 31 July 2011
- the cost and burden of debt.

International Background

3.3 In the third quarter of 2008 the Euro Area entered its first recession as a result of the global financial crisis that commenced in 2007. The crisis bore more heavily on countries at the periphery. The impact on different countries varied depending on the scale of exposure to risky assets and the size of the financial sector, the export dependency of the economy and current account position as well as the extent to which house prices had been overvalued and construction industries oversized[16].

3.4 By late 2010, Ireland had reached a point where the cost of borrowing was challenging and a package of measures was negotiated with the International Monetary Fund (IMF), the European Union (EU) and the European Central Bank (ECB) and bilaterally with the United Kingdom (UK), Denmark and Sweden.

3.5 In December 2010, a programme of financial support from the EU and the IMF (the Programme) was put in place for Ireland. Under the agreement, Ireland can access up to €67.5 billion from the following sources

- IMF – Extended Fund Facility (EFF) — €22.5 billion
- EU – European Financial Stability Mechanism (EFSM) — €22.5 billion
- EU – European Financial Stability Fund (EFSF) — €17.7 billion
- Bilateral loans (UK, Sweden and Denmark) — €4.8 billion.

15 The yield is the return demanded by lenders or purchasers of Irish debt.

16 European Economic Forecast – Autumn 2010, European Commission.

The International Arrangements

The key instruments for the provision of facilities are

- Loans from the IMF – the Fund, which currently has 187 members, was created in 1945 to protect the stability of the international financial system. A member country can apply to the IMF for a loan if it cannot access finance to make international payments or maintain a safe level of reserves. Loan disbursements are dependent on the achievement of specific targets as set out in the country's programme of economic policies.
- The EFSM was established by EU finance ministers and came into being on 12 May 2010. To qualify for assistance under the EFSM, a member state must be either experiencing or be in serious threat of a severe financial disturbance caused by events beyond its control. The European Council makes the decision to grant the assistance. Economic policy conditions, established by the European Commission in liaison with the ECB, attach to the assistance. These are set out in a Memorandum of Understanding and must be complied with by the assisted member state.
- The EFSF is a company that was incorporated in Luxembourg on 7 June 2010 whose shareholders are the Euro Area states. A state that cannot borrow on capital markets at acceptable rates makes a request for assistance and negotiates a country programme with the European Commission and the IMF. The Euro Area finance ministers must accept the programme. A Memorandum of Understanding between the borrowing country and the European Commission is signed containing economic policy conditions. The EFSF issues bonds, or other debt instruments, on the market in order to raise funds to lend to applicant states.
- Bilateral loans from the UK, Denmark and Sweden.

3.6 The Programme does not preclude Ireland from seeking funding directly through the market. The yields on Irish bonds will be a key determinant of when Ireland returns to borrow in the market. The yield spreads[17] on Irish debt compared to those of Germany began to diverge substantially from mid-2010. The yields on 10-year Irish and German bonds for the period 2008 to mid-2011 are compared in Figure 13.

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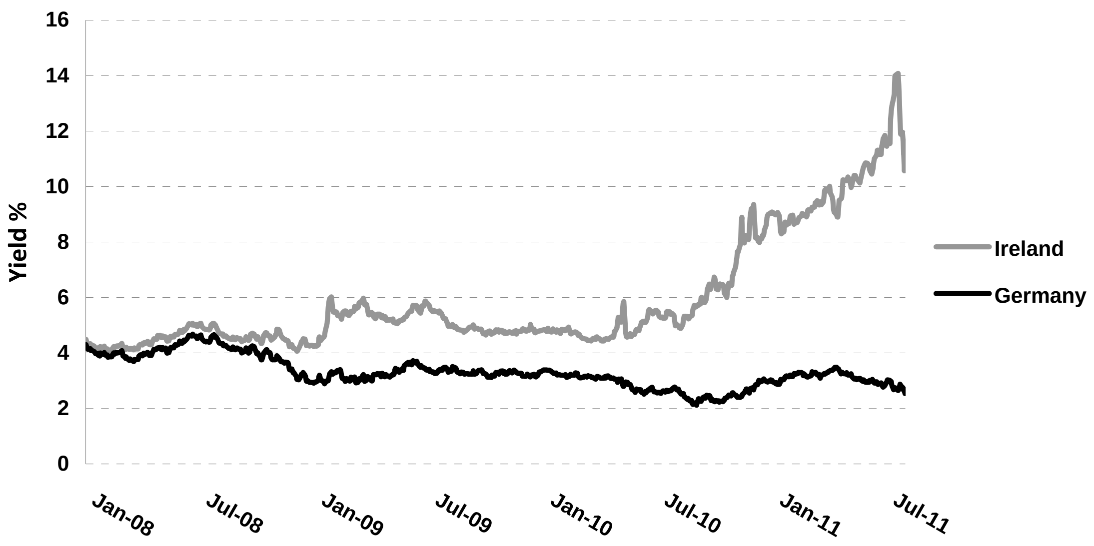
17 Yield spread is the difference between the yields on two bonds of the same maturity.

Figure 13 Irish and German 10-year Bond Yields 2008 to July 2011



Source: National Treasury Management Agency

National Recovery Plan

3.7 The Government published a National Recovery Plan (the Plan) on 24 November 2010. The Plan's objectives formed the basis for the fiscal policy and structural reform part of the Programme. The Plan provided for €15 billion in budgetary savings over the period 2011-2014 derived from expenditure cuts and tax increases of €10 billion and €5 billion respectively. These were the savings projected to be required to bring the budget deficit below 3% of GDP by 2015[18]. The Plan aims to return sustainable growth to the economy by

- setting out measures to be taken to restore order to the public finances
- identifying areas of economic activity that will provide growth and employment
- specifying Government reforms needed to accelerate growth in these key areas.

[18] The European Council had extended this target date from 2014 to 2015 on 7 December 2010.

EU-IMF Programme

3.8 The Programme, which was agreed with the European Commission, the ECB and the IMF, has two parts - the first dealing with fiscal policy and structural reform and the second dealing with bank restructuring and reorganisation[19]. The Programme's purpose is to

- provide a secure source of funding that can be availed of while the process of restoring sustainability to the public finances continues
- identify reforms to improve the economy's efficiency in order to enhance growth potential
- fundamentally restructure the banking system by downsizing, reorganising and recapitalising the banking sector so it is proportionate to the size of the economy and is capitalised to international standards
- introduce institutional reforms to improve the shock-absorbing capacity of the economy, a special resolution regime for banks, stronger supervision and greater budgetary oversight.

3.9 Progress in implementation of the policies under the Programme is monitored through quarterly reviews upon which the release of further funding depends. Ireland had successfully completed the first and second quarterly Programme reviews (the Spring review)[20] with the European Commission, the IMF and the ECB by May 2011[21]. The purpose of the quarterly reviews is to evaluate Ireland's performance against its assigned targets[22]. The review team reported following the Spring review that

- the economy is rebalancing away from domestic demand and towards net exports
- fiscal targets have either been met or are on track to be met
- steps have been taken towards structural reform objectives
- a comprehensive strategy to recapitalise, restructure and deleverage domestic banks has been developed based on thorough stress tests.

3.10 The team noted, however, that challenges still remain and that strict Programme implementation would be a crucial factor in Ireland returning to the capital markets at affordable interest rates.

3.11 A further quarterly review was carried out in July 2011. It was announced at the conclusion of the review mission that Ireland's compliance with the programme remained on track. The review will be formally concluded in September 2011 when the IMF Executive Board and Eurogroup/Ecofin[23] consider the appraisal reports on Ireland's performance prepared respectively by the IMF and the European Commission.

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19 The EU/IMF Programme of Support for Ireland is available on the Department of Finance's website.

20 The first and second quarterly reviews were combined and are referred to as the Spring review.

21 A revised Memorandum of Understanding between the European Commission and Ireland (May 2011) drawn up following the Spring review is available on the website of the Department of Finance.

22 Targets have been set for fiscal policy and structural reform as well as bank restructuring and reorganisation targets.

23 The Eurogroup comprises the Finance Ministers of the Eurozone while Ecofin comprises the Finance and Economic ministers of the member states of the EU.

National Debt at mid-2011

3.12 At the end of July 2011

- The gross national debt including borrowing under the Programme was €126.4 billion (December 2010: €109.6 billion).
- The State held €13.6 billion in related assets (December 2010: €16.2 billion).
- The net national debt was €112.8 billion (December 2010: €93.4 billion).

3.13 Net borrowing increased by €19.4 billion between January and the end of July 2011. The increased borrowing was applied for

- capitalisation of the banks arising from the Prudential Capital Assessment Review (PCAR) carried out by the Central Bank of Ireland to an amount of €7.6 billion[24]
- meeting Promissory Note payments of €3.1 billion in March[25] and
- funding a residual Exchequer deficit of €8.7 billion[26] in the period to 31 July 2011.

Details of the national debt at 31 July 2011 are set out in Figure 14.

Figure 14 Net National Debt Components - July 2011

Gross National Debt	**€m**	**€m**
Government Bonds – maturity more than one year	89,684	
Other Medium/Long-Term Debt – maturity more than one year[a]	22,924	
Short-Term Debt – maturity less than one year	870	
Borrowings from other State Funds	1,721	
Government Savings Schemes – maturity of up to 5½ years	11,237	**126,436**
Related Assets		
Exchequer Account	(6,500)	
Capital Services Redemption Account	(138)	
Bank Deposits	(3,182)	
Housing Finance Agency Commercial Paper	(3,786)	**(13,606)**
Net National Debt		**112,830**

Source: National Treasury Management Agency

Note: a Includes borrowing under the EU-IMF Programme.

24 If the assumptions underpinning the PCAR are borne out, no further Exchequer cash outlays (excluding annuities under Promissory Notes) should be required for bank capitalisation.

25 Annual payments of €3.1 billion will be made until the principal amount of the Promissory Notes (€30.85 billion) and accrued interest on the Notes has been repaid.

26 The deficit takes account of €460 million of net expenditure from the Capital Services Redemption Account.

3.14 By the end of July 2011, the State had drawn down just over €23 billion in funding under the EU/IMF arrangements. The funds were borrowed from the EFSM (€11.4 billion), the IMF (€7.4 billion) and the EFSF (€4.2 billion)[27].

3.15 The bulk of Irish borrowing at the end of 2010 was in the form of Government bonds. Government bonds constituted just under 60% of gross national debt at the end of 2008 rising to 82% at the end of 2010. This proportion had fallen by the end of July 2011, due to borrowing under the Programme which has increased the proportion of borrowing in classifications other than Government Bonds to 29% from 18% at the end of 2010.

3.16 The amount of short-term debt held has fallen in the last two years from 30% of gross national debt at the end of 2008 to 6.4% at the end of 2010 and, subsequently, to less than 1% at the end of July 2011.

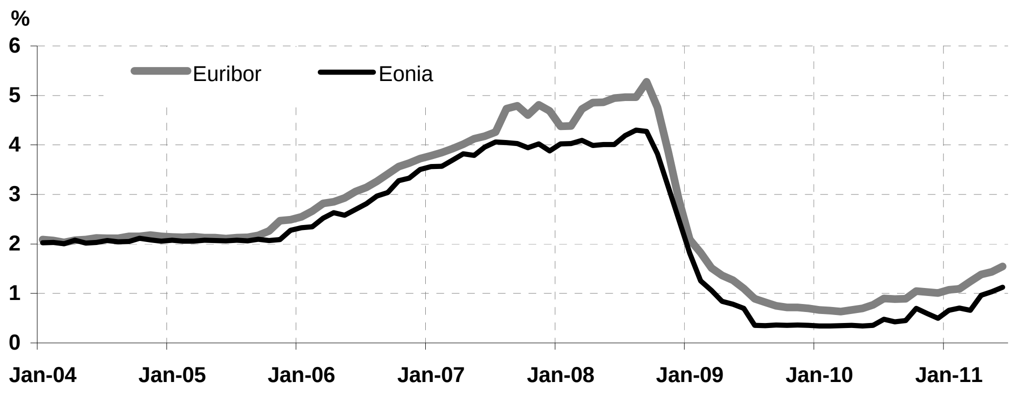
Ireland's gross national debt was €126 billion at the end of July 2011 and the Programme provides for further borrowings of around €45 billion.

Cost of Irish Borrowing

3.17 The cost of borrowing in recent years has been largely driven by the coupon rate on Government bonds. The weighted average[28] interest rate on Government bonds between the end of 2007 and end of July 2011 has risen from 4.41% to 4.64%.

3.18 The cost of short-term borrowing has varied significantly over the same time period. The average annual interest rate on short-term debt reflects market rates and has ranged from around 4% in 2007 and 2008 to around 1% as interest rates fell in 2009 and 2010. The amount of short-term debt has fallen from €22 billion at the end of 2008 to less than €1 billion at end of July 2011 and the fact those borrowings have been replaced with longer-term debt has caused an increase in the cost of servicing. Figure 15 shows the trends in key short-term rates[29] for the period from January 2004 to June 2011.

Figure 15 Eonia and 3-month Euribor Interest Rates 2004 to June 2011



Source: National Treasury Management Agency

27 The amount received by the State following pre-payment of some interest was €22.4 billion.

28 The weighted average coupon rate takes account the different rates at which debt was issued.

29 The Euro Overnight Index Average Rate (Eonia) and the three-month Euro Interbank Offered Rate (Euribor)

3.19 The interest cost on the various Government savings schemes has also varied. The two biggest savings schemes are Savings Certificates and Savings Bonds, which together accounted for around 80% of the total amount invested in Government savings schemes. The rates paid on savings bonds and savings certificates vary with the period of investment – at the end of June 2011, the highest rates on offer for those schemes were between 3.2% and 3.5%.

3.20 The weighted average effective interest rate for the loans drawn down under the EU-IMF Programme was 5.58% while the effective interest rates for the individual loans[30] ranged from 4.7% to 6.48%

- the effective interest rates for the IMF loans were 4.7% to 5.01% which take account of hedging undertaken by the NTMA – cross currency swaps undertaken to fix the exchange rate at which the loans will be repaid and interest rate swaps which were used to convert the IMF floating rate of interest to a fixed rate. The weighted average maturity of these loans was seven and a half years.
- the effective interest rates for the loans denominated in Euro were 5.54% to 6.48% (EFSM) and 5.9% (EFSF) taking account of fees and prepaid interest in the case of the EFSF funds[31]. The maturities of these loans range from just under five years to ten years and the higher interest rates apply to the loans with the longest maturities.

Taking into account the interest rates applying to all of the debt components, the weighted average interest rate being paid for the debt was just under 4.7% at the end of July 2011.

Ireland's Debt Burden

3.21 The level of debt relative to the economic output and taxation raised is indicative of the burden of public debt on the economy. Key debt indicators that are relevant to Ireland's capacity to generate resources to service and repay its debt include

- the ratio of net national debt to GDP which shows the level of debt relative to the economy's output
- the net national debt by comparison with taxation revenue which indicates the number of years of future taxation that would have to be devoted to debt repayment.
- the ratio of debt interest costs to taxation revenue which indicates the financial cost of the debt as a proportion of tax revenue.

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30 The variable rates pertaining on IMF loans when those loans were issued were 1.925% to 2.426%, while for other loans the rates were fixed at rates between 5.425% to 6.425% (EFSM) and 5.22% (EFSF).

31 In a statement following a meeting of the Heads of State or Government of the Euro Area on 21 July 2011, it was announced that the rate on EFSF loans to Greece would be reduced and that the maturity of future loans to Greece would be extended to a minimum of 15 years and up to 30 years with a grace period of 10 years. The statement noted that the EFSF lending rates and the maturities agreed for Greece would also be applied to Ireland and Portugal.

3.22 The salient facts relating to the change in these ratios since 2007 are

- the net national debt, as a proportion of GDP, rose from 20% to 60%
- this net debt represented 80% of taxation raised in 2007 and almost 300% by 2010 i.e. it constituted less than one year's taxation revenue in 2007 but by the end of 2010 it would require all tax revenue for three years to repay it.
- the proportion of taxation required to service the national debt rose from under 4% in 2007 to over 11% in 2010.

3.23 The trends in those indicators up to end 2010 are set out in Figure 16. The trend continued in 2011 due to further borrowing to meet debt stabilisation payments and fund the deficit.

Figure 16 Debt Indicators 2007 to 2010

Ratio	2007 %	2008 %	2009 %	2010 %
Net National Debt: GDP	19.8	28.0	46.8	59.9
Net National Debt: Taxation	79.5	123.6	227.4	294.3
Debt Interest: Taxation	3.5	4.0	8.0	11.4

Views of the Department

3.24 In regard to the debt burden, the Accounting Officer stated that the sharp downturn in economic activity since 2007, three years of large budget deficits and the significant level of State support required for the banking sector have combined to drive the ratio of Irish Government debt to GDP up steeply. He noted that a continuation of this upward trajectory is not sustainable and the debt ratio must be stabilised and returned to lower, safer levels as quickly as possible. The evolution of the debt ratio depends on the relationship between economic growth, the interest rates applying to Government debt - both the stock outstanding and new debt - and the level of budgetary adjustment.

3.25 The Accounting Officer pointed out that a crucial requirement for debt sustainability is that the ratio of debt to GDP stabilises and starts to come down. Based on the economic and fiscal forecasts contained in the Stability Programme Update (SPU) which was published by the Department in April 2011, the General Government debt[32] to GDP ratio[33] is expected to peak at 118% in 2013, before declining to 111% by 2015. He stated that the narrowing of the gap that exists between revenues and expenditure through additional fiscal consolidation, together with the implementation of policy measures that will assist in boosting economic growth will help in this regard, as will the achievement of a primary surplus – an excess of revenues over expenditure excluding interest expenditure – by 2014.

3.26 In addition, the Accounting Officer pointed out that on the basis of the SPU forecasts, some 21% of tax revenues will be required to pay interest on the national debt by 2015. While a significant level, it is below the ratio experienced in the mid-1980s when around a third of the tax revenues generated in the State went towards servicing the interest on the national debt.

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32 The General Government Debt measures indebtedness taking account of all liabilities included in the national debt without offsetting liquid assets, together with other liabilities of the State including Promissory Notes, non-commercial State agencies and local authorities.

33 In 2010, the General Government Debt to GDP ratio was 95%, up from 65% in 2009.

Conclusion

In December 2010, having withdrawn from borrowing on the markets following the increase in yields on Irish government bonds, an EU/IMF Programme of Financial Support was negotiated by Ireland. Under the Programme, Ireland can access up to €67.5 billion in external borrowing.

In November 2010, the Government approved a National Recovery Plan, which forms the basis for the fiscal and structural reform part of the Programme. Progress in implementing policies under the Programme, which also provides for bank restructuring is monitored by way of quarterly reviews by the European Commission, the ECB and the IMF. The first reviews have been successfully completed.

By the end of July 2011, the net national debt stood at €112.8 billion, an increase of a further €19.4 billion since December 2010. The associated borrowing was applied as follows

- €7.6 billion to meet the capitalisation requirements of the banks following the Prudential Capital Assessment Review carried out in 2011
- €3.1 billion in respect of financial obligations under Promissory Notes issued by the State
- €8.7 billion to fund the residual Exchequer deficit for the period to the end of July 2011.

The weighted average interest rate on Irish Government bonds, which comprised the bulk of debt to the end of 2010, has risen marginally in the period since 2007 to around 4.64%. During 2009 and 2010, the amount of short-term debt, which generally carries lower interest rates than Government bonds, has fallen sharply and been replaced with longer-term debt with a consequent increase in the overall cost of servicing the debt.

The effective interest rates charged for borrowing under the EU-IMF Programme averaged 5.58% and have ranged between 4.70% and 6.48% for the amounts drawn to date. The lowest rate applies to the IMF loans while for the EFSF and EFSM loans, higher interest rates apply to the loans with the longer maturities.

At the end of July 2011, the weighted average interest rate for the total debt was just under 4.7%.

By the end of 2010, the net national debt stood at around 60% of GDP and around three times the amount of tax revenues in 2010. In 2010, over 11% of tax revenues was applied in the payment of interest on the national debt.

Chapter 4

Banking Stabilisation Measures

Central Government

Banking Stabilisation Measures

4.1 Previous reports have outlined the measures taken to stabilise the banking system and its institutions in Ireland since the onset of the financial crisis of 2008. In 2010, and the first half of 2011 the State has continued this process through recapitalisation of banks, provision of guarantees of deposits and certain liabilities and through the provision by the Central Bank of Ireland (CBI) of liquidity to financial institutions domiciled in Ireland. As a result of the scale of capital injections, by mid 2011 the State had a controlling shareholding in Anglo Irish Bank Corporation (Anglo), Allied Irish Banks plc (AIB), Irish Nationwide Building Society (INBS) and EBS Building Society (EBS).

Chapter Focus

The purpose of this chapter is to

- outline the banking stabilisation measures taken
- set out the post-restructuring base value of the banks based on the assumptions in the Financial Measures Programme
- outline the State's liabilities under guarantee schemes
- set out the extent of liquidity support to the banking sector
- report the cost of consultancy related to stabilisation measures
- outline the credit availability measures taken to date
- review the arrangements for managing the State's investments in the banks.

Measures to Strengthen Banking Institutions

4.2 Measures taken to address the financial stability of credit institutions in Ireland have included

- purchase of impaired bank assets
- capitalisation of certain credit institutions
- guarantee of certain liabilities of credit institutions and
- liquidity support.

Purchase of Impaired Bank Assets

4.3 The National Asset Management Agency (NAMA) was established to acquire loans that had been advanced for the purchase and development of land and other related advances from five credit institutions that participated in the NAMA scheme[34].

4.4 By the end of 2010, NAMA had paid €30.2 billion to banks to purchase loans where the borrowers owed just over €71 billion. The loss incurred by the credit institutions on the loans was of the order of €41 billion, or almost 58%. NAMA issued debt to pay for the loans. 95% of the payment was in the form of Floating Rate Notes guaranteed by the Minister for Finance (the Minister). The NAMA Financial Statements in respect of 2010 reported a further impairment provision of €1.5 billion on the loans it acquired.

Capitalisation of Credit Institutions

4.5 By the end of 2010, the State had made capital injections of almost €47 billion into five Irish credit institutions. In March 2011, a Financial Measures Programme (FMP) Report published by the CBI identified a need for up to a further €20 billion of capital assistance for those five institutions and a requirement for up to €4 billion for a further institution.

4.6 By the end of 2010, the State's investment comprised

- €16 billion in new investment and
- €31 billion by way of Promissory Notes.

4.7 Figure 17 provides details of the capital injections made up to the end of 2010 and the extent of the projected future further capital requirements as determined under the FMP.

Figure 17 Capitalisation of Credit Institutions, December 2010

Credit institution	Cost of share acquisition [a]	Cost of preference shares	Value of Promissory Notes issued	Total capital provided to 31 December 2010	Future capital needs	Total capital requirement
	€bn	€bn	€bn	€bn	€bn	€bn
Anglo	4.00	–	25.30	29.30	–	29.30
AIB	4.10	3.50	–	7.60	13.30	20.90
Bank of Ireland	1.91	1.84	–	3.75	5.20	8.95
INBS	0.10	–	5.30	5.40	–	5.40
EBS	0.63	–	0.25	0.88	1.50	2.38
Irish Life and Permanent	–	–	–	–	4.00	4.00
Total	**10.74**	**5.34**	**30.85**	**46.93**	**24.00**	**70.93**

Source: Department of Finance
Note: a Ordinary shares acquired are included at cost. The investment in ordinary shares includes dividends received in the form of ordinary shares from AIB (€280 million) and Bank of Ireland (€250 million) in 2010.

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[34] The five credit institutions were Anglo, AIB, Bank of Ireland, INBS and EBS.

Assessments of Banks' Capital Requirements

4.8 In March 2010, following a Prudential Capital Assessment Review (PCAR)[35], the Financial Regulator determined a target capital ratio for banks of 8% for Core Tier 1 capital[36]. In December 2010, the joint EU/IMF Programme outlined in Chapter 3 noted that a further PCAR would be carried out in 2011 based on criteria to be determined by the CBI in consultation with the European Commission, the European Central Bank (ECB) and the International Monetary Fund (IMF). The assessment would be carried out under two scenarios – a baseline scenario and a stress scenario[37].

4.9 Under the new PCAR (PCAR 2011), banks would be required to meet a minimum Core Tier 1 capital ratio of 10.5% under the baseline scenario and 6% under the stress scenario. Under the EU/IMF Programme €35 billion of funding was made available for the recapitalisation of the banks.

4.10 In March 2011, the CBI published the FMP Report, which comprised

- an independent loan loss assessment exercise carried out for the CBI by BlackRock Solutions (BlackRock)
- the results of PCAR 2011
- the results of a further Prudential Liquidity Assessment Review (PLAR) to establish funding targets for banks subject to PCAR 2011.

4.11 In summary, the reviews reported in the FMP Report concluded that a further €24 billion of capital was required[38]

- The minimum amount of capital that the banks would be required to generate in order to meet the Core Tier 1 capital ratio targets was €18.7 billion on the basis of the combined results of three-year stress losses (up to end-2013) derived from the BlackRock and PCAR analyses.
- A further €5.3 billion by way of a capital buffer was added by the CBI to take account of the possible emergence of losses after 2013.
- In order to meet the funding targets under PLAR, the banks would be required to deleverage by disposing of non-core assets in order to achieve a target loan-to-deposit ratio of 122.5% by the end of 2013. The Report anticipated that the banks' losses from these disposals could amount to €13.2 billion before taking account of related loan impairment provisions already recognised by the banks. These projected losses were taken into account when calculating the capital requirements.

4.12 The €24 billion capital that the banks were required to raise could be provided either directly by the State or from private capital sources including, for example, new capital from shareholders, burden sharing with subordinated bondholders or the disposal of assets.

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35 PCAR is an annual stress test of the capital resources of domestic banks under a given stress scenario undertaken in order to calculate the extent of capitalisation necessary to meet CBI requirements.

36 Core Tier 1 capital generally comprises share capital, capital contributions, retained earnings and certain preference shares.

37 Baseline scenarios are built on assumptions about key economic variables – for example, Gross Domestic Product, unemployment rates, inflation and property prices over the period of the review. The stress case scenario assesses capital needs against a deterioration from the baseline forecast. The FMP Report noted that, to ensure clarity and consistency, the PCAR scenarios were to a large degree in line with the 2011 European Banking Authority stress tests on European banks.

38 Four credit institutions were included in the reviews – AIB, Bank of Ireland, EBS and Irish Life and Permanent. Anglo and INBS were not included as their loan books are being wound down.

Restructuring of the Banking System

4.13 In March 2011, the Minister announced that the Irish banking system would have two full-service banks (Bank of Ireland and AIB/EBS) as its core pillars as well as a restructured Irish Life and Permanent (ILP).

4.14 On 24 February 2011, following a High Court order, €8.5 billion of deposits were transferred from Anglo to AIB and €3.6 billion of deposits were transferred from INBS to ILP. AIB and ILP also received assets supporting these liabilities comprising Senior NAMA bonds and Irish Government bonds together with Government guaranteed bonds issued by Irish financial institutions.

4.15 On 1 July 2011, AIB completed the acquisition of EBS to form one of the two pillar banks in Ireland. The Minister approved the acquisition under Section 7(11) of the Credit Institutions (Financial Support) Act 2008 on the basis that the result of the acquisition will not be to substantially lessen competition in the Irish banking market. On the same day, under Section 34 of the Credit Institutions (Stabilisation) Act 2010, the High Court ordered the transfer of all assets and liabilities of INBS to Anglo.

4.16 On 28 April 2011, the Minister for Finance and the Governor of the CBI wrote to the IMF, the European Commission and the ECB about progress in implementing the EU/IMF Programme. In the 'Memorandum of Understanding on Specific Economic Conditionality' accompanying the letter it was noted, *inter alia*, that

- the Irish authorities would ensure that the capital needs identified in PCAR 2011 would be fully met by 31 July 2011
- actual and forecast loan to deposit ratios would be reported to the CBI every six months
- the Department of Finance (the Department) would, by 31 July 2011, introduce legislation enhancing the powers of the CBI to intervene in the financial system when fulfilling its role as supervisor.

4.17 Following the enactment of this legislation, the CBI will have the power to enforce the implementation of a loan to deposit ratio of 122.5% as well as the power to direct the banks to sell assets.

4.18 By the end of July 2011, the capital requirements identified in PCAR 2011 had been substantially met

- The State invested €17.66 billion in capital in the newly merged AIB/EBS, Bank of Ireland (BoI) and ILP. €10.08 billion of the funds were sourced from the National Pensions Reserve Fund (NPRF) and €7.58 billion were sourced from the Exchequer.
- The three credit institutions had raised €4.9 billion by way of a number of measures including the repurchase of subordinated debt, the issue of new shares and rights issues.

4.19 Figure 18 provides details of the implementation of the bank recapitalisation programme under PCAR 2011.

Figure 18 Capitalisation of Credit Institutions, PCAR 2011

Credit institution	State investment			Capital raising measures to date[a]	Total capital requirement
	Cost of share acquisition	Cost of Contingent Capital Notes	Cost of capital contribution		
	€bn	€bn	€bn	€bn	€bn
AIB/EBS	5.00	1.60	6.05	2.15	14.80
BoI	1.31	1.00	–	2.55	4.86
ILP	2.30	0.40	–	0.2	2.90
Total	**8.61**	**3.00**	**6.05**	**4.9**	**22.56**

Source: Department of Finance

Note: a These included the repurchase of subordinated debt, private investments and other internal capital raising exercises implemented by end July 2011. Anticipated further capital raising measures by BoI and ILP will bring bring the capital raised to just over €24 billion.

4.20 In addition to the investment of €8.61 billion in ordinary shares, the State provided a further €9.05 billion in capital

- €3 billion in contingent capital - this capital will convert to ordinary shares if the Core Tier 1 capital ratio in an institution falls to 8.25% and
- a capital contribution of €6.05 billion to AIB/EBS.

4.21 Following the July 2011 investments, the total State investment in the capitalisation of the banks stood at €64.88 billion[39].

4.22 Under a direction from the Minister, the NPRF will dispose of part of its shareholding in BoI to a group of institutional investors for €1.05 billion. Following this sale, the total amount of capital provided by the State to the credit institutions will be of the order of €63.83 billion.

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39 Including the reinvestment of dividends totalling €0.29 billion received in the form of ordinary shares from AIB in 2011.

Base Value of Bank Businesses

4.23 The key assumptions relative to the base value of the banks following their restructuring as set out in the FMP Report were

- a further €24 billion would be provided to banks by way of capital[40]
- in the period to 2013, the banks will incur losses of between €33 billion and €41 billion of which around €10 billion had been provided for by the banks in the form of loan impairment provisions at the end of 2010
- €20 billion to €27.7 billion[41] of the projected losses will be incurred in the normal course of their business and €13.2 billion from deleveraging through the disposal of certain assets in order to achieve the liquidity ratio targets set out in the PLAR.

4.24 Overall, the assumptions in the FMP Report are consistent with something of the order of €13.7 billion to €21.4 billion being available by 2013 as Core Tier 1 capital in those banks in which the State has invested. Under accounting norms, this capital would represent an equivalent amount of assets.

4.25 This asset value would accrue to the shareholders and the amount attributable to the State investment will be proportional to its shareholding. On foot of the recapitalisation transactions in July 2011, the State owns almost all of AIB and ILP. Following the sale of shares to a group of institutional investors and completion of BoI’s liability management exercise, the State will own 15% of that institution.

4.26 The residual value of the capital injections that the State has made into Anglo and INBS will be dependent on the amounts realised from the disposal of the assets in the merged entity.

Liabilities under Guarantee Schemes

4.27 Certain liabilities of banks have been guaranteed by the State under three main schemes

- a Deposit Guarantee Scheme covering deposits up to a value of €100,000 per depositor per institution
- the Credit Institutions (Financial Support) Scheme which provided a two-year State guarantee in respect of a wide range of banking liabilities from September 2008 to September 2010
- the Eligible Liabilities Guarantee Scheme, which provides a State guarantee from 9 December 2009 for a narrower range of banking liabilities.

40 The CBI made its decision on the required capitalisation based on loan-loss projections of BlackRock along with further calculations based on the prospective income, expenditure and deleveraging plans of the banks.

41 Projected losses are €20 billion under the baseline scenario and €27 billion under the stress scenario.

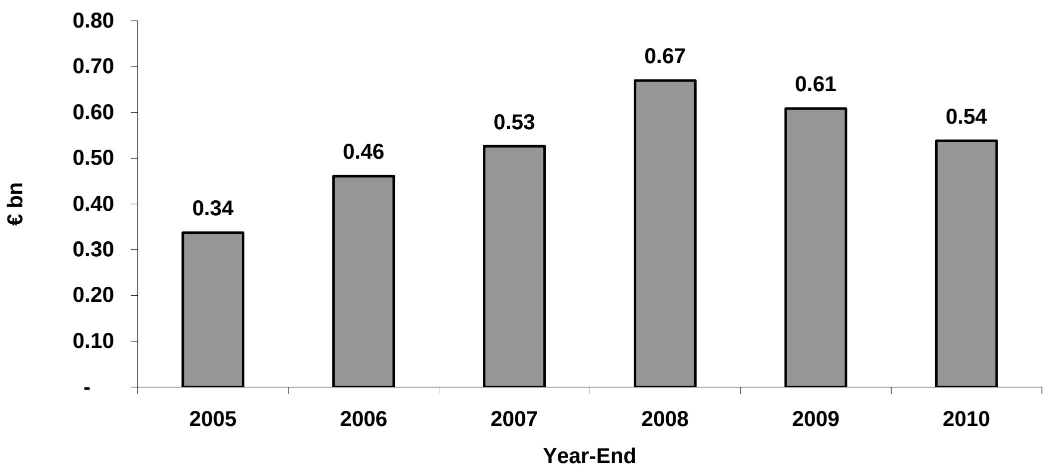
Deposit Guarantee Scheme

4.28 Under the Deposit Guarantee Scheme, deposits by individuals in credit institutions that are licensed to receive deposits in Ireland and are authorised by the CBI are guaranteed up to a limit of €100,000 per eligible depositor per institution[42].

4.29 Credit institutions subject to the provisions of the scheme are required to deposit funds, to the value of 0.2% of all current customer deposits held by the institution, in a Deposit Protection Account administered by the CBI. Any claims of depositors under the scheme would be met in the first instance from the resources of the Deposit Protection Account and any residual shortfall would then be met from the Central Fund of the Exchequer, which would be recouped in due course from the banking sector. No claims have been made under the scheme since its inception.

4.30 At the end of 2010, 47 credit institutions were subject to the provisions of the scheme with the balance in the Deposit Protection Account being €0.54 billion. Comparative balances for the years 2005 to 2009 are also provided in Figure 19.

Figure 19 Deposit Protection Account Balance Movements from 2005 to 2010



Source: CBI Statement of Accounts for the years ended 2005 to 2010

4.31 The extension of the scheme included a provision that credit union deposits would subsequently be covered and the legislation provided for this. However, an order has not yet been made requiring credit unions to hold funds in the Deposit Protection Account.

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42 The legal basis for the change from the previous limit of €20,000 was provided through the Financial Services (Deposit Guarantee Scheme) Act 2009.

CIFS Bank Guarantee Scheme

4.32 The Credit Institutions (Financial Support) Scheme (the CIFS Bank Guarantee Scheme), which commenced in September 2008[43], provided a guarantee for a broad range of bank liabilities for the seven institutions (covered institutions)[44] that opted to avail of the scheme.

4.33 The covered institutions were required to make quarterly payments to compensate the State for the scheme's impact on the cost of State borrowing. By mid-2011, just over €759 million had been received from the credit institutions under the scheme. A special account was set up at the CBI into which the covered institutions lodged their payments. The account earned interest of over €4 million which was also transmitted to the Exchequer.

4.34 The balance of this account was held as a reserve to cover any payments to be made under the scheme. Subsequent to the expiry of the scheme on 29 September 2010, the account's balance of almost €761 million was paid over to the Exchequer in October 2010. Subsequent payments amounting to just over €3 million had all been paid over to the Exchequer by April 2011.

4.35 Following the expiration of the CIFS Bank Guarantee Scheme, covered institutions can no longer make calls under the guarantee in respect of defaults of their obligations under covered liabilities.

Eligible Liabilities Guarantee Scheme

4.36 The Eligible Liabilities Guarantee Scheme (ELG scheme) came into effect on 9 December 2009. It was designed to provide a longer-term guarantee of certain banking liabilities and to bring the Irish bank guarantee structure more into line with guarantees in other EU member states.

4.37 The ELG scheme requires approval every six months from the European Commission under EU State aid rules. The scheme was initially approved in December 2009, and renewed approval has been given every six months, most recently in June 2011. This approval means that eligible debt securities and deposits issued or rolled over on or before 31 December 2011 will be guaranteed under the scheme up to a maximum maturity of five years.

4.38 The scheme is administered by the National Treasury Management Agency (the NTMA) on behalf of the Minister. The NTMA approved the participation of six of the credit institutions covered under the CIFS Bank Guarantee Scheme (including certain subsidiaries) in the new scheme[45].

4.39 The institutions participating in the ELG scheme pay a fee for the cover they receive, but at a higher level than provided for under the CIFS Bank Guarantee Scheme. The pricing is designed to encourage the institutions to reduce their reliance on State support over time.

4.40 The payment level for liabilities depends on factors such as the maturity profile and amount of the liabilities, and is based on ECB recommendations on pricing government guarantees of banking liabilities. For instance, an annualised fee of 0.5% applies to short-term debt (i.e. with a maturity of up to one year). For longer-maturity debts, an additional fee (based on the credit default swap rating of the institution prior to the banking crisis) is also applied. Since 1 July 2010, further additional fees of between 0.2% and 0.4% (depending on the credit rating of the institution) apply on all covered liabilities.

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43 The legal basis for the scheme was provided through the Credit Institutions (Financial Support) Act 2008, which was signed into law on 2 October 2008.

44 AIB, Anglo, BoI, EBS, ILP, INBS and Postbank Ireland Limited.

45 AIB, Anglo, BoI, EBS, ILP and INBS.

4.41 Fee payments by the institutions are made into a designated account at the CBI. These receipts accrue to the Exchequer and are not held in a reserve. Fees collected to the end of July 2011 amounted to €1.54 billion. Interest which is paid twice yearly in April and October amounted to just over €1 million to end July 2011. €1.17 billion had been paid over to the Exchequer by end of July 2011.

4.42 In response to my enquiries about delays in the payover of fees to the Exchequer, the Department stated that the ELG scheme was silent on the timing of the transfer of fees received from the participating institutions, unlike the CIFS Bank Guarantee Scheme which required that the scheme's account at the CBI should operate as a reserve account for the duration of the scheme. The Department advised that for the period when the two schemes were in operation it treated the fees received under the ELG scheme in the same manner – it allowed the fees to accumulate in the ELG account at the CBI. The Department also stated that the termination of the CIFS Bank Guarantee Scheme in September 2010 triggered the payment of fees collected under that scheme to the Exchequer and that the Department then decided to transfer the fees received under the ELG scheme with the transfer taking place in late October 2010. The Department pointed out that it has since regularised procedures for the transfer of ELG scheme fees to the Exchequer on a quarterly basis with the first quarterly transfer having taken place in April 2011.

Aggregate Value of Covered Liabilities

4.43 Figure 20 indicates the estimated total value of the liabilities covered by the guarantee schemes at the end of each quarter from December 2008 to June 2011.

Figure 20 Estimated Value of Guaranteed Liabilities of Covered Credit Institutions, December 2008 to June 2011

	Banking liabilities covered by			Total value of guaranteed liabilities
	Deposit guarantee[a]	CIFS Bank guarantee	Eligible Liabilities Guarantee	
	€bn	€bn	€bn	€bn
End Quarter 4 2008	82	346	–	428
End Quarter 1 2009	79	293	–	372
End Quarter 2 2009	79	276	–	355
End Quarter 3 2009	78	287	–	365
End Quarter 4 2009	77	281	–	358
End Quarter 1 2010	77	130	139	346
End Quarter 2 2010	78	103	153	334
End Quarter 3 2010	62	–	131	193
End Quarter 4 2010	72	–	113	185
End Quarter 1 2011	76	–	111	187
End Quarter 2 2011	74	–	123	197

Source: Department of Finance

Note: a This relates only to eligible deposits in the institutions that were covered by the CIFS Bank Guarantee Scheme.

Liquidity Support for Banks

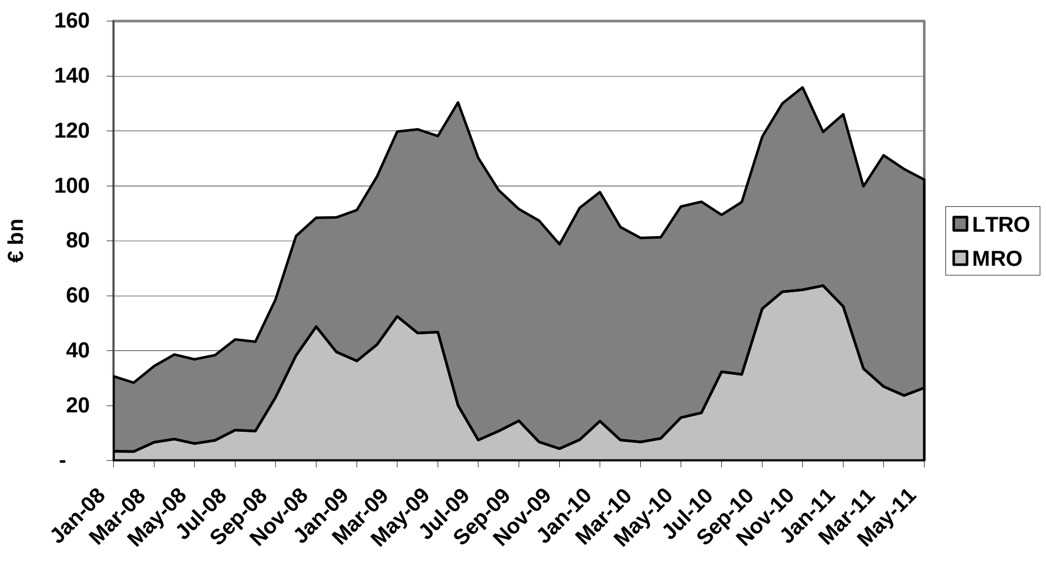
4.44 The CBI, through Eurosystem monetary policy operations, provides liquidity to the banking sector in the form of advances to credit institutions based in Ireland (including credit institutions based in the Irish Financial Services Centre). All the advances are secured by collateral approved by the Eurosystem. In practice, the Eurosystem has, since October 2008, provided as much liquidity as banks have sought[46]. The credit institutions whose loans were acquired by NAMA can use the Floating Rate Notes they received as consideration for the loans to obtain collateralised liquidity from the Eurosystem under monetary policy operations as the Notes qualify as eligible collateral. Both retail and international banks can avail of Eurosystem liquidity through the CBI.

4.45 Advances under the Eurosystem fall into two broad categories

- The Main Refinancing Operations (MRO) comprise weekly offers of loans with a maturity of one week
- The Long Term Refinancing Operations (LTRO) comprise mainly monthly offers of loans with a maturity of three months. In 2008, loans with a maturity of six months were added and in 2009 loans with a maturity of 12 months were added. The last of these loans matured in 2010. In August 2011, an LTRO offering loans with a maturity of approximately six months (maturing on 1 March 2012) was announced.

4.46 As Figure 21 indicates, Eurosystem lending to credit institutions increased significantly from €31 billion at the end of January 2008 to a peak of €130 billion at the end of June 2009. Subsequently, the level of liquidity support fell, fluctuating in the range of €80 billion to €100 billion from August 2009 before rising again and peaking in November 2010 at a high of €136 billion. Since April 2011 the level of borrowing has levelled off at just over €100 billion and it stood at €103 billion at the end of June 2011. The drop in demand for liquidity coincided with the placement of around €19 billion of State funds on deposit with Irish commercial banks (€10 billion by the NPRF and €9 billion from Exchequer funds).

Figure 21 Eurosystem Lending to Credit Institutions, January 2008 to June 2011



Source: CBI Monthly Money and Banking Statistics

46 The level of Eurosystem lending is limited, however, by the amount of available eligible collateral held by banks.

4.47 In addition to liquidity provision within the Eurosystem monetary policy operations, the CBI also provides Exceptional Liquidity Assistance (ELA) to domestic credit institutions where required. The CBI reports ELA lending as part of ‘Other Assets’ in its balance sheet. In its annual Statement of Accounts it reported that the amount of ELA advanced at the end of 2009 was €11.5 billion (90% of ‘Other Assets’) and €49.5 billion (98% of ‘Other Assets’) at the end of 2010. During 2011, the ‘Other Assets’ figure increased to €70 billion in February and had fallen back to €56 billion at the end of June.

4.48 As with the Eurosystem monetary policy operations the ELA lending must be collateralised. The collateral provided by the banks availing of ELA includes Promissory Notes issued by the Minister, loans including residential mortgages and investment or development loans and guarantees of the Minister[47]. In addition, the CBI has received letters of comfort from the Minister. These confirm that any shortfall on the liquidation of collateral can be made good by the State.

Consultancy Costs

4.49 The State, through the Department of Finance, the CBI, the NTMA and the NPRF has used the services of advisors in the course of developing and implementing the measures aimed at stabilising the banking sector. By the end of June 2011, over €73 million had been paid on foot of consultancy costs. Figure 22 sets out the costs incurred, classified by the measure for which the related service was provided.

Figure 22 Consultancy Costs Classified by Nature of Service Provided

Phase of Stabilisation	2008 €m	2009 €m	2010 €m	2011 €m	Total €m
Recapitalisation, Restructuring and Guarantees	6.473	14.235	12.021	6.863	39.592
Financial Measures Programme	–	–	–	22.864	22.864
Crisis Management	0.036	2.012	0.338	0.016	2.402
Other[a]	0.026	2.357	1.771	1.392	5.546
NAMA[b]	–	2.042	0.462	0.090	2.594
Banking Crisis Inquiry	–	0.084	0.154	0.126	0.364
Total	**6.535**	**20.730**	**14.746**	**31.351**	**73.362**

Sources: CBI, NTMA, Department of Finance and the NPRF

Notes: a Other advice includes advice in respect of bank nationalisation, Credit Unions, liquidity assistance and advice of a general nature.

b NAMA related costs are those incurred by the CBI, the NTMA and the Department of Finance. Costs incurred directly by NAMA are not included.

4.50 The highest level of costs were incurred in respect of financial advice (€35.1 million) followed by legal services (€22.5 million) and accounting-related services (€15.6 million). Details of the costs incurred each year and the commissioning Department or agency are set out in Figure 23.

[47] Where appropriate discounts have been applied to the collateral by the CBI.

Figure 23 Agency Consultancy Costs Classified by Type

Consultancy Type	CBI €m	NTMA €m	Department of Finance €m	NPRF €m	Total €m
Financial services	19.555	15.360	0.076	0.146	35.137
Legal services	1.876	5.184	13.000	2.418	22.478
Accountancy services	13.734	0.223	0.100	1.580	15.637
Other services	–	–	0.110	–	0.110
	35.165	**20.767**	**13.286**	**4.144**	**73.362**

Sources: CBI, NTMA, Department of Finance and the NPRF

Credit Availability Measures

4.51 From the initial provision of support for the recapitalisation of AIB and BoI, a number of credit requirements directed at supporting small and medium sized enterprises (SMEs) and entrepreneurs have been set. This included a requirement for both banks to make available more than €3 billion each in new SME lending, to include working capital, in 2010 and 2011 (a total of €12 billion).

4.52 As part of the recapitalisation agreement, the Government established the Credit Supply Clearing Group, chaired by the Department of Enterprise, Trade and Innovation, in May 2009 with bank, business and State representation. Its role was to identify credit supply solutions where the flow of credit to viable businesses appeared to be blocked. The Group was responsible for the publication of 'Your Business, Your Bank' in December 2010 designed to help viable small businesses develop better relationships with banks and gain access to credit to grow and create jobs.

Credit Review Office

4.53 The Credit Review Office (CRO)[48] was established in March 2010, to help ensure that credit is not refused to viable businesses with valid business propositions. As an independent body, it has no regulatory or statutory powers to override banks' lending decisions but gives an independent opinion on banks' credit decisions. Banks are required to comply with the CRO recommendations or explain why it would not be appropriate to do so.

Review of Banks' Lending Targets

4.54 The CRO publishes quarterly reports, which include a general summary on each bank's lending outcomes outlining specific packages and supports provided. The quarterly report in May 2011, covering the period from April 2010 to March 2011, noted that each bank had exceeded the target of sanctioning €3 billion in lending and that, taken together, the cumulative amount of lending sanctioned was just over €8 billion. The amount actually loaned to customers is not tracked in those reports.

48 The enabling legislation is in the guidelines issued under Section 210 (1) of the National Asset Management Agency Act 2009 relating to the review of decisions of participating institutions to refuse credit facilities.

4.55 In the CRO Report, the Credit Reviewer noted that while the loan sanction targets have been met, the two banks are experiencing a decline in their SME/Farm balance sheets due to two significant factors

- today's economic activity is smaller by 16% with the effect that repayment inflows from lending in earlier periods are outweighing the demand for new lending in the current climate
- a high proportion of new loans arise from restructuring of existing debt for some SMEs that are unable to service the original loan conditions on their legacy debt.

4.56 The CRO report notes that while it can be argued that restructuring of debt is providing little real economic benefit, without such restructuring activity many of these businesses would have gone out of existence.

4.57 In its quarterly report to June 2011 the CRO noted that

- The demand for credit from the SME and farm sectors remains unmeasured. However, interaction with the banks suggested a sluggish demand for credit and a slow drawdown of sanctioned facilities.
- There has always existed a 20% to 25% level of banks' declining credit.
- Businesses need to upskill in the areas of business case production to support applications for credit facilities.
- It will be a challenge for the two main banks to reach their €3 billion sanction targets for new and restructured facilities in 2011.

Appeal Applications to the CRO

4.58 In respect of the period from 1 April 2010 to 20 May 2011, 76[49] review applications had been received by the CRO[50]. Of these

- in 22 instances, the bank's credit decision was upheld
- in 23 cases, the CRO disputed the banks credit decision and the bank subsequently provided credit
- 13 applications were awaiting an eligibility decision while 12 were proceeding through the review process
- six applications required further work by the borrower and bank or were withdrawn.

4.59 The CRO report in May 2011 noted that over 85% of credit applications in the SME sector were approved by the two banks. However, the Irish Small and Medium Enterprises Association (ISME) published the results of a survey in March 2011, which states that 48% of SMEs were refused credit by their banks in the previous three months and 79% reported that banks were making it more difficult to access finance. The CRO report notes that quarterly surveys by ISME cover all banks not just the two monitored by the CRO.

49 40 applications were in respect of AIB and 36 were in respect of BoI.

50 This had risen to 98 in the report for the June quarter 2011. However, the outcome of reviews followed a broadly similar pattern.

Enterprise Ireland Bank Engagement

4.60 A Banking Relationship team was established within Enterprise Ireland (EI) in January 2010 to encourage banking support for exporting companies with difficulties in accessing credit for export development. As a result

- Both AIB and BoI have appointed senior executives in each bank to work with EI in relation to supporting companies and as appropriate to review lending decisions and to consider EI's experience of overseas markets and sectors. EI has also set up links with other banks that operate in Ireland.
- A range of sectoral seminars was arranged by EI along with ten workshops undertaken in 2010 on a variety of topics. Joint work was undertaken seeking to improve the delivery of existing and new financial products to support exporters including those in the technology sectors.
- During 2010, of 154 individual cases raised by EI with the banks regarding credit facilities for its clients, 36% resulted in the confirmation of existing facilities, 34% resulted in the provision of additional new facilities, 25% involved restructuring of facilities while in 5% of cases credit requests were declined. In addition, there were 38 cases where companies sought assistance in regard to matters other than credit requests including introductions to other banks, developing better working relationships with banks and planning for future requirements.

4.61 EI has stated that the banks need to develop intense knowledge of exporting businesses and sectors and to adopt a proactive cashflow lending approach to supporting Irish exporters rather than an assets based lending approach as had pertained over the previous ten years.

Managing the State Investments

4.62 By July 2011, the State had invested €65 billion in Irish financial institutions with an interest that ranges from minority shareholder up to nationalisation. As the State's attention moves from stabilisation to disposal it will be necessary to balance its obligations to

- maximise the value for the taxpayer
- maintain financial stability while doing so
- maintain competition within the sector in the interests of consumers and
- encourage the institutions to act commercially.

4.63 At the same time, it is necessary for it to maintain its normal policy and oversight roles. This range of objectives appears to suggest a need to address certain corporate governance issues including how the State's investment might best be consolidated and managed and what institutional adjustments, including separation of functions, might be appropriate. The current position is outlined below.

4.64 In March 2010, the Minister delegated certain banking functions to the NTMA[51]. The NTMA established a dedicated banking unit to carry out this function. The unit comprises nine permanent personnel including a number with previous experience in banking, corporate finance and research. As of 5 August 2011, the delegation order has been revoked and the banking functions have moved to the Department. The NTMA banking unit is now working on secondment in the Department.

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[51] Statutory Instrument 115 of 2010, National Treasury Management Agency Act 1990 (Delegation of Banking System Functions) Order 2010 and a Ministerial direction of 19 March 2010 in relation to the NTMA's functions under the statutory instrument.

4.65 The role of the banking unit includes

- advising the Minister about meeting the capital requirements of the credit institutions and the form any such capital injections might take
- implementing decisions by the Minister to make capital injections
- advising on the process towards ultimate disposal of the investments, including implementation of the disposals process and returning the banks to private ownership
- ensuring that the banks take appropriate steps to deleverage by disposing of assets within agreed price parameters.

4.66 The NPRF Commission operates under the aegis of the NTMA. Pursuant to directions issued by the Minister, the Commission had, at December 2010, invested €11.35 billion in AIB and BoI and, by July 2011, a further €10.29 billion[52]. The Commission cannot take any actions in regard to those investments other than in accordance with the Minister's directions.

[52] These investments included the reinvestment of dividends received in the form of ordinary shares (2010: €530 million and 2011: €288 million).

Conclusion

€71 billion is required to capitalise Irish financial institutions according to the latest assessments carried out by the Central Bank of Ireland. To date €65 billion of this sum has been provided by the State. €1.05 billion of this investment will be recouped from the disposal by the National Pensions Reserve Fund of shares in the Bank of Ireland to a group of institutional investors.

As a result the State is managing a very large investment in the financial institutions. This management involves input from the Department of Finance, the National Treasury Management Agency and the National Pensions Reserve Fund. In view of the materiality of the investment and the number of State sector entities involved there may be merit in rationalising the structure for the management of the State's banking investment, so as to ensure a coherent approach by the State including an appropriate separation of its investment and policy roles.

Based on the assumptions implicit in the Financial Measures Programme Report, published by the Central Bank of Ireland, the associated asset value of the banks after making good the anticipated losses is projected to be between €14 billion and €21 billion by the end of 2013.

The State through the National Asset Management Agency is managing the 'work out' of distressed land and property loans with an original book value of €71 billion, which it acquired for €30.2 billion. In its first year of operation a further impairment provision of €1.5 billion has been recognised in its accounts. This was largely due to the continued reduction of property values.

The State had guaranteed liabilities and deposits of financial institutions to an aggregate amount of €197 billion at the end of June 2011.

Fee payments made by credit institutions whose liabilities are guaranteed are paid into a designated account in the Central Bank of Ireland where interest was earned at a rate of around 1% per annum. In 2010, there were delays in transferring the fees received into the Exchequer. The average rate of interest that the State pays on its borrowings under the EU-IMF Programme is just under 5.6%. In order to achieve optimum debt management all amounts due to the Exchequer should be transferred at the earliest opportunity.

The amount of liquidity advanced by the Central Bank of Ireland through Eurosystem monetary policy operations stood at just under €103 billion in mid 2011. These advances are fully collateralised by way of bank assets.

Further advances by way of Exceptional Liquidity Assistance have been made to credit institutions. These advances constitute the bulk of a category of assets totalling €56 billion reported by the Central Bank of Ireland in mid 2011. They are backed by collateral and sovereign guarantees.

Chapter 5

European Union – Financial Transactions 2010

Central Government

European Union – Financial Transactions 2010

5.1 Ireland is a net beneficiary of EU funding. In 2010, Ireland contributed €1.35 billion to the EU budget and benefited from EU budget expenditure of €1.88 billion. Receipts from and payments to the EU budget over the past five years are set out in Figure 24.

Figure 24 Ireland's Receipts from and Payments to the EU Budget 2006 - 2010

Year	Receipts €bn	Payments €bn	Surplus/ (deficit) €bn
2006	2.20	1.53	0.67
2007	2.08	1.57	0.51
2008	2.06	1.59	0.47
2009	1.81	1.49	0.32
2010	1.88	1.35	0.53
Total	**10.03**	**7.53**	**2.50**

Source: Department of Finance

Chapter Focus

This chapter has been compiled to present an overview of the financial transactions between Ireland and the European Union, the procedures for the allocation of EU funds and the various audit arrangements relating to those transactions.

Contribution to EU Budget

5.2 The Irish contribution to the EU budget for 2010 was €1.35 billion. The component elements of this total are shown in Figure 25.

Figure 25 Ireland’s Contribution to EU Budget 2010

Contribution element	2010 determination base[a]	€000
Traditional own resources	75% of total received into Exchequer	185,644
VAT-based contribution	0.3% of established VAT base	193,781
GNI-based contribution	0.789% of established GNI	908,232
UK correction mechanism[b]		56,078
Netherlands/Sweden GNI reduction[c]		8,634
Total		**1,352,369**

Source: Department of Finance

Notes:

a The rates presented for the VAT and Gross National Income (GNI) based contributions are those agreed at the beginning of the budget year. These can alter during the year as amending budgets are agreed. GNI is the sum of incomes of residents of an economy in a given period and is conceptually identical to Gross National Product (GNP).

b Since 1985, the UK has received a partial refund of its EU budget contributions. The refund is financed by contributions from all other member states in proportion to their national percentage of EU GNI.

c The Netherlands and Sweden benefited from reductions in their GNI-based contributions to the EU budget in 2010 amounting to €651 million and €162 million respectively. The reductions were financed by contributions from all member states in proportion to their national percentage of EU GNI.

Receipts from EU Budget Funds

5.3 Receipts of €1.88 billion from the EU in 2010 were sourced from particular EU funds and programmes. The 2010 receipts were applied by Ireland as amounts voted by Dáil Éireann of €416 million, Central Fund payments of over €146 million and amounts paid directly to implementation agencies and beneficiaries amounting to €1.3 billion as specified in Figure 26.

Figure 26 Ireland's 2010 Receipts by Source[a]

Source of EU receipts	Total receipts	Application of funds		
		Votes	Central Fund	Direct[b]
	€000	€000	€000	€000
Agriculture and Rural Development Funds				
European Agricultural Guarantee Fund (EAGF)[c]	1,305,000	_	_	1,305,000
European Agricultural Fund for Rural Development (EAFRD) [d]	381,000	327,000	54,000	–
Structural Funds[e]				
European Regional Development Fund (ERDF)[f]	67,400	1,200	66,200	–
European Social Fund (ESF)	52,100	52,100	–	–
Other Funds/Receipts				
Other receipts	76,700	35,800	26,100	14,800
Total	**1,882,200**	**416,100**	**146,300**	**1,319,800**

Source: Department of Finance

Notes:

a European Commission figures show that between 2007 – 2009 the State received over €150 million in research and development funding from the FP7 Framework Programme for Research and Technological Development. 2010 funding is estimated at €85 million. These amounts have not been verified by the national authorities and are not included in the table as the funds are paid directly by the Commission to the beneficiaries.

b These receipts are held separately from State or Voted funds and paid to recipients on behalf of the EU.

c The principal component consists of single farm payments amounting to over €1.2 billion. The figure of over €1.1 billion for the single farm payment scheme and amounts for export refunds and intervention reported in note 6.1 to the Department's Vote account, relate to expenditure claims rather than receipts, which do not reconcile to this table as expenditure claims are recouped over two months in arrears.

d An amount of €54 million was received in 2010 due to increased financial ceilings and advance funding and is retained in a suspense account. The Vote amount figure of €327 million includes receipts of €21 million paid to the Department of Community, Rural and Gaeltacht Affairs.

e The structural funds consist of the ERDF which provides financial support for the development and structural adjustment of regional economies and the ESF which provides for education, training and employment supports.

f Includes receipts from the Programme for Peace and Reconciliation of €14.4 million.

5.4 The €76.7 million in other receipts set out in Figure 26 is comprised of the funds detailed in Figure 27.

Figure 27 Estimated EU Receipts from Other Sources[a]

Source of other EU receipts	Total receipts	Application of funds		
		Votes	Central Fund	Direct
	€000	€000	€000	€000
European Globalisation Adjustment Fund[b]	24,800	–	24,800	–
European Fisheries Fund (EFF)	14,700	14,700[c]	–	–
Veterinary Fund	14,000	14,000	–	–
Education programmes	14,500	–	–	14,500
Fisheries protection/ EAGF fish markets and conservation and management of fisheries	2,300	2,300[c]	–	–
European Refugee/Integration/Return Funds[d]	3,500	3,500	–	–
EEA/TENs/other[e]	1,300	–	1,300	–
CSO – Eurostat receipts	800	800	–	–
Life+[f]	500	500	–	–
Customs and Fiscalis receipts[g]	300	–	–	300
Total	**76,700**	**35,800**	**26,100**	**14,800**

Source: Department of Finance

Notes:
- a Some EU Funds from other sources may be paid by the EU Commission directly to private firms or individuals and therefore the term estimated is used.
- b These receipts relate to three Irish applications for assistance from the Fund in relation to redundancies at Dell Computers, Limerick and eight of its suppliers and downstream producers, at Waterford Crystal and three ancillary companies, and at SR Technics, Dublin Airport.
- c These receipts of €17 million in total may be reconciled to the Department of Agriculture, Fisheries and Food's Vote account amount of €23 million for fisheries as the Vote includes an additional €6 million approximately in receipts received in 2008 and 2009 which were held in a suspense account and lodged in 2010.
- d €3.2 million was received in respect of the European Refugee Fund and the Integration Fund for Third Country Nationals. The balance comprises receipts from the European Return Fund.
- e These receipts relate principally to transport, energy and telecommunication projects.
- f These receipts relate to a funding programme for environmental projects.
- g These receipts relate principally to payment for expenses for staff engaged in customs work and in the Fiscalis 2013 programme which relates to the operation of the taxation system.

Allocation of EU Funds

5.5 EU funding is allocated for multi-annual programming periods. The current programme period is 2007-2013. An associated financial framework for this period was agreed between the European Parliament, the EU Council and the European Commission (the Commission) under an Inter-Institutional Agreement adopted in May 2006. An annual EU budget of expenditure and receipts governs the allocation of funds in each year within the programming period.

5.6 The annual EU budget is decided by the EU Council and the European Parliament on the basis of a budget proposal from the Commission, which is also responsible for implementing it. The two principal elements of the 2010 budget were payments for

- agriculture and rural development – which accounted for over 47% of the budget
- sustainable growth – which includes structural and cohesion funding and accounted for a further 39% of the budget.

Sources of EU Funding

5.7 The main sources of EU funding to Ireland are agriculture and rural development funds and structural funds. Each of the funds is governed by different rules for financial management, control and accountability. A principal difference is that independently certified annual accounts of expenditure must be submitted each year for the agriculture and rural development funds, whereas for structural funds certified accounts must be submitted at the end of the programme period.

Agriculture and Rural Development Funds

5.8 EU expenditure on agriculture and rural development is financed out of two funds

- the European Agricultural Guarantee Fund (EAGF), which, with a few exceptions, fully funds direct aid payments to farmers as well as a range of market support measures
- the European Agricultural Fund for Rural Development (EAFRD), which came into operation in 2007 and is used for co-financing measures implemented under Ireland's Rural Development Programme 2007-2013.

5.9 EAGF and EAFRD expenditure is paid by accredited paying agencies[53] in member states. In Ireland, the Department of Agriculture, Fisheries and Food is the sole accredited paying agency and Managing Authority[54] for the EAFRD. The authority to make rural development payments in respect of specific measures of the EAFRD relating to LEADER[55] is delegated to the Department of the Environment, Community and Local Government.

5.10 At year-end, independently certified annual accounts of EAGF and EAFRD expenditure must be submitted to the Commission. The Secretary General of the Department of Agriculture, Fisheries and Food is required to provide annually a statement of assurance regarding the EAGF and EAFRD accounts and control systems. In the case of EAFRD, the Department submits an annual report on its implementation.

5.11 The Commission clears both of the annual accounts in two stages – by an annual clearance decision based on the independent certification of the annual accounts and by ad-hoc clearance decisions arising from follow up audit work by the Commission. The Commission undertakes an annual programme of audits on specific schemes and areas following certification of the annual accounts. It conducted three audit missions in Ireland in 2010.

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53 Paying agencies are accredited by member states if they comply with specific requirements on financial control and accountability over EU expenditure as set out in Community legislation (EU Reg. 885/2006).

54 The Managing Authority is responsible for managing and implementing the programme in an efficient, effective and correct way.

55 The LEADER initiative is designed to aid the development of sustainable rural communities.

Structural Funds

5.12 Ireland's receipts from the structural funds (ERDF and ESF) peaked during the 1993-1999 financial framework period and have declined in each subsequent programming period. Structural funds accounted for 6% of EU budget payments to Ireland in 2010.

5.13 The regulations governing the structural funds require member states, in conjunction with the Commission, to prepare and agree operational programmes to implement strategic priorities and impose financial management and control requirements relating to the implementation of co-funded assistance.

5.14 Each member state is required under the regulations to designate a Managing Authority for each operational programme. The member state must also designate a Certifying Authority and an Audit Authority for each structural fund. The functions and responsibilities of these bodies include the following

- The Certifying Authority is responsible for drawing up and submitting certified statements of expenditure and applications for payment. It is responsible for ensuring the accuracy and probity of these statements of expenditure.
- The Managing Authority is responsible for managing and implementing the operational programme in accordance with the principles of sound financial management and for ensuring that activities selected for funding match the operational programme criteria. It is also responsible for verifying that co-financed projects are delivered, that expenditure declared by the beneficiaries has actually been incurred and complies with EU and national rules and that an adequate audit trail exists.
- The Audit Authority functions include ensuring that audits are carried out to verify the effective functioning of the management and control system of the operational programmes. It must present an audit strategy to the Commission and submit an Annual Control Report setting out the findings of audits carried out and provide an annual audit opinion as to whether the management and control systems function effectively.

5.15 The Department of Finance has overall policy responsibility for the structural funds and is also the Certifying Authority for the ERDF. There are two Managing Authorities for the ERDF in the 2007-2013 programming period - the Regional Assembly for the Border, Midlands and Western region and the Regional Assembly for the Southern and Eastern region. The Department of Education and Skills[56], as Managing Authority and Certifying Authority, has primary responsibility for the ESF.

5.16 The Secretary General of each department involved in the implementation of co-financed projects is required to sign a declaration annually and submit it to the Department of Finance to confirm compliance with all applicable EU regulations. An Implementation Report is submitted annually to the Commission by each Managing Authority which sets out the financial implementation of the operational programmes in terms of targets and outlines the monitoring and evaluation procedures in place.

[56] Responsibility for the functions of the ESF Policy/Operations and ESF Audit Authority transferred to the Department of Education and Skills on 1 May 2010 from the Department of Enterprise, Trade and Innovation.

Audit of EU Funds

5.17 The audit arrangements in place within each of the relevant departments in relation to EU funds are outlined below together with an outline of the roles of my Office, the EU Commission and the European Court of Auditors (ECA).

Audit Authorities

Agriculture and Rural Development

5.18 The Department of Agriculture, Fisheries and Food appoints a firm of auditors to provide an independent annual certificate and report on internal controls to the Commission. In addition, the Department's Internal Audit Unit finalised and issued eleven system audit reports on the EAGF and EAFRD funded schemes in 2010.

Structural Funds

5.19 Audit Authorities for ERDF and ESF have been established in the Departments of Finance and Education and Skills. These units are required to perform audits of operations[57] and to verify[58] eligible expenditure declared to the Commission within managing authorities, intermediate bodies and beneficiaries in operational programmes in the 2007-2013 programming period. The audit activity performed by the ERDF and the ESF units for the 2000-2006 and 2007-2013 rounds is shown in Figure 28.

Figure 28 Audit Authority Activity in 2010

	Programming Period			
	2000 – 2006		2007 – 2013	
	ERDF[a]	ESF	ERDF	ESF
Number of organisations visited/operations in 2010	16	26	63	45
	€m	€m	€m	€m
Amount verified in 2010	55	61	132	47
Cumulative verified expenditure at 31 December 2010	495	284	132	65
Cumulative eligible expenditure at 31 December 2010	4,155	1,981	189	283
Cumulative expenditure verified at 31 December 2010	12%	14%	70%	23%

Source: Departments of Finance and Education and Skills

Note: a The ERDF Audit Authority is also responsible for performing 15% verification on eligible expenditure from the Cohesion Fund. At 31 December 2010, it had verified €319 million or 41% of cumulative expenditure of €777 million declared to the Commission.

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57 EU regulations require that the sample of operations to be audited each year is based on a random statistical sampling method. A non-statistical method may be used where the number of operations is insufficient to allow the use of a statistical sampling method.

58 'Verifying' means that there is supporting evidence for EU co-financed expenditure and that the expenditure complies with relevant national and Community rules.

5.20 Systems-based audits are also performed at each level in accordance with a Commission guidance document[59] on a common methodology for the assessment of management and control systems. The ESF Audit Authority coordinates an annual plan of systems-based audits to be completed by Internal Audit Units in bodies involved in the management and administration of the operational programmes. The ERDF Audit Authority carried out these systems-based audits in respect of ERDF operations from the Certifying Authority level down to the public beneficiary body level in accordance with EU regulations[60].

Audit by the Comptroller and Auditor General

5.21 Where a Department or State body audited by the Comptroller and Auditor General is in receipt of EU funds, the receipt and application of the funds are audited in like manner to national funds and to all other transactions by that body. Audit planning has regard to the audit tasks undertaken by others including the ECA, the Audit Authorities, the independent external Certification Body for agricultural supports and Internal Audit units. Audit work includes testing of compliance with national rules that have been transposed from EU directives and regulations. However, the transposition process is outside the remit of the audit.

Audits by EU Commission

5.22 Audit services from the Commission carry out a number of audits annually in member states and have the right to carry out on-the-spot audits or may request a member state to audit specific programmes or projects.

European Court of Auditors

5.23 Ireland contributed €1.35 billion in 2010 towards the total EU budget of approximately €123 billion which amounted to about 1% of the Gross National Income (GNI) of its 27 member states. Because Ireland's financial contribution is pooled with that of other member states, it shares an interest that the common funds are managed to good effect. At EU level this assurance is provided by the ECA.

5.24 The ECA is required to give an annual Statement of Assurance (an audit opinion) on the reliability of the accounts of the European Union and of the legality and regularity of the transactions underlying those accounts. In carrying out these functions, ECA staff visit member states to review management structures, test systems of control and to examine in detail a sample of applications submitted in support of payments to final beneficiaries.

5.25 Liaison arrangements provide for ECA visits to Ireland to be organised by my Office and all correspondence including the ECA audit findings and management responses are addressed to my Office for transmission to the audited body. Nine such visits were carried out in 2010. Following consultation with the certifying authority, the findings will be incorporated into the annual report of the ECA for 2010.

5.26 The Statement of Assurance provided by the ECA addresses two separate matters

- whether the accounts are reliable
- whether the transactions undertaken with EU budget moneys were legal and regular.

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59 EU Commission Guidance Document (COCOF 08/0019/01).

60 Article 60 of General Regulation 1083/2006.

5.27 For the third consecutive year, the ECA gave a positive Statement of Assurance, without qualification, on the reliability of the 2009 accounts[61]. However, for the sixteenth successive year, the ECA did not give a positive Statement of Assurance on the legality and regularity of most categories of EU expenditure. It reported that payments from the budget continue to be materially affected by error[62] (estimated to be between 2 and 5% overall) for the policy groups

- Agriculture and Natural Resources
- Cohesion
- Research, Energy and Transport
- External Aid, Development and Enlargement
- Education and Citizenship.

5.28 Two policy groups were reported not to be materially affected by error – Economic and Financial Affairs and Administration. The ECA reports that there was a significant decrease in its estimate of the most likely error in Cohesion spending compared with previous years and that for the budget as a whole, the estimate of error had fallen over recent years.

Conclusion

Ireland contributed €1.35 billion to the EU budget in 2010 while €1.88 billion was received from EU funds.

Ireland, like other member states, has an interest in how the EU budget is used. While the European Court of Auditors noted that the estimate for material error in the budget had fallen in global terms across the EU, it was unable to give positive assurance on the legality and regularity of most elements of EU expenditure.

Financial corrections in Ireland are lower than the EU average. In particular, in relation to the 2000-06 and the 2007-13 programming periods, there have to date been no financial corrections in respect of Structural Funds received. Agricultural disallowances in the last decade are of the order of 0.12% which is considerably lower than the EU average.

61 The audit of the 2010 accounts is not yet completed.

62 The ECA treats an error in excess of 2% of total expenditure in a policy area as material.

Chapter 6

Financial Commitments under Public Private Partnerships

Central Government

Financial Commitments under Public Private Partnerships

6.1 A public private partnership (PPP) is an arrangement between public and private sector partners for the delivery of public infrastructure and/or public services.

6.2 Commitments under PPPs give rise to financing obligations usually extending over 25 to 30 years. These agreements with private sector partners come in a number of forms, the basis of which are outlined in Annex A.

Chapter Focus

This chapter has been compiled to provide information about the financial commitments entered into by central government departments and agencies under PPP contracts. It also reviews the current status of the Health Service Executive co-location programme.

Summary of Expenditure and Commitments

6.3 Annex B lists the major[63] PPP projects, as at the end of December 2010, in respect of which central government departments and agencies had entered contracts as the sponsoring agency, or had otherwise made financial commitments to the projects.

6.4 Up to the end of 2010, the total expenditure incurred by central government departments and agencies under PPP contracts was over €1.9 billion (see Figure 29). Expenditure in the year under contracts amounted to €415 million.

63 Projects where the capital cost of asset creation was less than €20 million are not included.

Figure 29 Expenditure and Commitments under PPP Contracts in Place at End 2010, by Department/Agency

Department/Agency	Number of projects	Expenditure Prior to 2010	Expenditure In 2010	Outstanding Commitment[a]
		€m	€m	€m
Education and Skills	5	168	38	1,128
Courts Service	1	–	39	588
Transport, Tourism and Sport/ Office of Public Works	1	–	41	716
National Roads Authority	10	844	228	1,872
Environment, Community and Local Government[b]	20	525	69	18
Total	**37**	**1,537**	**415**	**4,322**

Source: Annex B

Notes: a Assumes inflation will average 2% a year over the remaining lives of the contracts.

b Amounts shown in relation to projects sanctioned by the Department of the Environment, Community and Local Government are the contributions by the Department towards the capital cost of local authority PPP projects. They do not include expenditure under the contracts by the relevant local authorities, or the outstanding commitments that will have to be met by the local authorities from their own future budgets.

6.5 The total outstanding commitments of central government departments and agencies in respect of contracted PPP projects at end 2010 is estimated at €4.3 billion. Based on expenditure incurred to end 2010 and the estimated outstanding commitments, the aggregate Exchequer expenditure in respect of the currently contracted PPP projects is projected to be €6.3 billion.

Potential Future Commitments

6.6 A number of PPP projects were in development at the end of 2010 but had not yet reached contract stage[64].

6.7 Given the complexities involved in the PPP process and payment mechanisms, it is difficult to estimate potential future commitments under projects that are still in planning. The cost of a project depends on a range of factors, including the project specification, perspectives on risk pricing and the cost of borrowing in the project finance market. These are not finally settled until projects reach contract stage.

6.8 The Department of Public Expenditure and Reform maintains a list of 'pipeline' PPP projects in respect of which it is envisaged that construction could begin by 2016. The Department has stated that those projects are at various stages of planning and procurement and the estimated costs are at various stages of robustness. The Department considers that providing a composite estimate of cost for all 'pipeline' projects at a point in time would be of limited value.

[64] The Department of Public Expenditure and Reform maintains and publishes a project tracker database, listing all PPP projects with an estimated capital value of over €20 million each. The tracker includes projects where a contract is in place, and those for which project advisors have been appointed. The information on each project is provided by the relevant sponsoring authority. The tracker, however, has not been updated since March 2010. See www.ppp.gov.ie

6.9 Projects in the 'pipeline' that would give rise to unitary payment commitments include

Education projects	3 schools bundle projects [65]
	3 third level bundle projects
	Dublin Institute of Technology Grangegorman campus
Transport projects	Metro North
	DART Underground [66]
	N17/N18 Gort-Tuam
	N11 Arklow to Rathnew (including N7 Newlands Cross junction upgrade)
	M11 Enniscorthy Bypass/N25 New Ross bypass[67]
	M20 Cork-Limerick South[67]
Other projects	Radiation Oncology Units.

PPP Contracts in 2010

6.10 Three PPP projects reached contract stage during 2010. These are outlined in the following sections.

Portrane/Donabate/Rush/Lusk Waste Water Treatment Plant

6.11 A design, build and operate PPP is being used to provide an upgraded and expanded main drainage system in North County Dublin, including a single waste water treatment plant at Portrane. It will cater for a population equivalent of 65,000 and have a two-year construction phase followed by a 20 year operation and maintenance period. The plant commenced construction in March 2010 and the Department of the Environment, Community and Local Government will provide funding of €23.3 million out of a total capital contribution cost of €35 million. The plant is expected to commence operation in March 2012.

Tullamore Waste Water Treatment Plant

6.12 This project involves the design and building of a waste water treatment plant over a two-year construction period followed by a 20 year operation and maintenance period. The plant is intended to cater for a population equivalent of 45,000. The Department of the Environment, Community and Local Government will provide funding of €15.7 million out of a total allocation for the project of €20.2 million. The plant will become operational in May 2012.

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65 Includes two PPP schools bundles announced as part of the Jobs Initiative.

66 The tunnelling element of this project has been deferred due to the reduced capital available in the National Recovery Plan. It is envisaged that re-signalling and associated works could proceed over the next four years, and this would prepare the network for the delivery of the underground tunnel once financial resources permit.

67 Procurement of these projects has been deferred until at least 2014 under the National Recovery Plan.

Second Schools Bundle Project

6.13 Contracts have been signed to design, build, finance and maintain six schools providing primary and post primary education in five towns – Bantry (two schools), Kildare, Abbeyfeale, Athboy and Wicklow. Taken together with a PPP bundle contracted in 2009, this will bring to ten the number of schools to be provided by PPP out of a total of 27 that had been planned in September 2005.

6.14 The second schools bundle will provide accommodation for 4,500 post primary pupils as well as an eight-classroom primary school. The Department of Education and Skills expects the schools to be brought into operation in late 2011.

Financing Challenges

6.15 It was noted in last year's Report that State bodies were beginning to separate funding competitions for the financing of PPP projects. This had become necessary because the financial crisis led to a significant reduction in the number of banks willing to provide long-term funding while those remaining active in the market generally wished to keep lending terms open for only short periods of two or three months.

6.16 The National Development Finance Agency (NDFA) has stated that there was a further significant decrease in the second half of 2010 in the number of banks expressing interest in providing funding for infrastructural projects in Ireland. The prevailing Irish sovereign risk was a further constraining factor reducing the pool of international banks willing to lend into the Irish PPP market.

6.17 In response to the finance risk and reduced willingness of banks to lend, the NDFA introduced its preferred tenderer funding competition arrangement. By separating the process of procuring a preferred tenderer from the obligation of all tenderers to prove they had the necessary funding sourced, the length of time banking terms have to be held and the number of banks from whom commitments have to be raised has been reduced. The approach is being used in the schools projects and the first third-level bundle project.

6.18 The NDFA stated that it is also engaging with the banking market and exploring other funding opportunities to ensure sufficient funding at a price that ensures value for money is achieved for projects currently being procured. It believes that clarity on the prevailing banking uncertainties and a stable or improved fiscal position will also help alleviate some of the concerns of the international financial institutions who traditionally lend to the Irish project finance market.

6.19 Overall, the NDFA believes that well-defined projects with relatively low funding requirements still retain an interest for the debt and equity funding markets. The NDFA was satisfied that such projects continued to merit taking the PPP procurement route and were likely to achieve value for money as defined in the Department of Public Expenditure and Reform PPP guidance.

National Roads Authority Traffic Risk Sharing

6.20 All of the PPP road contracts, with the exception of the M50 upgrade (for which the PPP company does not collect tolls), provide for a share of revenues to accrue to the National Roads Authority (NRA), subject to traffic or sales levels exceeding specified thresholds. Revenue received for 2010 amounted to €1.28 million. The NRA has forecast revenue receipts of €1.5 million to €1.75 million for 2011.

6.21 In the case of the Clonee/Kells (M3) and Limerick Tunnel PPPs, the contracts also provide for traffic-related guarantee payment mechanisms whereby the NRA is obliged to make payments to the PPP company if traffic falls under a certain level. The NRA stated that payment arises where the actual traffic in any half year period does not exceed the figures set out in the relevant PPP contract. As these routes opened during the second half of 2010, amounts due only became payable in 2011. The NRA estimated that it will make payments in 2011 of €5 million to €5.5 million in respect of these two projects[68]. The extent to which such payments will arise in the long run is dependent on the outturn traffic volumes on the roads concerned.

6.22 The NRA noted that it is difficult at this point to forecast future traffic levels given current economic uncertainties. The pattern has been mixed with traffic growth on some routes well in excess of expectation, while on other routes traffic volumes has reduced in the last 12 months.

Co-location of Hospitals

6.23 In 2005, the Minister for Health issued a direction to the Health Service Executive (HSE) to implement a policy aimed at development of private hospital facilities on public hospital sites and freeing up of beds for public patients in public hospitals. The financial and public health and welfare benefits brought about by the new public bed capacity was expected to outweigh the loss of private bed fee income for public hospitals and the tax advantages conferred on the private partners.

6.24 Following an EU-wide competition first advertised in May 2006, the HSE issued invitations to tender to short-listed bidders for seven hospitals in April 2007. These were

- Waterford Regional Hospital
- Sligo General Hospital
- Limerick Regional Hospital
- St James's Hospital
- Beaumont Hospital
- Cork University Hospital.
- James Connolly Memorial Hospital.

6.25 Project agreements for the Beaumont, Cork and Limerick projects were signed in March 2008 and in the case of St James's Hospital, in December 2008. Planning permission was granted for each of these projects. However, the project agreements in each case expired at the end of March 2011, when the time allowed for the preferred bidders to secure funding had passed. All discussions with the preferred bidders have ceased and the HSE has stated that it has no proposals to progress any of the projects.

6.26 The legal and financial costs associated with the procurement of the co-located hospitals project have been of the order of €1.46 million to date. The Accounting Officer of the HSE told me that there had, to date, been no legal costs associated with the expiry of the agreements.

Local Authority PPP Arrangements

6.27 PPP agreements entered into by local authorities require prior approval by the Minister for the Environment, Community and Local Government who exercises policy making, sanctioning and oversight roles in local government matters. The Minister's approval is required, even where there are no direct Exchequer funding implications foreseen by the PPP arrangements.

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[68] The payments in 2011 will relate to the second half of 2010 and the first half of 2011. The amount payable by the NRA for traffic risk sharing on the Limerick Tunnel and the M3 in respect of 2010 was €1.79 million.

6.28 The costs reported in Annex B in respect of local authority schemes only include those schemes where there is an Exchequer contribution and associated commitments. Consequently, the costs of large-scale PPP arrangements entered into by local authorities in recent years without a direct Exchequer involvement, for example, the Dublin Waste to Energy Scheme, are not included in the figures.

Conclusion

The total outstanding commitments of central government departments and agencies in respect of contracted PPP projects at end 2010 is estimated at €4.3 billion. A further significant number of PPP projects were in development at the end of 2010 but had not yet reached contract stage. Estimates of the potential cost of those projects are not currently available from the Department of Public Expenditure and Reform.

The current economic and financial situation has brought about a climate of significant uncertainty over the availability of finance to underpin investment by the private sector in major public projects, including PPPs. Until market conditions improve, the NDFA strategy of advising the separation of the procurement decision from the need for tenderers to prove availability of funding is an approach that may help to bring some of the projects in development to the preferred tenderer stage. The NDFA's view is that well-defined projects with relatively low funding requirements still retain an interest for the debt and equity funding markets.

Difficulties in securing funding for hospital co-location projects resulted in the lapsing of project agreements in four cases. The HSE has indicated that it does not have any proposals to progress its hospital co-location programme.

Another impact of the economic downturn has been lower than projected traffic on some roads developed under PPP arrangements. Two projects have guarantee payment mechanisms and the reduced traffic levels will result in additional payments to the private sector partner in 2011 estimated to be in the region of €5 to €5.5 million.

Annex A Financial Nature of PPP Arrangements

Typically, a PPP project involves a formal contract between a government agency and a private partner, where the latter undertakes to deliver specified facilities and/or services over the life of the contract. This is usually 25 to 30 years, although some contracts in the roads sector may be up to 45 years in duration. Project risks, which are a feature of all long-term projects, are allocated between the public and private sector partners, depending on which partner is in the best position to manage them. Under the PPP process, the State retains ownership of the assets throughout the contract period. At the end of the contract period, the sponsoring Government agency assumes responsibility for the ongoing maintenance and operation of the assets.

The structure put in place to compensate the private sector partner for developing the assets and delivering the required services varies, with different implications in terms of the financial commitments involved for the sponsoring public bodies. In many cases, the public sponsors of the project take on contractual commitments to make regular payments to the private sector partner over the life of the project. In other cases, projects are designed on a concession basis, whereby the private sector partner receives some or all of the compensation in the form of charges imposed on the users of the service.

Unitary Payment Projects

This is where the sponsoring public agency makes regular payments (monthly, quarterly or annually) over the term of the contract to the private sector partner, subject to satisfactory performance in providing agreed facilities to the required standard. Typically, part of this unitary (or all-in) payment amount is fixed over the life of the contract, with the remainder varying in line with price fluctuations (usually the Consumer Price Index). The split between the fixed and variable elements varies from project to project. Deductions are made to the unitary payment for non-performance and/or unavailability of the project.

Up-front Capital Payment Projects

In the water and wastewater sector, many PPP projects are procured on a design, build, operate and maintain (DBOM) basis. In these cases, the Exchequer provides up-front capital funding (as with traditional procurement), so there are no capital or financing costs to be paid back over the life of the project. Annual operating costs (paid by the relevant local authorities) are based on the volume of waste water arriving for treatment or the volume of drinking water produced.

Concession Projects

In concession projects, the users of the service pay fees to the private sector partner e.g. motorists using toll roads. The State may pay a contribution towards the capital costs of providing the infrastructure, and may also pay operating subventions during the contract period. Where user payments exceed projected levels, there may be scope for the additional income to be shared between the public and private sector partners.

Asset-based Schemes

In this kind of project, the public sector contribution to the project includes provision of an asset (usually land), with the private partner developing the asset e.g. social/affordable/private housing projects. Ultimately, much of the funding for this kind of project depends on sales or rentals on the open property market, and the ongoing difficulties in the property market have made many proposed developments unviable. Such projects are usually of shorter duration (five to seven years) than concession or unitary payment projects.

Annex B Expenditure up to end 2010 and outstanding commitments on large PPP project contracts, by public sector agency and by project

The table lists the individual projects reported by the respective departments or agency. Only commitments and expenditure in relation to projects which have an estimated capital development value of €20 million or more are included.

A summary outline of the individual projects contracted up to the end of 2008 was included in the Comptroller and Auditor General's Report on the Accounts of the Public Services 2008 (pages 29 to 34). Summary outlines of other projects were included in the Report on the year of contract.

Inflation

The commitment amounts are projected based on the assumption that inflation will average 2% a year over the remaining life of each project. All amounts include VAT (unless otherwise stated).

Scope of PPP Projects

The private sector elements contributed to each project are indicated as follows

D **Design** of service/infrastructure

B **Build**/construct/extend/renovate capital assets

F Provide **finance** (e.g. provide/secure private equity and borrowing; collect user charges)

O **Operate** assets (e.g. facilities management; employment of services staff)

M **Maintain** assets over contract life.

Sponsoring authority/ project name	Scope of project	Key project dates			Expenditure			
		Contract signed	Service commencement	Contract end	Pre 2010	2010	Future commitment	Projected total expenditure
					€m	€m	€m	€m
Department of Education and Skills								
Pilot PPP schools bundle	DBFM	November 2001	2002	2027	85.9	10.7	188.4	285.0
Maritime College	DBFM	February 2003	2004	2029	54.3	8.6	136.3	199.2
Cork School of Music	DBFM	September 2005	2007	2032	28.3	8.1	193.8	230.2
First bundle PPP schools	DBFM	March 2009	2010	2035	–	10.2	256.8	267.0
Second bundle PPP schools	DBFM	June 2010	2011	2036	–	–	352.7	352.7
Courts Service								
The Criminal Courts of Justice	DBFM	April 2007	2009	2035	–	38.9	587.9	626.8
Department of Transport, Tourism and Sport/Office of Public Works								
National Conference Centre	DBFOM	April 2007	2010	2035	–	41.0	715.6	756.6
National Roads Authority[a]								
Kilcock/Kinnegad	Concession	March 2003	2005	2033	169.3	0.2	7.8	177.3
Dundalk Western Bypass	Concession	February 2004	2004	2034	2.2	0.2	3.9	6.3
Rathcormack/Fermoy	Concession	June 2004	2006	2034	97.9	5.6	46.5	150.0
Waterford City Bypass	Concession	April 2006	2010	2036	107.0	4.0	89.8	200.8
Limerick Tunnel	Concession	August 2006	2010	2041	160.5	25.0	68.8	254.3
Clonee/Kells	Concession	March 2007	2010	2052	235.3	77.9	399.1	712.3

Sponsoring authority/ project name	Scope of project	Key project dates			Expenditure			
		Contract signed	Service commencement	Contract end	Pre 2010	2010	Future commitment	Projected total expenditure
					€m	€m	€m	€m
Galway/Ballinasloe	Concession	April 2007	2010	2037	43.7	28.2	288.6	360.5
Portlaoise/Cullahill	Concession	June 2007	2010	2037	27.9	18.6	37.3	83.8
M50 Upgrade	DBFOM	September 2007	2007	2042	–	42.0	908.8	950.8[b]
Motorway Service Areas	Concession	October 2009	2009	2034	–	25.9	21.2	47.1
Department of Environment, Community and Local Government[c]								
Waste water treatment plants								
Dublin Bay[d]	DBM	March 2001	2003	2024	203.7	16.6	–	222.8
Wexford	DBOM	July 1999	2004	2026	18.4	–	–	18.4
Cork	DBOM	December 2001	2004	2027	68.1	–	–	68.1
Balbriggan/Skerries	DBOM	September 2004	2006	2028	19.0	–	–	19.0
South Tipperary	DBOM	March 2003	2007	2029	13.4	–	–	13.4
Dungarvan	DBOM	April 2004	2007	2029	12.2	–	–	12.2
Sligo	DBOM	September 2006	2008	2030	17.0	–	–	17.0
Donegal (A)	DBOM	June 2006	2008	2030	25.2	–	–	25.2
Waterford	DBOM	September 2006	2010	2033	21.5	1.0	0.5	23.0
Portlaoise	DBOM	December 2006	2009	2031	20.1	–	–	20.1
Meath villages	DBOM	October 2007	2010	2032	21.3	1.1	–	22.4
Mullingar	DBOM	April 2008	2010	2032	16.5	–	–	16.5
Castlebar	DBOM	September 2008	2010	2032	11.3	0.1	–	11.4
Bray/Shanganagh	DBOM	September 2008	2011	2034	26.5	28.8	1.1	56.4
Wicklow	DBOM	September 2007	2009	2031	14.4	–	–	14.4

Sponsoring authority/ project name	Scope of project	Key project dates			Expenditure			
		Contract signed	Service commencement	Contract end	Pre 2010	2010	Future commitment	Projected total expenditure
					€m	€m	€m	€m
Portrane/Donabate/Rush/Lusk	DBOM	February 2010	2012	2032	–	16.8	6.5	23.3
Tullamore	DBOM	April 2010	2012	2032	–	4.8	10.9	15.7
Water treatment services								
Clareville	DBOM	December 2006	2010	2030	16.7	–	–	16.7
Area development projects								
Fatima Mansions redevelopment[e]	DBF	June 2004	2004	2011	–	–	–	–
Greystones harbour development	DBOF	December 2007	2017	2047	–	–	–	–

Notes:

a In the case of NRA concessions contracts, the projected total expenditure represents the total payments expected to be made to the PPP companies concerned over the life of the contract. The PPP companies also benefit from user charges which contribute to their capital and operational costs. The contracts incorporate a revenue sharing mechanism whereby the NRA receives a portion of toll revenue.

b Excludes VAT.

c Expenditure/commitments exclude those of local authorities.

d The Department has not indicated the future commitment for the Dublin Bay project as the amount is under examination as part of the final account, and it states that no further payments are being made pending clarification of certain issues. The currently approved grant is shown in the projected total expenditure column.

e The Department was the sanctioning authority in this case. Dublin City Council was the sponsoring authority.

Chapter 7

Functions and Governance

National Treasury Management Agency

NTMA Functions and Governance

7.1 The National Treasury Management Agency (the Agency) is a complex organisation with multiple functions that now extend beyond its original and core function of managing Ireland's national debt. It reports directly to the Minister for Finance.

Chapter Focus

This chapter outlines

- the principal functions of the Agency
- the arrangements for its governance
- the result of audit of its accounts.

Functions of the Agency

7.2 The Agency has the following functions

- It borrows moneys on behalf of the Exchequer and manages Ireland's national debt which at the end of 2010 was €93.4 billion after taking account of related assets.
- It acts as the Manager of the National Pensions Reserve Fund (NPRF) which held net assets of €22.7 billion at the end of 2010.
- It manages compensation claims on behalf of certain State authorities. Awards and associated costs of the State Claims Agency (SCA) in 2010 amounted to €96 million while the estimated cost of settling claims outstanding at 31 December 2010 was €885 million.
- It discharges the functions of the National Development Finance Agency (NDFA). Fees and expenses incurred by the Agency in the performance of its financing and advisory functions in relation to specific public investment projects amounted to €4.9 million in 2010.
- It purchases carbon credits required to meet Ireland's climate change obligations. The Carbon Fund held assets to a value of €97 million at the end of 2010.
- It provides central treasury services for government departments and non-commercial State bodies. Deposits held at year-end were €33.3 million and loans provided were €48.3 million.

7.3 During 2009 and 2010 a number of additional functions and services were added to the Agency's remit as follows

- the provision of support services for the National Asset Management Agency (NAMA)
- the operation of the Eligible Liabilities Guarantee Scheme
- certain banking system functions.

Support to NAMA

7.4 The NTMA assigned staff and provided services to NAMA during 2010 for which a cost of almost €15 million was incurred and charged to NAMA[69]

- €10.3 million was incurred in respect of around 100 staff directly employed by the NTMA and assigned to NAMA (€9.2 million) and the cost of NTMA employees operating shared services including IT, Human Resources and Finance (€1.1 million)
- €4.6 million was incurred in respect of other costs incurred by the NTMA including rent, office services and consultancy costs.

Guarantee Scheme Administration

7.5 Under the Eligible Liabilities Guarantee Scheme (the Scheme), certain eligible liabilities, including deposits and debt securities of up to five years maturity in participating institutions are guaranteed by the State. The NTMA operates the Scheme on behalf of the Minister for Finance. Under State aid rules, the Scheme requires the approval of the EU Commission at six-monthly intervals. On 1 June 2011, the Commission approved the extension of the Scheme to 31 December 2011. There were 16 participating institutions at the end of 2010. While the scheme is administered by the Agency, accountability for fees collected under the scheme lies with the Accounting Officer of the Department of Finance.

Banking System Functions

7.6 In March 2010, the Government delegated certain banking system functions of the Minister for Finance to the NTMA. The delegation related, in particular, to management of the State's interest in the credit institutions covered by the banking guarantees, negotiation of capital support to those institutions and the sustainable development of the banking sector. The delegation was revoked in August 2011. Further information on these additional functions is set out in Chapter 4.

Governance of the Agency

7.7 The Agency is in the process of further enhancing its governance arrangements which will provide additional assurance and support to the Accounting Officer. By virtue of the terms of its legislation[70], the Agency does not have a Board and the management and business of the Agency are the responsibility of its Chief Executive. However, the legislation provides for an Advisory Committee to assist and advise the NTMA on such matters as are referred to that committee by the NTMA.

7.8 In regard to the core functions of the NTMA, including management of the national debt and the SCA, the NTMA Chief Executive is directly answerable to the Minister for Finance. The SCA has, in turn, a Policy Committee to provide advice on policy and procedures relating to the performance of its functions.

7.9 NAMA, the NDFA, and the NPRF each has a Board or Commission which are answerable to the Minister for Finance for their respective functions. The NTMA Chief Executive is an ex officio member of the NAMA Board and the NPRF Commission and is Chairman of the NDFA Board. The NTMA acts as the executive in respect of the NPRF and the NDFA. In the case of NAMA, it assigns staff to NAMA and also provides it with business and support services and systems.

7.10 In response to my enquiries in regard to the Agency's internal governance arrangements in the light of this complex range of functions, the CEO informed me that during 2010, the NTMA, in conjunction with the

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69 The total administrative costs of NAMA were €46 million in 2010.

70 The NTMA is governed by the National Treasury Management Agency Act 1990.

Advisory Committee, reviewed the Code of Practice for the Governance of State Bodies (the Code of Practice) and how it could be applied in the context of the NTMA's governance structure. Following this review, the NTMA is implementing the Code of Practice, adapted to its specific circumstances, and the Advisory Committee now formally advises the NTMA Chief Executive on the following matters, on an ongoing basis

- Funding and Debt Management Policy
- Business Function Goals and Objectives
- Delegated Authority Levels
- Remuneration
- Senior Management Performance Appraisal and Succession Planning
- Significant Amendments to the Pension Benefits of Staff
- Corporate Policies and Plans
- Risk Management Policy
- System of Internal Financial Control
- NTMA Annual Report and Accounts
- Appointment of Internal Auditors
- Oversight of Audit Committee (including annual review of Committee terms of reference)
- Operating Budget, and
- Compliance by the NTMA with Statutory and Regulatory Requirements.

7.11 The Advisory Committee has established two sub-committees, an Audit Committee and a Remuneration Committee. The membership of these committees is external to the Agency and formal terms of references, which are subject to periodic review by the Advisory Committee, are in place. The Advisory Committee is also periodically updated by the NTMA on activities across all of its business functions.

7.12 The Agency's senior management team, which includes the heads of each business unit, meets to discuss operational issues on a weekly basis. The team also meets on a bimonthly basis to provide a forum where key strategic and common corporate issues can be addressed and organisational synergies can be realised.

7.13 In regard to the confidentiality of information, the Accounting Officer stated that employees of each business unit are obliged to use the information they receive in the course of their work only for the purposes for which it is obtained. Confidential information may only be communicated to other persons within the Agency on a 'need to know' basis in order for them to perform their duties. The Code of Practice on Confidentiality and Professional Conduct for employees of the Agency (the Code) informs employees of these obligations. Employees are required to sign an undertaking stating that they have read and understood the Code and will observe the requirements restricting the disclosure of information contained therein.

7.14 A separate Code of Practice – Conduct of Officers of NAMA applies to employees who are assigned to NAMA. This contains similar provisions in relation to confidential information and conflicts of interest and has been approved by the Minister for Finance. Additionally, the NDFA operates under a Code of Conduct for the Management of Conflicts of Interest, which has been approved by the Minister for Finance. These codes are supplemented by training undertaken by the Agency's Compliance Officer, which, *inter alia*, advises employees of their obligations in respect of confidentiality and conflicts of interest.

7.15 The Agency's corporate functions were reviewed by Accenture in 2010 and a number of other governance initiatives are being considered.

Accounts of the Agency

7.16 Under the provisions of the National Treasury Management Agency Act 1990, I am required to audit the accounts of the Agency and, when making my statutory annual report under Section 3 of the Comptroller and Auditor General (Amendment) Act 1993, to also make a report to Dáil Éireann on the correctness of the sums brought to account by the Agency in the year.

Conclusion

The Agency's accounts for 2010 have been audited and the accounts, including an administration account and accounts relating to the national debt, have been presented to the Minister who has laid copies of them before both Houses of the Oireachtas.

I am satisfied that the accounts properly present the transactions of the Agency for 2010 and its balances at year end.

The Agency is in the process of further enhancing its governance arrangements which will provide assurance and support to the Accounting Officer who is responsible for its management.

Chapter 2 outlines the outcome of the Agency's debt management activity in 2010 and the amount and composition of Ireland's national debt at 31 December 2010.

Chapter 8

National Pensions Reserve Fund

National Pensions Reserve Fund

8.1 The National Pensions Reserve Fund (NPRF) was established in 2001 with the objective of providing a fund of money to meet a portion of the future costs of social welfare and public service pensions. An independent Commission (the National Pensions Reserve Fund Commission) was established to control and manage the NPRF.

8.2 No Exchequer contribution was made to the NPRF in 2010[71]. However an accelerated contribution of €3 billion made in 2009 included an element of pre-funding for 2010.

Directed Investments

8.3 In 2009, legislation[72] was enacted which permitted the Minister for Finance (the Minister) to direct the Commission to invest in listed financial institutions or to underwrite share issues in those institutions. The Act also provided that the Minister could direct the Commission with regard to the management and disposal of any such investments.

8.4 By the end of 2010, the Commission had effectively assumed the function of an investment vehicle for much of the State's capital injection into the main banks. At that point, the NPRF held 36% of the ordinary share capital in Bank of Ireland (BoI) and 49.9% of the voting ordinary shares in Allied Irish Banks Plc (AIB) together with non-voting shares (which were subsequently converted to ordinary shares in April 2011).

8.5 At 31 December 2010, 34% of the NPRF's resources were devoted to capitalisation of Irish banks and up to a further 44% had been allocated towards the State's contribution to the EU/IMF Programme of Financial Support for Ireland. By April 2011, the NPRF had converted €10 billion of its discretionary investment portfolio into cash and placed it on deposit with Irish commercial banks pending further direction from the Minister as to how this was to be invested.

Investments in Banks

8.6 In March 2009, the Commission was directed by the Minister to invest €3.5 billion in preference shares of BoI and in May 2009 to invest €3.5 billion in preference shares of AIB. In each case, the investment consisted of preference shares which pay an annual non-cumulative fixed dividend of 8% at the bank's discretion. If the dividend is not paid in cash, the NPRF receives its value in ordinary shares. Preference shares which were denominated in units of €1 could be repurchased by the bank at cost within the first five years and thereafter at €1.25 each.

8.7 Warrants attach to the preference shares giving an option to subscribe[73] for ordinary share capital in the bank. The warrants are exercisable anytime between the fifth and tenth anniversary of the date of the issue of the preference stock or in the event of an offer for the bank or other change of control, whichever is earlier.

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71 The adjustment to the contribution rate of 1% of Gross Domestic Product was made by the Credit Institutions (Stabilisation) Act 2010.

72 Investment of the National Pensions Reserve Fund and Miscellaneous Provisions Act 2009.

73 The exercise price for BoI warrants was set at €0.52 for 177,213,784 shares and €0.20 for 157,523,364 shares. The exercise price of AIB warrants was €0.975 for 155,780,375 shares and €0.375 for 138,471,444 shares.

8.8 Share placement arrangements, in which the NPRF was directed by the Minister to participate, were undertaken by both banks during 2010. In addition, the NPRF acquired further shares as a result of dividends paid by the two banks in the form of ordinary shares.

Directed Investments 2010

Bank of Ireland

8.9 In April 2010, BoI announced a plan to raise €3.4 billion equity capital through a share placement and rights issue. The NPRF converted almost 1.7 billion of its preference shares and used the proceeds to

- subscribe for 576 million ordinary shares at a price of €1.80 per unit (€1.04 billion) and
- participate in the rights issue, taking up its full allocation of almost 1,140 million shares at a price of €0.55 (€627 million).

8.10 The total investment in BoI, shown at cost, is set out in Figure 30.

Figure 30 NPRF Investments in Bank of Ireland at Cost

Date	Investment	Preference shares Cost €000	Ordinary shares Cost €000	Total Cost €000
March 2009	Preference shares	3,500,000	–	3,500,000
February 2010	Dividend paid in ordinary shares[a]	–	250,444	250,444
April 2010	Conversion of preference shares to ordinary shares	(1,662,959)	1,662,959	–
December 2010	**Investment at cost**	**1,837,041**	**1,913,403**	**3,750,444**

Note: a In February 2010, the NPRF received a dividend from the BoI of €250 million in the form of ordinary shares.

Allied Irish Banks Plc

8.11 In December 2010, the NPRF participated in a share placement by the bank and subscribed for

- 675 million ordinary shares at a price of €0.3793 per unit (€256 million) and
- 10,489 million cumulative non-voting shares at a price of €0.3396 (€3.562 billion).

8.12 The total investment in AIB, shown at cost, is set out in Figure 31.

Figure 31 NPRF Investments in Allied Irish Banks Plc at Cost

Date	Investment	Preference shares Cost €000	Ordinary and cumulative non-voting shares Cost €000	Total Cost €000
March 2009	Preference shares	3,500,000	–	3,500,000
May 2010	Dividend paid in ordinary shares[a]	–	280,000	280,000
December 2010	Ordinary shares and cumulative non-voting shares[b]	–	3,818,438	3,818,438
December 2010	**Investment at cost**	**3,500,000**	**4,098,438**	**7,598,438**

Notes: a In May 2010, AIB paid the NPRF a dividend of €280 million in the form of ordinary shares.

b 675 million ordinary shares and 10,489 million cumulative non-voting shares. The cumulative non-voting shares ranked pari passu with the ordinary shares except for voting rights and were subsequently converted into ordinary shares (in April 2011).

Return on Investments in 2010

8.13 During 2010, the NPRF received income and gains from its investment in the institutions comprising cash and non cash elements as outlined in Figure 32.

Figure 32 Income and Gains on Investments 2010

Income and Gains	Bank of Ireland €m	Allied Irish Banks Plc €m	Total €m
Cash			
Transaction Fees	64.0	65.9	129.9
Cancellation of warrants (which had been issued in conjunction with 2009 preference shares)	479.0	52.5	531.5
Other			
Dividend (paid in the form of ordinary shares)	250.4	280.0	530.4
Total	**793.4**	**398.4**	**1,191.8**

Value of Directed Investments in 2010

8.14 For the year ended 31 December 2009, the NPRF valued the directed investments at cost under a direction of the Minister. At 31 December 2010, following revised directions from the Minister, the directed investments were valued at fair market value. For the ordinary shares and the cumulative non-voting shares, the market price at 31 December 2010 was taken as the fair market value of the shares. For the preference shares, which are not quoted on the market, the National Treasury Management Agency, on behalf of the NPRF, engaged Davy Corporate Finance (Davy) to provide a fair market valuation of the NPRF's holding in the BoI and AIB preference shares as at 31 December 2010.

8.15 The Davy report, concluded that[74]

- the BoI preference shares had dropped in value by around 20.6% from €1.84 billion to €1.46 billion
- the AIB preference shares had declined in value by around 41.5% from €3.5 billion to €2.05 billion.

8.16 The value of the directed investments at the end of December 2010 is set out in Figure 33. Unrealised losses of €3.7 billion have been reported in the accounts of the NPRF for 2010.

Figure 33 NPRF Directed Investments – Fair Market Valuation at 31 December 2010

	Preference shares	Ordinary shares and cumulative non-voting shares	Total
	€000	€000	€000
Bank of Ireland			
Cost	1,837,041	1,913,403	3,750,444
Unrealised loss at year end	(378,431)	(1,200,950)	(1,579,381)
Valuation December 2010	**1,458,610**	**712,453**	**2,171,063**
Allied Irish Banks Plc			
Cost	3,500,000	4,098,438	7,598,438
Unrealised loss at year end	(1,452,499)	(689,509)	(2,142,008)
Valuation December 2010	**2,047,501**	**3,408,929**	**5,456,430**
Total Directed Investment	**3,506,111**	**4,121,382**	**7,627,493**

Developments Since Year End

8.17 In April 2011, the NPRF converted its cumulative non-voting shareholding in AIB into ordinary shares on a one-for-one basis. Following this conversion, the NPRF held 92.8% of the ordinary share capital of AIB.

Dividends

8.18 In the first half of 2011, the NPRF received dividends on its preference shares as follows

- On 21 February 2011, BoI paid a dividend due of €214.4 million in cash.
- On 13 May 2011, AIB paid part of a dividend due (€280 million) in the form of ordinary shares. The value of those shares was €112.3 million. The balance of the dividend was settled in July 2011 along with a penalty for late payment of shares to the value of €8.8 million.

[74] The shares were valued on the basis of publicly available information – the BoI shares were valued using discounted cash flow analysis of the expected dividends from the preference shares. AIB announced in late December 2010 that it was anticipated that the NPRF would convert up to €3.5 billion of its preference shares into ordinary shares. The valuation of the AIB preference shares took account of this announcement.

Decline in Value of Ordinary Shares

8.19 By the end of July 2011, the value of the NPRF's holdings of ordinary shares in the two banks had fallen

- ordinary shares in BoI had fallen in value by 72% from 37.5 cents to 10.5 cents
- AIB's ordinary shares had decreased by 67% from 30 cents to 10 cents.

Further Directed Investments 2011

8.20 In February and April 2011, the Minister issued two directions to the NPRF to hold a total of €10 billion in cash or debt instruments[75]. The Minister stated that the purpose of the directions was to facilitate a proposed contribution of €10 billion from the NPRF to the EU/IMF Programme of Financial Support for Ireland.

8.21 On foot of these directions, the NPRF liquidated assets from its discretionary portfolio to the value of €5.5 billion in February 2011 and €4.5 billion in April 2011. The cash was placed, again by direction of the Minister, on deposit with Irish commercial banks.

8.22 In July 2011, under further directions from the Minister, the €10 billion which was on deposit with Irish commercial banks was invested in AIB and BoI

- €5 billion was invested in ordinary share capital of AIB bringing the NPRF's shareholding to 99.83% and a capital contribution of €3.77 billion was made to AIB
- the NPRF underwrote a rights issue by BoI and took up the rights attaching to its 36% shareholding at a total cost of €1.23 billion.

8.23 On 24 July 2011, the Minister directed the NPRF to sell part of its shareholding in BoI following the rights issue to a group of institutional shareholders. The NPRF stated that this transaction will generate proceeds for the NPRF of €1.05 billion. Following the transaction, the NPRF's shareholding in BoI will be 15%.

Pension Asset Transfers

8.24 Under the Financial Measures (Miscellaneous Provisions) Act 2009 assets of the pension funds of certain non-commercial State bodies and universities were transferred in the course of 2009 and 2010 to the NPRF. By 31 December 2010 assets with a cumulative value of €2.1 billion had been transferred. The source of the assets transferred is set out in Figure 34. The pension schemes associated with the funds transferred continue in force for existing members with no impact on benefits or associated provisions for members. All future pension costs will be paid, in the first instance, by the relevant State body or university and, after current contributions are exhausted, will be met by way of Oireachtas grant.

8.25 The assets of the pension funds transferred to the Commission in 2009 were valued at €1 billion while the assets of six further pension funds transferred in 2010 were valued at €1.1 billion. The value of each fund transferred is set out in Figure 34.

[75] It was a requirement that such instruments be issued or guaranteed by Eurozone governments and be rated AA or better with a maturity in 2012.

Figure 34 Pension Assets Transferred to the NPRF 2009 and 2010

Responsible State Body/University	Value €m
2009	
Arts Council	2.5
Bord Bia	15.7
National Tourism Development Authority	32.9
FÁS	364.6
Forfás	186.3
National University of Ireland Maynooth	58.5
Shannon Development	52.3
Trinity College Dublin	280.5
2010	
ESRI	17.2
IPA	24.7
National University of Ireland	6.2
National University of Ireland Galway	215.7
University College Dublin	501.6
University College Cork	313.7
Value of Funds Transferred	**2,072.4**

Value of the NPRF

8.26 The value of the NPRF stood at €22.7 billion at 31 December 2010 (2009: €22.3 billion) composed of discretionary investments with a market value of €15.1 billion and directed investments of €7.6 billion. Figure 35 sets out the movement in the NPRF for the year ended 31 December 2010.

Figure 35 Movement in the NPRF Value for 2010

	€m	€m
Value of the NPRF at 1 January 2010		**22,336**
Movements		
Assets transferred from pension schemes	1,079	
Income and gains on discretionary investments	1,824	
Income and gains from directed investments	1,192	
Unrealised loss on directed investments	(3,721)	
Taxation and administration costs	(23)	
Change in Value of the NPRF (including asset transfers)		**351**
Value of the NPRF at 31 December 2010		**22,687**
The assets of the NPRF are composed of		
Discretionary Investments	15,060	
Directed Investments	7,627	**22,687**

Conclusion

The National Pension Reserve Fund (NPRF) was valued at €22.7 billion at the end of 2010.

Up to the end of 2010, the NPRF had invested, pursuant to directions from the Minister for Finance, an aggregate of €11.35 billion in Ireland's two main banks, Allied Irish Banks plc and Bank of Ireland. This included reinvestment of €0.53 billion of dividends received in the form of ordinary shares.

At the end of 2010, as a result of an impairment loss of €3.7 billion, the value of these directed investments had fallen to €7.6 billion.

In 2011, the value of the directed investments has been further impaired. By the end of July 2011, the value of ordinary shares held as part of the investments had fallen from the end-December 2010 values by 67% (Allied Irish Banks plc) and 72% (Bank of Ireland).

In 2011, the NPRF has reinvested a €288 million dividend received in the form of ordinary shares from Allied Irish Banks plc and has liquidated €10 billion of assets in its discretionary portfolio. The NPRF deposited this cash in Irish commercial banks pending further direction from the Minister for Finance.

In July 2011, the Minister for Finance directed that the €10 billion be invested in Allied Irish Banks plc and Bank of Ireland and that the NPRF sell shares to the value of €1.05 billion in Bank of Ireland to a group of institutional investors.

Chapter 9

Public Procurement

Central Government

Public Procurement

9.1 Estimates prepared by the Department of Public Expenditure and Reform (the Department) indicate that public expenditure on procurement of goods and services in 2010 totalled around €9 billion, with a further €6 billion being spent on capital works (see Figure 36).

Figure 36 Estimated Annual Public Procurement Expenditure by Sector

Expenditure area	**2009 €bn**	**2010 €bn**
Health sector[a]	4.70	4.60
Central government sector[b]	2.00	1.95
Local government sector	1.70	1.60
Education sector	0.90	0.90
All goods and services procurement	**9.30**	**9.05**
Capital works	7.00	6.00
Total public procurement	**16.30**	**15.05**

Source: Estimates by Department of Public Expenditure and Reform

Notes: a Includes expenditure relating to drugs and medicines and GP and pharmacist fees.

b Government departments and agencies, including Defence Forces and An Garda Síochána.

9.2 Procurement of goods and services by public bodies must be conducted in accordance with EU and national regulatory requirements. In addition, under guidance issued by the Department there is an obligation on Government agencies to follow a competitive process, carried out in an open, objective and transparent manner.

9.3 At a strategic level, the Department is responsible for setting a broad strategic direction for procurement implementation. This is done through the Department's National Public Procurement Policy Unit (NPPPU), which has responsibility for national public procurement policy, legislation and construction procurement reform.

9.4 A National Procurement Service (NPS)[76] was established in March 2009 within the Office of Public Works (OPW). Its objectives are

- to establish national framework agreements to allow all central government departments and offices, agencies and non-commercial public bodies to procure commonly-used goods and services more effectively, efficiently and with better value for money
- to provide professional procurement advice to central government and non-commercial public sector bodies
- to develop targeted and accredited procurement training and education measures and
- to further develop web-based e-procurement.

[76] The NPS was originally titled the National Public Procurement Operations Unit.

Chapter Focus

This chapter focuses on

- the progress that has been made by the National Procurement Service in implementing initiatives to provide better value in the procurement of goods and services
- the results of a procurement expenditure reduction drive commenced in 2009
- the extent of non-competitive procurement undertaken by government departments in 2010
- the results of an audit review of the implementation of key procedures in relation to procurement rules and regulations
- a review of general findings on non-competitive procurement in the wider public sector.

For purpose of referencing, the department titles used in this chapter are those that applied in 2010. However, the functions of the Department of Finance in this area moved to the Department of Public Expenditure and Reform.

National Procurement Service Initiatives

9.5 The NPS has a wide remit covering central government agencies, non-commercial State bodies, health sector bodies (including the HSE), third level education institutions and local government. The unit has responsibility for managing the purchase of goods and services common to all areas of the public service e.g. office equipment, furniture and fittings, fuel, electricity, natural gas, printing, stationery and office supplies, ICT consumables, uniforms, travel and transport fleets. Procurement of sector-specific items (such as drugs, medical supplies and military equipment) is managed by the relevant departments and agencies.

9.6 The NPS has been staffing up and as of mid July 2011, the unit employed 34 WTE staff. In the past year, it has recruited six new buyers by way of open competition conducted by the Public Appointments Service. The NPS anticipate that it will be close to full complement in early 2012.

9.7 Links have been established between the NPS and the Commercial Contracts Section of the Chief State Solicitors Office (CSSO), which services the needs of central government departments for procurement-related legal advice. The NPS, in partnership with the CSSO and the Office of the Attorney General, developed a suite of standard tender competition and contract documents which was made available to all departments, government offices and agencies in June 2011. Two solicitors have been recruited by the CSSO and seconded to work in the NPS on a full-time basis.

9.8 The NPS budget for non-staff expenditure for 2010 was €769,000, and the outturn was €496,000. The main reason given for the shortfall in expenditure was the fact that the competition for the replacement of the eTenders website was not completed during 2010.[77]

[77] www.eTenders.gov.ie has been developed as part of the Irish Government's strategy for the implementation of e-Procurement in the Irish public sector. The site is designed to be a central facility for all public sector contracting authorities to advertise procurement opportunities and award notices.

Strategic Goals for the NPS

9.9 The NPS Strategy Statement 2010-2012 sets out the approach it will adopt in its first years of operation. It has set three goals. Figure 37 sets out those goals and the achievements in 2010.

Figure 37 NPS Goals and Reported Achievements for 2010

Strategic Goals	2010 Achievements
To optimise the efficiency of, and the value for money obtainable from, all sourcing activities thus enabling public service clients to gain access to quality goods and services to support their business processes.	An analysis of procurement categories was carried out to assess their suitability for NPS intervention. 35 contracts and framework agreements were put in place across various procurement and market categories.
To facilitate the provision of learning, development and guidance opportunities that will assist both procurers and potential suppliers to develop appropriate skills to enable them to operate at optimum capacity in all procurement related business.	A number of training initiatives were delivered for buyers and suppliers. Standard procurement documents and guidance material were developed and distributed with the aim of making procurement by other public bodies in categories not covered by the NPS more effective and efficient.
To ensure the availability of a world-class, e-Procurement platform affording maximum visibility for procurement campaigns.	A competition to replace the eTenders website is being commenced.

Source: National Procurement Service

9.10 The Strategy Statement sets out a number of performance indicators which the NPS has put in place. Annex A provides the detail of the performance measures.[78]

Top Expenditure Areas

9.11 The NPS undertook a survey of public bodies, asking them to report their 'top 30' suppliers of goods and services in 2009. Bodies were also asked to indicate the category of goods and services procured. The survey targeted 310 public bodies in respect of 2009[79] and by the end of June 2011, a total of 257 bodies (83%) had responded. Certain categories of goods and services were excluded from the scope of the survey i.e. professional fees, construction related activities, costs related to the purchase and rent of property and all payroll costs.

9.12 The NPS aggregated the results of the survey by expenditure type. Figure 38 shows the resulting categories of expenditure where the combined reported spend was €50 million or over in 2009. The areas of highest spending were medical supplies, computing, fuel and water.

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[78] The NPS, as a unit of the OPW, will report on progress against all performance indicators in the normal course through the OPW's Annual Report.

[79] The 2009 survey is the most up-to-date survey available.

Figure 38 Top Spending Areas (over €50 million) as reported by Public Bodies within the remit of the NPS for 2009

Procurement Category	€m
Medical supplies	352
ICT and IT consumables	235
Fuel	173
Water	101
Insurance	85
Plant and equipment	56
Telephony	53
General maintenance[a]	53

Source: National Procurement Service analysis

Note: a This includes refurbishment, landscaping and signage.

9.13 The NPS could achieve a more useful analysis of spending by focusing its annual survey on categories of spending on goods and service rather than on major suppliers. Collecting data about all spending by category would allow for development of optimum strategies for procurement from suppliers in sectors where there is more competition or more diversified distribution — such as cleaning, security and professional fees — as well as strategies for procurement in sectors where a limited number of suppliers meet most of the demand.

Development of Framework Agreements

9.14 Another approach of the NPS is to develop national framework agreements in key areas as a means of achieving an impact on public procurement. The general concept of framework agreements is outlined in Annex B. Framework agreements are open for use by public bodies and agencies. However, it is up to the individual organisation to decide whether or not to use the agreements.

9.15 The following categories of spend have been identified as areas suitable for agreements

- stationery (including paper and ICT consumables)
- electricity
- natural gas
- Liquefied petroleum gas (LPG)
- managed print services and
- certain categories of motor vehicle.

9.16 By the end of 2010, the NPS had put a total of 41 framework agreements and contracts in place since its establishment. 35 of those arrangements were put in place in 2010, including electricity and natural gas frameworks with an estimated combined annual value of €400 million. Other framework agreements covered purchase of automotive fuel using charge cards, supply of liquid fuel/LPG and a State advertising framework agreement. The remaining contracts put in place by the NPS covered a wide variety of goods and services ranging from a drawdown contract arrangement for cars for An Garda Síochána and other public bodies (annual value estimated at €4.6 million), to small contracts for printing (e.g. printing of Revenue P35 forms worth an estimated €85,000), a range of contracts for the provision of uniforms and footwear and a contract for the development of a new website for the NPS.

9.17 All NPS framework agreements and contracts contain a ‘contract monitoring’ clause whereby the supplier is obliged to report at regular intervals with regard to elements such as usage, prices and contract expiry, and as required.

General Measures Taken by the NPS

9.18 The Accounting Officer informed me that in the course of 2010 the NPS had undertaken a range of measures designed to improve overall procurement by government bodies

- The NPS has established networks of public service procurement officials to leverage synergies in relevant market areas with a view to encouraging a more collaborative approach to public service procurement.
- An Advisory Board consisting of procurement experts from the public, private and academic sectors was established by the NPS to ensure access to current research and knowledge in all aspects of procurement.
- To further assist in the education and development of public service procurement officials the NPS has, since 2009, hosted three major seminars. These events have become significant occasions for officials who wish to learn more about procurement processes and to benchmark their procurement practices against those of other organisations.
- Cognisant of the need to ensure that suppliers in the market are aware of public service procurement procedures the NPS has hosted, or participated in, 28 supplier and buyer education events, interacting with approximately 500 SMEs.
- To further strengthen communications with both public service buyers and suppliers the NPS signed a contract for the establishment of a new NPS corporate website[80]. This site will serve as a single point of information on public service procurement issues.
- During 2010 the NPS engaged with its counterparts in Europe on various issues relating to EU procurement rules and directives.

Conclusion – National Procurement Service

The NPS has been slow in becoming established. However, by the end of 2010 it had set out its strategic goals, set challenging targets and begun to identify those areas of spend that need to be targeted. In the next stage of its development, it needs to ensure that appropriate approaches to procurement are taken in the areas of major spend and that it monitors the utilisation of framework agreements.

The analysis by the NPS of the major categories of spend could be improved if all spending in a category was aggregated. Currently its review focuses on the major suppliers.

80 The website is www.procurement.ie

Expenditure Reduction Initiative

9.19 In 2009, the Government sought expenditure reductions of up to 8% on contracts for all goods and services purchased by government departments, agencies, offices, third level institutions and local authorities. The procurement savings were to be achieved by reductions in price and/or in the quantity purchased.

9.20 In May 2009, the NPS requested bodies to make a monthly report, listing all contracts for the supply of goods and services with a value over €100,000, beginning in June 2009 and indicating agreed savings on each contract. The initiative excluded expenditure on professional fees[81] and on construction related activities.

9.21 The initial target set for the savings to be achieved through this initiative was €25 million in 2009. Savings of €29.3 million on existing contracts were reported in 2009. In 2010, further savings of €8.8 million were reported under the initiative. This was achieved by continuing to request public bodies to negotiate a reduction of up to 8% on all contracts for goods and services above €100,000 where legally feasible.

9.22 The NPS considers that in addition to the reported savings on existing contracts, public bodies also achieved significant savings by re-tendering for goods and services, and by entering into new contractual arrangements at lower prices. The financial impact of those measures has not been quantified.

9.23 Procurement budgets have been significantly reduced across the public service in 2009 and 2010. In 2010, procurement budgets were reduced by €39 million.

9.24 The Expenditure Reduction Initiative is now considered closed.

Conclusion – Expenditure Reduction Initiative

A drive to reduce expenditure in the area of procurement which began in 2009 resulted in reported savings of €38 million through price reductions. The overall budget for procurement has been reduced by €39 million in 2010.

The NPS believes that further savings were achieved due to re-tendering and new contracts at more competitive prices but those savings have not been quantified.

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81 A separate Department initiative sought a reduction of 8% in professional fee levels, including fees paid to health sector professionals.

Procurement without a Competitive Process

9.25 EU directives set out advertising requirements and tendering procedures for contracts above certain value thresholds that must be applied by all public bodies involved in procurement. For contracts or purchases below the threshold values the following procedures apply

- supplies or services costing less than €5,000 in value may be purchased on the basis of verbal quotes from one or more competing suppliers
- contracts for supplies or services between €5,000 and €25,000 in value should be awarded on the basis of responses to specifications sent by fax or email to at least three suppliers or service providers
- goods and general services with an expected value of €25,000 or more should be advertised on the eTenders website.[82]

9.26 Exceptional arrangements are allowed under national and EU procurement rules in limited circumstances. Department Circular 40/2002 outlines the course to be followed where government departments and offices propose to award contracts that exceed €25,000 in value (exclusive of VAT) without a competitive process. An annual statement (40/2002 return) must be prepared in respect of those contracts, giving the details of the supplier, the nature of the contract, its value and the reasons for not having followed a competitive process. A copy of that statement must be submitted to my Office and to the Department by 31 March of the following year.

Health Service Executive Return

9.27 The 40/2002 return from the Health Service Executive and my comments in relation to it are included in Chapter 42, Procurement in the HSE.

Extent of Non-Competitive Procurement

9.28 The annual 40/2002 returns for 2010 indicate that payments were made under 469 contracts which were concluded without a competitive procurement competition. The total value of the contracts reported for 2010 was €75.4 million. The number of reported non-competitive procurement payments reported decreased marginally in 2010 relative to 2009. However, the value of those contracts increased by €6.3 million .

9.29 Figure 39 shows the number of contracts and the total contract expenditure disclosed in the departmental returns.

[82] Department Circular 10/10, Facilitating SME Participation in Public Procurement, August 2010.

Figure 39 Reported Contracts Awarded without Competition, 2009 and 2010

Department or office [a]	Number of cases		Total contract expenditure	
	2009	2010	2009 €m	2010 €m
Defence[b]	40	62	4.2	15.1
Irish Prison Service	154	124	22.0	14.0
Justice and Law Reform	44	45	5.7	9.6
Office of Public Works	11	18	0.9	6.8
Education and Skills	3	4	1.2	5.4
Garda Síochána[c]	62	33	8.1	5.3
Courts Service	20	30	1.9	3.6
HSE[d]	26	50	4.2	3.5
Property Registration Authority	2	7	0.2	3.2
Foreign Affairs	3	3	0.2	1.7
Agriculture, Fisheries and Food	10	22	5.5	1.4
Tourism, Culture and Sport	9	5	1.2	1.0
Enterprise, Trade and Innovation	11	13	1.0	1.0
Others	78	53	12.8	3.8
Total	**473**	**469**	**69.1**	**75.4**

Source: Circular 40/2002 returns for 2010 received by my Office including subsequent returns received after 31 March 2011 in respect of the Department of Defence and the Valuation Office

Notes:
a There were eight nil returns by departments and offices in 2010 and 14 nil returns by departments and offices in 2009.
b Certain defensive equipment contracts are exempted from the terms of Circular 40/2002.
c The return from An Garda Síochána was adjusted to exclude a contract that had been competitively tendered for and therefore should not have been included on the 40/2002 return.
d 2010 data based on the HSE return received by my Office in June 2011. The return was adjusted to exclude incorrectly reported contracts – nine grant payments and a duplicate contract. Contracts incorrectly omitted are dealt with in Chapter 42.

9.30 The Irish Prison Service (IPS) had the highest reported level of contracts awarded without a competitive process, with expenditure of €14 million on 124 contracts in 2010. This is a reduction on the 2008 and 2009 levels. The IPS has indicated that a further 71 supply arrangements are in the process of having tenders completed which should reduce the levels further in 2011. The IPS has stated that it is working closely with the NPS on a number of collaborative tenders that should provide better value for money in future procurement.

9.31 The Department of Defence reported 62 cases with expenditure of €15.1 million in 2010 that had been awarded without a competitive process. The most valuable contract, worth €6.4 million, was placed with a company, deemed to be the sole supplier in Chad that possessed the necessary capability to assist in the repatriation from that country to Ireland of military personnel and equipment when the mandate for the mission expired on 15 March 2010. The Department of Defence submitted a claim in June 2011 to the United Nations for reimbursement in the amount of €6.4 million in respect of the repatriation expenditure.

Figure 41 Non-Competitive Procurement not included on the 40/2002 Returns

Vote	Number of contracts	Total value €000
Social Protection	1	2,400
Attorney General's Office	5	732
Office of the Director of Public Prosecutions[a]	2	570
Garda Síochána	1	159
Tourism, Culture and Sport	3	139
Taoiseach	3	135
Enterprise, Trade and Innovation	2	91
Foreign Affairs	1	46
Chief State Solicitor's Office	1	37
Charitable Donations and Bequests	1	33
Total	**20**	**4,342**

Source: Office of the Comptroller and Auditor General

Note: a These instances related to contracts originally awarded after tender that were extended to maintain services pending a move to new premises.

Compliance with Administrative Rules

9.36 Circular 40/2002 requires each department or office to

- have a procedure in place under which proposed non-competitive contracts are reviewed prior to award by the relevant department's or office's Internal Audit unit or by an appropriate senior officer who is not part of the procurement process[83]
- appoint a designated Procurement Officer to collate the information on those contracts
- maintain an up-to-date central register of all non-competitive contracts.

9.37 In the course of audit, my Office reviewed the arrangements in place in the 34 government departments or offices in order to ascertain their compliance with the Circular's administrative requirements. The audit found that

- seven departments or offices did not have a procedure in place to review non-competitive contracts prior to their award
- six departments or offices did not maintain a central register of non-competitive contracts. In a further three cases, while a central register of non-competitive contracts was kept, it was not maintained up-to-date
- two departments or offices did not have a designated Procurement Officer in place.

9.38 Figure 42 sets out the audit findings in regard to compliance by the individual departments or offices with the Circular requirements.

83 The Department issued a supplement to Circular 40/2002 in July 2003, providing guidance for officers reviewing the case for such proposed contract awards.

Figure 42 Procurement Systems in Departments[a]

Vote Name	Procurement Officer appointed	Central register maintained[b]	Central register up to date	Independent review procedure in place[c]
Taoiseach	○	○	○	○
Attorney General's Office	○	○	○	○
Central Statistics Office	○	○	○	○
Finance	○	○	○	○
Revenue Commissioners	○	○	○	○
Office of Public Works	○	○	○	○
State Laboratory	○	○	○	●
Chief State Solicitor's Office	○	○	○	○
Director of Public Prosecutions	○	○	○	○
Valuation Office	○	●	●	●
Public Appointments Service	○	○	○	○
Commission for Public Service Appointments	○	○	○	○
Ombudsman's Office	○	○	○	○
Justice and Law Reform	○	○	○	○
Garda Síochána	○	●	●	○
Prisons	○	○	○	○
Courts Service	○	○	○	○
Property Registration Authority	○	○	○	○
Charitable Donations and Bequests	●	●	●	●
Environment, Heritage and Local Government	○	○	○	○
Education and Skills	●	○	○	○
Community, Equality and Gaeltacht Affairs	○	●	●	○
Foreign Affairs	○	○	●	○
International Cooperation	○	○	○	●
Communications, Energy and Natural Resources	○	○	○	○
Agriculture, Fisheries and Food	○	○	●	●
Transport	○	○	○	○
National Gallery of Ireland	○	●	●	○
Enterprise, Trade and Innovation	○	○	○	○
Tourism, Culture and Sport	○	●	●	●
Defence	○	○	○	○
Army Pensions	○	○	○	○
Social Protection	○	○	●	○
Health and Children	○	○	○	●

Key: ○ Yes ● No

Notes:
a The systems referred to are those related to the provisions of Circular 40/2002.
b This is a register of non-competitive procurement only.
c The circular requires this review to be conducted by Internal Audit or a senior officer who is not part of the procurement process.

9.44 Chairpersons of State bodies must attest annually in a statement on internal financial control that their respective organisations have effective internal control systems (which include controls over procurement). The Code also requires the Chairperson to annually affirm compliance with procurement procedures to the relevant Minister. For good corporate governance, it is essential that each Board of a State body has appropriate processes in place that will provide assurance to its Chairperson that the annual confirmation on compliance with procurement rules and procedures can be made.

9.45 As in the case of departments, it may be appropriate for State agencies to depart from normal procurement rules in exceptional circumstances. However, their procurement procedures should state the general circumstances in which departures would be appropriate (e.g. urgent need). In addition, the reasons for the departure should be documented in advance and the departure should be approved at a more senior level than the person requesting that departure. Although government departments and offices are required to make an annual return[84] about non-competitive procurements, there is no such onus on State agencies.

9.46 In procuring goods and services, public bodies should follow a competitive process that is carried out in an open, objective and transparent manner. They should also seek to apply good contract management principles to achieve best value for money. However, the existence of formal procurement policies and guidelines within an organisation does not guarantee that they will be observed or that national public procurement policy will not be breached.

9.47 In previous reports, I have drawn attention to weaknesses in procurement procedures in public bodies, including

- Beaumont Hospital (Special Report 10, May 2008)
- FÁS (Special Report 73, December 2009)
- HSE Skill Programme (Report of the Comptroller and Auditor General, 2009).

9.48 Instances continue to be noted on audits of State bodies where procurement does not appear to have operated in an open way. Reports under Section 7 of the Comptroller and Auditor General (Amendment) Act 1993 also deal with such issues. These types of reports have issued or are in the course of preparation in the case of three Vocational Education Committees. A further instance of where procurement does not appear to have operated in an open way in the case of a State body is outlined below.

The National Library of Ireland – Procurement of Services

9.49 The National Library of Ireland was established as an autonomous cultural institution under the National Cultural Institutions Act 1997. The Library's total annual expenditure was in the order of €12 million in 2009. Procurement of services to support its administration and cultural programmes accounted for €2.6 million in 2009 and €2.9 million in 2010.

[84] The return, under Circular 40/2002, is made to both the Department and to the Comptroller and Auditor General.

9.50 The Library commenced a tender competition to procure research services on 15 April 2008 by publishing a notice on the e-tenders website for ‘Placement of a Panel to provide Supplementary Research Services’. The Request for Tender (RFT) specified a range of skills required including a ‘*proven track record working on exhibitions and publications*’ and ‘*an ability to write in a clear and concise fashion and produce texts suitable for different contexts*.’ It was pointed out that successful tenderers would be placed on a panel of researchers, but that contracts for work would be awarded at the discretion of the National Library.

9.51 A key project in respect of which research input was required by the Library was one which aimed to produce an exhibition and an associated book about the Library’s ‘treasures’. Following receipt of a tender on 28 April 2008, a researcher was engaged on 1 May 2008 on a one-year contract to work on the project.

9.52 The total cost of the book including publication costs was €98,000. Ancillary costs of €33,000 were also incurred.

9.53 The planned book, entitled ‘The National Library of Ireland’, was published in April 2009. However, shortly after publication, the Library was obliged to withdraw the book from public sale due to errors and other defects.

Review Findings

9.54 A review by the Library, carried out after the book had been withdrawn from sale, found a number of deficiencies in the manner in which the Library had carried out the tender competition and the award of the contract to the selected researcher.

- The tender submitted by the researcher on 28 April 2008 was evaluated by one member of staff of the Library and there was no documentary evidence of the evaluation and scoring.
- A day after receipt of the first tender, a contract was offered to the tenderer providing for her ‘*to carry out research, produce texts and engage in other tasks as required in order to produce an exhibition and publications on the general theme of (National Library of Ireland) treasures scheduled to open in Spring 2009*.’
- The contract did not specify a limit on expenditure but rather fees to be charged per hour, per half day or per full day. The contract was dated 1 May 2008 and specified a term of 12 months, ending April 2009.
- There was no documentary evidence that the three other tender submissions received later in response to the Library’s RFT were formally evaluated and no other applicant was assigned to the panel of researchers, or awarded a contract.

9.55 In relation to the management of the contract with the researcher, the review concluded that

- the contract lacked clarity as to detail about the work to be performed, the time frame for completion and a limit on the expenditure involved
- there had been a lack of clarity in the contract agreed with the researcher about how the work would be supervised and monitored
- there were deficiencies in the management of the project in that no project plan had been developed and that the responsibilities for proof reading had been unclear.

9.56 The then Chairman of the Board of the Library[85] sent his report for 2008 to the Minister for Arts, Sport and Tourism on 13 November 2009. In the report, he gave a positive affirmation regarding compliance with procurement procedures. However, his report for the year 2009 (dated 30 April 2010) brings the Minister's attention to the failure of proper procurement procedures that occurred in 2008 but which was uncovered in 2009.

9.57 The Chairman submitted the internal enquiry report into the procurement difficulties that had arisen along with his report for 2009 to the Minister. He stated that he was satisfied that the failure that had occurred, in the department of the Library involved, had been specific to the management of and control over that department and did not indicate a more general problem in the Library. He concluded by reporting that appropriate procedures for procurement were being implemented by the Library.

Views of the National Library

9.58 The current Director of the National Library[86] acknowledged that procurement procedures had not been followed in this case. The Director emphasised that the Library took this matter extremely seriously and outlined the actions taken to address the issues that arose. She set out the following actions that have been taken.

- Disciplinary action was taken against two members of staff involved in the project.
- The Library had taken a number of steps to strengthen its procedures and controls in order to address any weaknesses. These included procurement training for all managers and the appointment of a staff member as Procurement Officer who had undertaken further detailed training in public procurement.
- The Library now requires managers to prepare a business case for all projects over €25,000 in value, which are reviewed, in the first instance, by the Library's Management Advisory Committee. If the estimated cost exceeds €50,000, it is subject to Board approval. The business case outlines the key elements to be considered in the procurement process including business need, anticipated benefits and outcomes, procurement plan, costs, timescales and risks.
- The Library has drafted a detailed procurement policy and related procedures with guidelines, templates and checklists to aid in the tendering process.
- The Library requested its newly appointed internal auditors to prioritise a review of procurement in the 2011 Internal Audit plan and this audit had been completed.

9.59 The Director stated that the Library is satisfied that it has invested significant effort into improving procurement and contract management practices in an effort to provide best value for public expenditure.

9.60 In response to my enquiries regarding management assurances given to the Board, the Director stated that the Library provides the appropriate management assurances to enable the Board to fulfil its obligations by

- preparation of annual budgets which are approved by the Board
- provision of regular financial updates on actual expenditure compared to budget and analysis of any material variances
- the presentation of business cases with an estimated cost in excess of €50,000 to the Board for approval[87]

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85 The current Chairman was appointed on 30 April 2010.

86 The current Director was appointed on 8 March 2010.

87 The Library has reduced the expenditure levels requiring Board approval from €100,000 to €50,000.

- an annual programme of internal audits agreed by the Board Audit Committee and reports by the internal auditors on their findings to the Audit Committee.

Conclusion – Wider Public Sector Procurement

Deficiencies in procurement practices relating to State bodies have been reported in a number of special reports under Section 11 of the Comptroller and Auditor General (Amendment) Act 1993 and three reports under Section 7 of the Act have issued or are in the course of preparation that related to procurement matters in Vocational Education Committees.

Due to the level of errors and other defects, the National Library of Ireland was obliged to withdraw a book from publication, which had cost almost €98,000 to produce. There was a failure to carry out the related procurement of research services in an open and competitive way.

At present, Circular 40/2002 applies only to government departments and offices. In the light of failures to observe procurement practices in a number of instances, there would be merit in considering widening its application to State bodies under the aegis of departments. By extending the scope of the Circular, or through some analogous procedure, departments could strengthen overall procurement compliance. However, this would need to be done in the context of the evolving public procurement framework which needs to ensure that

- there is accurate information on the classification of purchases
- there is a response to that information through choosing the most appropriate procurement approach
- non-competitive procurement is minimised.

The nature of monitoring and reporting may need to adjust to these system changes so as to give equal weight to rule conformance and value achievement.

Annex A Performance Measurement by the NPS

Performance Indicator	Method of Measurement	Frequency of Measurement
€50 million in cost savings through all interventions in 2011	Analysis of cost savings and estimate of administrative savings	Monitored throughout year and measured at year end
50% of all targeted public sector clients joined as parties to all contracts completed in 2011	Contract monitoring	Monitored throughout year and measured at year end
70% of all targeted public sector clients joined as parties to all contracts completed in 2012	Contract monitoring	Monitored throughout year and measured at year end
40% of Public Service's 'Top 30' spend categories to be under new contracts by end 2011	Analysis of contracts against 'Top 30' spend data	Monitored throughout year and measured at year end
50% of Public Service's 'Top 30' spend categories to be under new contracts by end 2012	Analysis of contracts against 'Top 30' spend data	Monitored throughout year and measured at year end
80% usage of Standard Documents by Central Government Departments by the end of the third quarter, 2011	Adoption by Central Government Departments of the standard suite of documents for standard goods and services	Monitored throughout the year and measured at year end
Complete 10 supplier seminars/ interventions annually	Diary of events	Annual
Complete 3 Procurement Officer seminars annually	Diary of events	Annual
Complete 5 Procurement Officer workshops annually	Diary of events	Annual
80% roll-out of eTenders modules by the end of 2011 and full implementation thereafter	Modules available to Buyers and Suppliers	Monitored throughout year and measured at year end
Publish information on the NPS website in relation to 100% of the contracts that are available for use by public sector bodies	Website content compared with live contracts	Quarterly review
Contribute to the development of an eInvoicing strategy. Strategy in place by end 2011	Date of completion of strategy documentation.	End of year review of progress on eInvoicing
Support uptake and implementation of eInvoicing across the public sector	Extent of progress in eInvoicing implementations in place or in progress.	End of year review of progress on eInvoicing

Annex B Framework Agreements

The concept of a framework agreement was clarified by an EU Directive in 2004. The Directive defined a framework agreement as an agreement with suppliers, the purpose of which is to establish the terms governing contracts to be awarded during a given period, in particular with regard to price and quality. They set out terms and conditions under which specific purchases (call-offs) can be made throughout the term of the agreement.

The framework agreement may, itself, be a contract to which the EU procurement rules apply if it creates an obligation to purchase. However, the term is normally used to cover agreements which are not, themselves, covered by the definition of a contract to which the EU rules apply (though they may create certain contractually binding obligations).

Such agreements set out the terms and conditions for subsequent call-offs but place no obligations in themselves on the procurers to buy anything. With this approach, contracts are formed, in EU Directive terms, only when goods, works and services are called off under the agreement. A benefit of this type of agreement is that, because authorities are not tied to them, they are free to use the frameworks when they provide value for money, but to go elsewhere if they do not.

However, in order to avoid conflict with EU rules, it is more practical to treat the framework agreements as if they are contracts in their own right for the purposes of application of the EU rules. Therefore, the practice has been to advertise the framework itself in the Official Journal of the EU (OJEU).

This provides transparency for the whole requirement across the EU and it removes the need to advertise and apply the award procedures for each call-off under the agreement, on the basis that the framework establishes the fundamental terms on which subsequent contracts are awarded.

Framework agreements can be with one or more participants.

In a one party agreement, terms for the provision of works, supplies or services will be settled with one supplier based on a competitive tendering process. Requirements will be drawn down on the agreed terms as they arise over the period of the agreement. Most of the terms will be established including price and delivery times but some, for example, total quantities, may not.

A multi-party framework can be established by inviting and selecting suitable parties to participate. The criteria for the award of subsequent contracts will have been set out. Precise specifications or prices may not be established. As requirements arise, an authority will contact the participants in the framework and invite them to submit competitive bids in “mini-competitions”. The bids received are evaluated and contracts awarded on the basis of the criteria specified in the rules of the framework.

Annex C Reasons Provided for Non-Competitive Procurement

Figure 40 sets out the reasons provided by departments and offices for not having followed a competitive procurement process for 2009 and 2010. This Annex provides details on the highest value contracts awarded in 2010 in respect of each category of reason cited.

Urgency Exception – €3.6 million

The most significant recourse to non-competitive procurement under this exception in 2010 was by the Department of Foreign Affairs. This involved the purchase of passport production equipment to replace equipment damaged by water from premises over the Passport Office at a cost of €1.4 million. The Department deemed it necessary to award this contract to ensure the continuity of supply of passports and the need for technical compatibility with existing infrastructure.

Proprietary Goods Exception – €14.2 million

Of the 91 instances of purchasing of proprietary goods contained in the 2010 departmental returns, 28 were in respect of purchases by the Garda Síochána with a value of €5 million; and 14 were in respect of purchases by the IPS with a value of €5.1 million. The proprietary goods purchased, in general, related to information and communications technology or to technical systems.

Extension/Rollover Contracts Exception – €19.4 million

114 cases reported involved the extension or rolling-over of existing contracts for goods and services. Some of the contracts extended or rolled over had been in place for several years.

Justifications reported by departments and agencies for continuing with existing contractual arrangements included

- the contractor had relevant experience gained from prior involvement with the department
- the contractor was best placed to provide the required goods/services without undue extra cost to the Exchequer
- it was not possible to go to the market due to staffing difficulties.

Almost all of the contracts in this category are for the provision of services. Examples include

- The extension of two contracts with a combined value of €4.2 million by the Department of Education and Skills for the licensing, support and maintenance of management information software for schools.
- Payments totalling €2.1 million by the Department of Justice and Law Reform in respect of some segments of the Department's and agencies' Local and Wide Area Networks.
- The extension by the Department of Education and Skills, at a maximum cost of €1 million, of a contract for the operation of Irish language examinations for primary school teachers who obtained their teaching qualifications outside the State.
- The extension by the Department of Justice and Law Reform of a contract at a cost of €0.9 million for air transport for deportation flights.

Expert or Recent Experience Exception – €4.4 million

45 cases were reported where departments and offices took the view that their interest was best served by entering contracts where they had used the services of individuals or firms in the recent past or had identified, without recourse to competitive processes, persons or firms whose expertise coincided with their requirements. This does not exclude the possibility that there might be other suitable suppliers. Examples include

- The hiring by the Department of Justice and Law Reform, at a cost of €1.1 million in 2010, of a group of four suppliers deemed uniquely qualified to provide gravesite surveying, excavation and archaeological forensic services to assist in the location of victims remains.
- The hiring of festival organisers to manage and organise the St. Patrick's Day festival on behalf of the Department of Tourism, Culture and Sport and Fáilte Ireland at a cost of €0.5 million.
- The purchase of parachutes and parachute systems by the Department of Defence at a cost of €0.3 million.

Single Suitable Supplier Exception – €25.3 million

This category relates to procurements where departments and offices consider there is only one suitable supplier of the required service. In 2010, expenditure was incurred under 92 single supplier contracts.

The largest contract in this category totalled €6.4 million and related to the repatriation of Department of Defence personnel and material from Chad back to Ireland.

Other high value contracts were awarded by the following departments or offices

- The Office of Public Works, in order to ensure the credibility of the Flood Hazard Mapping website entered into a contract, at a cost of €4.1 million with the State mapping agency Ordnance Survey Ireland (OSI), to produce digital maps for the whole country and keep that data up-to-date.
- The Property Registration Authority entered into a contract at a cost of €2.9 million with OSI for national mapping data.
- The Department of Defence entered two contracts for equipment/spare parts costing €2.7 million in aggregate.
- The Courts Services entered into a contract at a cost of €1.2 million for postal services.

Security Considerations – €1.5 million

Competition was limited in the interests of security in seven instances reported in the returns.

Other Reasons – €7 million

There were 108 reported instances of contracts being awarded for a variety of other reasons. Of these, 89 contracts were awarded by the IPS, at a total cost of €6.2 million. A large number of these were in respect of the local purchase of various goods and services such as cleaning, catering and transport services as well as the purchase of televisions and electrical equipment.

Chapter 10

Performance Management and Development

Performance Management and Development

10.1 In 2010, approximately 36,400 staff were employed in the civil service. The related pay bill, was around €1.7 billion. The effective management of civil service human resources is critical, if the State is to maximise value in the form of directed, focused activities from its workforce.

10.2 In May 2000, agreement was reached between civil service management and unions[88] on the implementation of a Performance Management and Development System (PMDS). Under this system, each employee's role and development needs are reviewed annually by his/her manager. The process is designed to help establish a shared understanding between the jobholder and the supervisor of the performance standard to be achieved and how it is to be achieved. The establishment of each jobholder's role profile in this way seeks to link an individual employee's objectives to the business plans of the unit in which he or she works.

10.3 Following a formal review of the initial phase of implementation of the system[89], the PMDS process was revised under the terms of a further management/union agreement in May 2005. This had the objective of integrating PMDS with other civil service human resource processes. Accordingly, the revised arrangements provided for each staff member's individual performance to be linked with the awarding of pay increments, eligibility for promotion and advancement to higher scales within existing grades. This direct linking of aspects of reward and career advancement to performance appraisal makes it important to ensure, both from the viewpoint of individual fairness and system effectiveness, that

- performance ratings are awarded on a consistent basis
- the award of pay increments is effectively linked to the rating results
- the system is used to address and enhance performance and aid individual development interventions.

10.4 The introduction of PMDS was part of a wider human resource management (HRM) change that included devolution of more autonomy and responsibility for the management of staff to local managers. Features of this devolution included giving departments more control over the recruitment, promotion and placement of staff in order to ensure that the skills and competencies required by departments are met. At workplace level, managers were assigned increased responsibility and accountability for HRM functions such as management of annual leave and flexitime.

10.5 At national level, the Department of the Taoiseach and the Department of Finance shared responsibility for development and oversight of implementation of the PMDS. On 4 July 2011, all central responsibility for PMDS was transferred from these two Departments to the Department of Public Expenditure and Reform, which now has responsibility for all issues relating to civil service remuneration and employment[90]. Responsibility for the application of the PMDS within individual civil service departments[91] lies with the HRM function.

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88 Changes to terms and conditions of employment for Civil Servants are agreed by a representative body made up of management and staff representatives. This is known as General Council. Three General Council Reports preceeded implementation and enhancements of the PMDS since 2000. The reports have been underpinned by provisions in successive social partnership agreements.

89 Mercer Human Resource Consulting, June 2004.

90 The Department of Public Service and Reform is attributed with responsibility for PMDS matters, except where it is necessary in the interests of greater clarity to refer to the Department of Finance, which had earlier responsibility.

91 The term department includes all central Government departments and offices.

Chapter Focus

The chapter reports the result of a review which sought to establish

- the consistency and quality of the PMDS assessment process
- the extent of timely compliance with PMDS
- whether pay increments are effectively linked to appraisal results and appraisals are carried out on all staff
- how well the system is contributing to competency development and performance improvement.

Assessment of the way in which objectives, workloads and competencies were allocated to jobholders was not included in the scope of the chapter.

10.6 The main elements of the review were

- analysis of annual returns by departments submitted to the Department of Public Expenditure and Reform around April each year reporting on the results of the PMDS process for the previous calendar year. This process commenced for the first time in 2009 and data for 2007 and 2008 was requested.
- interviews with the HR managers in four departments[92] to establish how PMDS is being implemented at individual department level
- a sample-based review of cases in four other departments[93] where pay increments were due to be awarded to establish compliance with PMDS requirements
- a focus group discussion to obtain the views of personnel managers in relation to ratings, consistency, underperformance and competency development.

10.7 A consultant[94] assisted my office in establishing criteria for this review.

10.8 The titles of departments used in this report are those that pertained at the time the matters reported on were surveyed or examined.

Consistency of Performance Assessments

10.9 The 2004 review of the operation of the PMDS concluded that there had been difficulties with the rating system applied in the initial years of operation of the system, and that a more robust rating system was required. In response to the findings, General Council Report 1452 (agreed in May 2005) set out a revised rating system to be applied in carrying out the assessment of individual performance. The five-point rating scale proposed in the report (see

10.10 Figure 43) was designed to reflect the full spectrum of performance that is typically found in civil service departments.

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92 Courts Service, Department of Enterprise, Trade and Employment, Department of Health and Children, Department of Social Protection.

93 Department of Agriculture, Fisheries and Food, Department of Justice and Law Reform, Department of Community, Equality and Gaeltacht Affairs, Department of the Taoiseach.

94 The consultant was Dr Gerry McMahon.

Figure 43 Expected Distribution of Assessment Ratings

Rating	Description	Suggested rating distribution
5	**Outstanding:** the role holder has substantially exceeded standard in all role requirements and performance has been consistently exceptional	0 -10% of staff
4	**Exceeds required standard:** the role holder has fully met all role requirements to the required standard and significantly exceeded the standard in some respects	20-30% of staff
3	**Fully acceptable:** the role holder has met all of the role requirements to the required standard and performance is at a fully acceptable level	40-60% of staff
2	**Needs improvement:** the role holder has met some role requirements to the required standard but performance has fallen short in some respects	10-20% of staff
1	**Unacceptable:** the role holder has met few of the role requirements and performance falls clearly short of the required standard	0-10% of staff

Source: Appendix, General Council Report 1452

10.11 In addition to providing a description of the rating assessment that is associated with each of the rating levels, the General Council Report included a suggested rating distribution to assist managers when making assessments. The suggested distribution was not based on firm empirical evidence about expected performance. Instead, it is intended to illustrate a broad pattern at organisational level. The report emphasised that each job-holder must be assessed on an individual basis and on their own merits, and that (individual) expected performance must take into account the usual range of factors such as skills, experience and time in the job.

10.12 The assessment form used to record the performance rating assigned also requires a narrative assessment to be provided. This is partly intended to refer to any factors outside the control of the job-holder which impacted on the individual's performance.

10.13 The audit reviewed the outturn ratings based on data collected by the Department of Public Expenditure and Reform for the years 2007 to 2009. The distribution of the average ratings for the three years is depicted in Figure 44, and compared with the rating distribution pattern suggested in Report 1452.

Figure 44 Performance Assessment Rating Outturn, 2007 to 2009[a]

Source: Analysis of departmental returns to Department of Finance

Note: a Results shown are based on the assessment ratings recorded for around 19,000 staff on average each year 2007 to 2009 inclusive.

10.14 The rating pattern indicates that more staff than that suggested by the General Council Report were awarded ratings at the higher end of the scale and fewer at the lower end.

10.15 This skewing was also noted in each of four departments examined as part of this review. In those cases, the skewing was even more pronounced. Approximately 60% of staff in the departments examined were rated at ‘4’ (higher than the 50% generally) and less than a third were rated a ‘3’ (less than the 40% shown in Figure 44).

Consistency Checks

10.16 Departments, through their HRM functions, are expected to ensure that the system is applied in a consistent, fair and equitable manner across all staff in the organisation and to monitor the actual ratings awarded over time.

10.17 Two departments reported that they complete consistency checks on a sample of ratings[95]. In addition to this internal review, one department also examined the distribution of ratings and recommended that managers consider a proposed rating in the context of the wider workplace functional area in which the jobholder is placed before awarding the individual a rating.

10.18 The audit noted examples of actions taken by departments to ensure consistent assessment, including

- Managers assigning ratings to staff in a section meet to agree an approach to completing annual reviews and to discuss the distribution of ratings to ensure it stays within the General Council distribution.
- Issuing examples of narratives to accompany ratings to senior managers, to ensure higher quality narratives (Department of Enterprise, Trade and Employment)
- Management Advisory Committee members meeting collectively to consider ratings for Principal Officers, and Principal Officers meeting to discuss the distribution of ratings for Assistant Principals (Department of Health and Children).

Review Process

10.19 PMDS also incorporates a system of formal review in cases where jobholders are dissatisfied with the performance assessment proposed by their manager. The reviewer must be of a higher grade than the manager who gave the original rating.

10.20 The role of reviewers as set out in the initial General Council agreement establishing PMDS indicates that, as well as the role they play in the event of differing views arising between jobholders and managers, they should

- be proactively involved in the development of the PMDS, including reviewing role profiles to ensure that they are consistent, fair and relevant to the needs of their business unit
- ensure consistency and correct application of the PMDS to a high standard and coach managers to develop their feedback skills.

95 The Department of Enterprise, Trade and Employment and the Department of Social Protection.

10.21 The audit found that the role of reviewer in departments is generally not a permanent designated role and fulfils no role outside of dispute resolution. By not having a designated formal reviewer for each section/division, it is difficult for the role to have a positive input into the consistency of the operation of PMDS.

10.22 The focus group of personnel managers were generally agreed that jobholders perceived ratings less than '4' in a negative light and, from the managers' perspective awarding those ratings, was regarded as bothersome in terms of the consequential burden of justifying the rating to the employee, sometimes involving appeals processes but also in the negative atmosphere generated in the workplace as a result.

10.23 Some members of the group noted a general expectation on the part of jobholders that ratings should not disimprove over time or with promotional advancement. This appeared to be counter intuitive to what might be expected in career progression in that a newly promoted jobholder is normally training and developing to be effective at the new grade and, therefore, would not normally immediately be at a standard equivalent to that at which they were in their previous position.

Conclusion – Rating Consistency

The results of PMDS assessments suggest a risk that underperformance is not being identified and, consequently, is not being adequately addressed. They also suggest that pay and advancement decisions may not reflect actual performance. However, this risk may need to be examined in a wider context and it would be desirable to attempt to establish whether in the context of the civil service the suggested pattern in General Council Report 1452 applies in fact and, if so, to address the consistency of awards.

It might also be useful to consider the scale itself since department Personnel Managers surveyed as part of this examination generally considered that a '3' grade is a negative rating in the view of their staff. In addition to this, where appeals were made to a reviewer, they noted that jobholders were appealing ratings of '3' or '4' as opposed to appealing ratings at the lower end of the scale.

To ensure ratings are applied in a consistent, fair and equitable manner across all staff in the organisation, departments should monitor the actual ratings awarded over time and ensure that the in-built review function is operating.

In general, the review of rating consistency should be followed by communication of the results and implications to managers and jobholders. Potential ways of addressing consistency are

- ensuring that the numerical rating aligns with the description of the performance captured on the review form
- examining the overall distribution against the expected pattern
- periodic review of the scale and ratings distributions to ensure they reflect the current work arrangements.

Views of the Accounting Officer

10.24 It is the opinion of the Department of Public Expenditure and Reform that the way in which objectives, workloads and competencies are allocated to jobholders is a critical element of fairness and consistency. It states that this has a direct bearing on how easy or difficult it may be for a jobholder to achieve their goals and therefore get a higher rating.

Compliance with PMDS

10.25 Analysis by the Department of Public Expenditure and Reform of the PMDS returns from departments indicates that, at the time they reported, PMDS annual reviews for 2009 had been completed for just 56% of staff across departments. This was down from the 70% average completion rate reported in respect of 2007 annual reviews.

10.26 As Figure 45 indicates, there was considerable variation between departments in the reported rate of completion of the 2009 annual review forms. This varied from full or almost full compliance in a number of offices of central government to a rate of just 18% in the Department of Social Protection, where industrial relations difficulties resulted in non-completion of the reviews[96].

10.27 The timeframe in which the results data has to be returned to the Department of Public Expenditure and Reform is a source of difficulty for the reliability of any PMDS compliance rate calculated based on the returns. The data reported by the Department for the period 2007 to 2009 was collated in the first quarter of each succeeding year. For 2007 (the first year for the collection of data), returns had to be made by February 2009. Departments report an increase in the compliance rate as the year progresses and as increment dates take effect. In recognition of this, the Department of Public Expenditure and Reform extended to 15 April 2011 the date for return of results for 2010. Thus, the data reported represents completion rates at the reporting date, and not the final rate, which continues to be updated over the year.

Conclusion – Compliance with PMDS

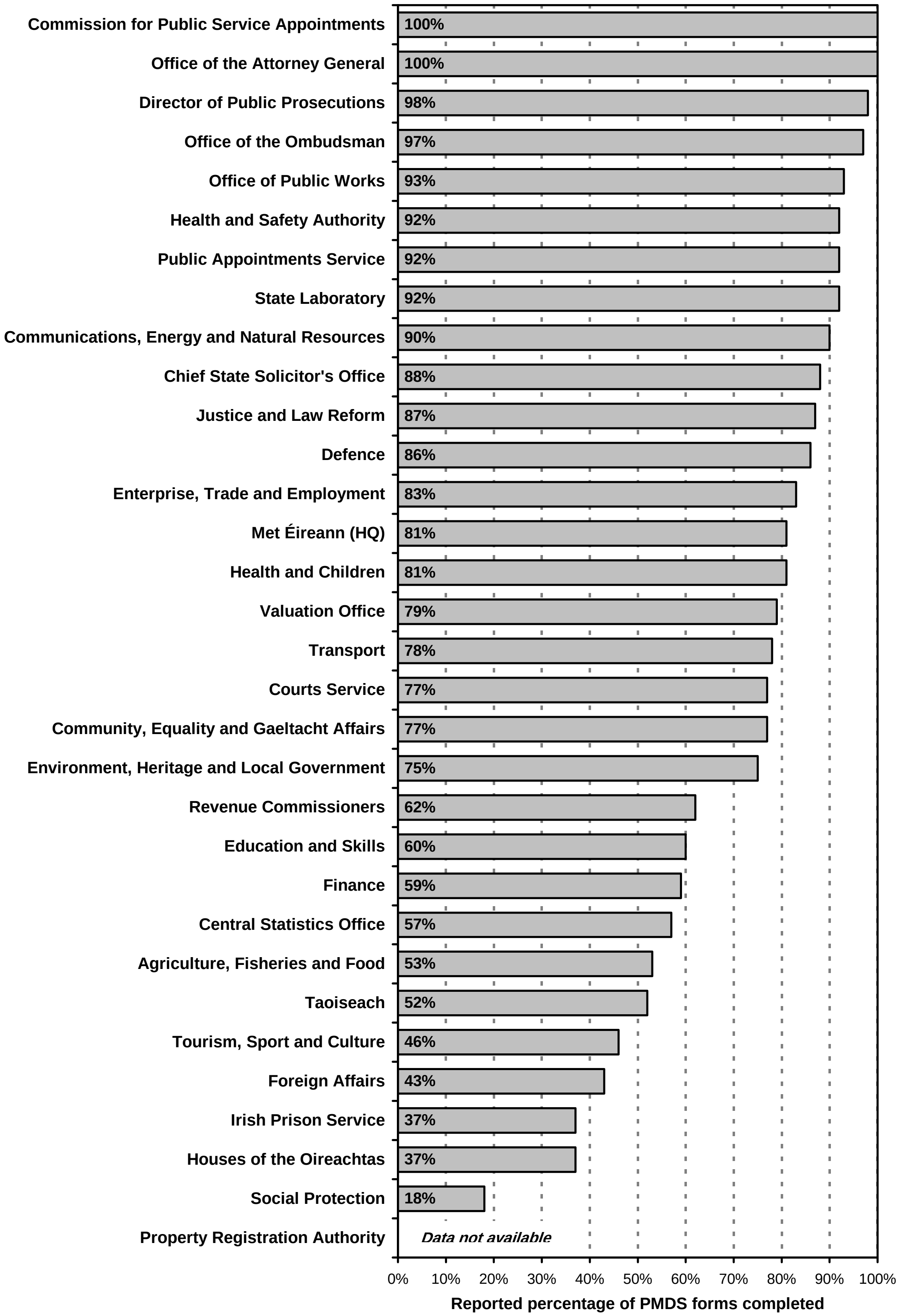
Point in time surveys by the Department of Finance suggest that there are delays in completion of assessments and that this had deteriorated somewhat in 2009. In that year, the overall compliance rate was 56%.

Views of the Accounting Officer

10.28 The Accounting Officer of the Department of Public Expenditure and Reform stated that his Department is taking steps to improve compliance and consistency, primarily by gathering data on compliance with a view to publishing the rates of compliance by departments and offices across the civil service. He has reported that compliance has increased by 13% in 2010.

[96] 60% of the Department's staff were affected by the industrial action, and there is a considerable improvement in compliance since, rising to 80% for 2010.

Figure 45 Reported Percentage of 2009 PMDS Annual Reviews Completed, by Department/Office[a]



Source: Departmental returns to the Department of Public Expenditure and Reform (then part of the Department of Finance)

Note: a Some department titles have changed due to reorganisations since the data was compiled. The original department name has been used.

PMDS and Award of Increments

10.29 Most civil service salaries are based on grade-specific pay scales, with a number of pay increases (increments) payable, usually at yearly intervals. Increments awarded or due for payment across the civil service as a whole are in the order of €40 million a year.

10.30 Up to 2005, recommendations for the award of pay increments were based on individual reviews that were additional to the PMDS assessments, with sick leave and attendance records also being taken into account in the final decision. Since 2005, the award of pay increments to civil servants has been conditional on the prior completion of a PMDS annual review and on receiving a minimum rating of '2' in the annual PMDS review assessment. As before, the individual staff member's sick leave and attendance records continue to be taken into account in the increment award decision.

10.31 Apart from the risk that annual increments of pay may be given in instances of poor performance due to 'assessment rate inflation', the Department of Public Expenditure and Reform's analysis indicating just 56% compliance with PMDS reviews gave rise to a risk that awards of incremental pay increases might have been made even in the absence of appraisal. I considered it important to review whether and to what extent that risk may have actually materialised.

10.32 The audit examined the procedures for awarding increments in four departments. In those four departments annual reviews and ratings were checked for all staff that were due an increment in May 2010 (see Figure 46). Overall, the audit found that almost all increments awarded were supported by prior annual reviews. In 9% of the cases examined, payment of the increment was delayed because the PMDS annual review form had not been completed. Two thirds of these delayed increments were paid by July 2010. The remainder of the delayed cases were paid by end 2010, with one exception which was paid in February 2011. In a further 7% of cases, the increment was withheld because of an unsatisfactory sick leave record. In 1.2% of the cases examined, increments were withheld as PMDS reviews had not been completed.

Figure 46 PMDS Annual Review Compliance for Award of May 2010 Pay Increments – Selected Departments[a]

Department	Increments due for payment in May 2010	Annual review completed and increment paid on due date	Increment delayed because		Increment not paid; PMDS review not completed
			PMDS review not completed on time	Excess sick leave	
Justice and Law Reform	112	107	3	–	2
Agriculture, Fisheries and Food	108	73[b]	18	16	1
Taoiseach	11	10	1	–	–
Community, Equality and Gaeltacht Affairs	11	11[b]	–	–	–

Notes: a Some department titles may have changed due to reorganisations since May 2010

b One person was paid an increment without prior completion of a PMDS assessment.

10.33 The audit noted some systematic issues

- There is a risk in instances where payment systems are not driven by authorisations from the human resource function that pay increments would be paid without appraisal or where appraisals do not warrant it. In the Department of Community, Equality and Gaeltacht Affairs[97], payment of increments was not withheld if a rating was not available. The practice was that the Personnel Unit subsequently followed up for a completed annual review form and associated rating. The Department informed me that a formal system was introduced in November 2010, whereby payment of increments was withheld if a PMDS rating was not available for an officer.
- There should be consistency in the definition of the rating period. Until 2011, the Department of the Taoiseach did not operate PMDS on a calendar year. Instead, it operated the system on a different timescale for each individual jobholder. Furthermore, the PMDS reviews were not effectively synchronised with the timescale for payment of increments. As a result, some of the increments paid in May 2010 were based on PMDS assessments carried out in April/May 2009. At the start of 2011, following an internal review, the Department harmonised the operation of PMDS across all Divisions to ensure that, in future, the same review period will apply for all Divisions and staff.

10.34 It was also noted that in the Department of Social Protection, the award of increments, while still subject to the manager's written confirmation of satisfactory performance, was not predicated on prior compliance with PMDS. Accordingly, most of the increments that were awarded to staff are paid in the absence of completed PMDS annual reviews. The Department has stated that it is taking steps to strengthen its PMDS.

10.35 Not all staff are eligible for a pay increment each year e.g. staff at the maximum point of the relevant payscale. Even where an increment is not payable, it is desirable that the performance management process should continue to function in such cases.

10.36 Overall, the focus group convened to discuss PMDS expressed the view that both jobholders and managers found it was time-consuming to comply with the paperwork requirements and the process. A simpler system was advocated[98].

10.37 The focus group opinion was that, in areas of the civil service that are customer-facing, completion of the PMDS process was not regarded as a priority due to pressures for service provision. What was also evident from the group discussion was that compliance was very significantly driven by the requirement for completion of reviews before pay increments could be awarded. It was also apparent to the group that those who were on the maximum point of their scale were not incentivised to complete the PMDS process. Their experience was that, in non-completed cases, most of these could be attributed to those who are no longer receiving increments.

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97 The functions of the Department of Community, Equality and Gaeltacht Affairs transferred to six different departments following the reconfiguration of Government departments in 2011.

98 The Department of Public Expenditure and Reform is moving to extend electronic processing of PMDS forms throughout the civil service.

Conclusion – PMDS and Pay Increment Awards

Completed appraisal forms are part of the substantiating documentation for certain pay awards. Consequently, it is important that they be in place in all cases. Audit sampling found that almost all increments awarded in May 2010 for four departments were based on current appraisals. There are some financial risks that arise out of practices that permit automated payment of pay increments or the basing of awards on appraisals completed more than 12 months previously. Departments should review their procedures to eliminate these risks.

While audit sampling indicates high compliance with reviews in advance of payment of increments, there remains a residual risk that the samples reviewed were not representative since Departments operate independent systems of payment and human resource management. Accounting Officers should consider asking their internal audit functions to review compliance periodically. It is also desirable to adjust the design and timing of surveys in order to get a more representative snapshot of compliance.

Views of the Accounting Officer

10.38 The Accounting Officer acknowledged the residual risk that the results of sampling of compliance with year-end reviews may not be representative as departments operate independent payment and HR systems. He also stated that the award of an increment was, at least in some cases, based on an unrealistic rating and it was likely therefore that increments were being paid even where there was a problem with performance.

Impact on Performance

10.39 An underlying rationale for performance management systems is the belief that worker performance can be positively influenced and that resources and time devoted to the process will yield a payback in enhanced productivity and effectiveness, except in cases where underperformance is persistent to the point that it manifests as ongoing failure to meet specified, realistic objectives and standards.

10.40 To assist in assessing whether PMDS is contributing to performance improvement and staff development two factors are key

- whether jobholders have or can develop the competencies necessary to carry out their work to the required standard
- to what extent under-performance is identified and managed.

Development of Staff Competencies

10.41 The business objective that underpins investing time in identifying and addressing development needs of staff is to ensure that they are equipped with the behaviour, abilities, knowledge and skills required to do their job well, to provide the highest quality of customer service and to realise their potential. Identification of specific development needs of an individual and agreeing ways to address those needs rests in the first place with the jobholders and their line managers.

10.42 In PMDS, each role profile identifies competencies required to carry out the job. Development of those competencies over a period can lead to development of the capability of the organisation as the competencies are practised. This mutual relationship between personal performance and organisational performance is at the core of PMDS.

10.43 A competency framework was developed to guide staff in the identification of the competencies required for an individual job, and of the areas where an individual post holder required development. The framework, which distinguished between job-related knowledge, skills and behavioural competencies, is summarised in Annex A.

10.44 The Department of Finance carried out an online survey of all civil service staff at the end of 2009 and the beginning of 2010, to ascertain their attitudes as to how PMDS was being operated. The overall response rate achieved was 20%. The methodology used and the low level of response may mean that the opinions expressed cannot be regarded as representative of the views of civil servants as a whole. In practice, those with the strongest views (for or against PMDS) are most likely to have responded. Nevertheless, the responses provide useful indicators of areas where there is scope for improvement to be made to the system.

10.45 The survey found that

- 63% of respondents believed that competencies relevant to their jobs had been identified in the PMDS process.
- Around half of the respondents felt that the training options identified for them were linked to the identified competencies.
- A similar percentage reported that the training needs identified for them were acted upon.

10.46 Only 40% of respondents reported that they had discussed with their manager whether they were operating at the required standard of proficiency or whether they fell short of it. At the senior management levels, the percentage dropped to 36%.

10.47 When competency gaps are identified, the challenge is to address them in an effective manner. In general, deficits in knowledge and skills can be addressed more easily than deficiencies in some behavioural competencies, such as conceptual thinking and interpersonal understanding.

10.48 Certain good practice approaches to addressing the development of competencies of individuals are suggested in Figure 47.

Figure 47 Good Practice for Competency Development

In each cycle, focus on two or three development areas, picked with an eye to the critical competencies for the job
Relate the development emphasis to the capacity of the jobholder vis-à-vis the demands of the job on the basis that competence development, and how it is to come about, will vary from individual to individual and situation to situation.
Agree how development will be recognised when it happens.
Encourage personal ownership of development through action research and other self-monitoring and evaluation techniques or methods.
While individual ownership of development must be encouraged, at the same time there needs to be review mechanisms. Consequently, there is a challenge for jobholders and their managers alike to ensure that, once competencies have been identified for development, there is a relevant monitoring framework that will allow progress to be charted in that development.

Source: Consultant – Dr. Gerry McMahon

10.49 In practice, the development of staff through identification of skills and behavioural competencies to be worked upon can only be effectively addressed as part of an interactive ongoing process where formal appraisal is only one, albeit important, element.

10.50 The focus group regarded the aspects of PMDS relating to competency development as very conceptual in character with limited practical application in the context of the civil service. Some reservations were expressed by the group that the selection of behavioural competencies for development was a 'box-ticking' exercise and that there should be more emphasis on the development of skills. The group also said that it was very difficult to identify whether softer skills had been enhanced as a result of specific training as distinct from technical skills which were more easily demonstrated.

10.51 While training courses are provided with the intention of developing a jobholder, in some cases it is difficult to make the direct link between improved performance and courses undertaken. Departments keep records on attendance at training courses, but no work has been undertaken to assess the output in terms of positive impact on an individual, team or organisational performance. It would be worth exploring whether indicators can be developed to measure the return from investment in staff development or training for softer skills such as communication.

Managing Underperformance

10.52 The utility of the PMDS as a driver of performance is influenced by the extent to which it effectively addresses underperformance. The Department of Finance's 2009 survey found that only 18% of respondents felt that their departments were managing underperformance appropriately.

10.53 A rating of '1' or '2' could be classed as signifying underperformance of the staff member receiving the rating. While the proposed distribution for PMDS assessment ratings indicates that as many as 30% of staff could be rated a '1' or '2', the results over the period 2007 to 2009 show that less than 3% of staff have been rated at these levels. This outturn may indicate that underperformance is not being identified and consequently not being addressed.

10.54 The audit found that some departments have taken steps to address underperformance. Measures noted in the course of this audit review include

- The Department of Social Protection has issued formal guidelines and an information pack to support managers. This is available on its intranet. The guidelines provide clarity about the process which managers can, and should, employ when managing underperformance, and dissemination makes the process transparent to those potentially affected by it. In a pilot exercise the Department of Social Protection also incorporated punctuality, timekeeping and attendance into the PMDS process. In deciding annual performance ratings, the Department seeks to take account of these measures of performance, but with limited success. The Department stated that while there were some positive indicators in the pilot study from the inclusion of these elements in the assessment of performance there had not yet been agreement on their formal adoption.
- In the Department of Enterprise, Trade and Employment, an information and training programme for staff is currently being finalised. A pilot training course was provided to managers who had experience of managing underperformance and the feedback provided at the end of the course was used to inform and further develop the guidelines and training. Additional feedback was obtained through a consultation process with managers and staff of the Department. Training for managers will include preparation for meeting with staff when dealing with difficult issues.
- In the Department of Health and Children, an office notice was issued to all managers highlighting the need to address underperformance in a consistent manner across all divisions. Managers were advised that a rating should accurately reflect performance, that if there are issues with performance that these should be well flagged during the year, and that managers should give explanations to staff in areas where they fall short of expected performance.

10.55 Managing underperformance is a shared responsibility. It is the line manager's responsibility to proactively address underperformance problems arising within their area. On the other hand, it is the responsibility of the jobholder to engage with the manager and to work towards an agreed solution where underperformance has been identified and documented.

10.56 The focus group were quite definite that the issue of under-performance is a serious issue for the civil service. The group were generally agreed that under-performance was not being addressed and set out a number of key observations related to this matter.

- There is a legacy problem to deal with in that some under-performing employees have been carried by other employees and their under-performance continues.
- Under-performance had not and is not being addressed at an early enough stage in an individual's career and this is having a negative knock-on effect throughout their working life.
- Top civil service management is not supporting managers in dealing with under-performance and so there is little incentive for these managers to address the problem.
- When managers receive an under-performing employee into their work area there is often no written evidence to prove the under-performance because this has not been recorded by previous managers – this can prove to be a barrier to raising the issue effectively when the employee has been transferred.
- Managers see a significant personal and administrative 'burden' attached to addressing under-performance.

10.57 An important element in addressing underperformance is to distinguish those individuals who can be assisted in achieving greater proficiency over time from those where there are potential disciplinary issues. In the case of the former, timely actions and agreement on issues between the parties are core elements for the management of underperformance. It may often be possible to achieve a successful resolution to underperformance issues through a personal development plan, tailored to the particular work situation. A desirable general framework for successful management would exhibit these elements.

Figure 48 Good Practice Approach to Managing Underperformance

Early identification and prompt response to observed underperformance
Agreement between jobholder and manager as to the problem
Agreement of the actions to be taken to remedy the situation
Application of appropriate resources to enable the agreed actions to materialise
Manager and jobholder monitoring of subsequent performance impacts

Source: Consultant – Dr. Gerry McMahon

Upward Feedback

10.58 Arrangements for the provision of upward feedback to managers were introduced in 2002. Upward feedback is designed to provide an opportunity for jobholders to constructively comment on how they are being managed, the running of the work unit and how PMDS is implemented.

10.59 Upward feedback was reviewed in four departments. It was found that

- In the Courts Service, no formal upward feedback provision is in operation but the Service stated that it appeared to take place informally. Training was provided to staff for upward feedback but implementation stalled due to industrial action and it was never followed up. It also stated that in 2011 a new management programme had been introduced which encouraged managers to seek feedback from staff on a number of areas including how they were managed, team performance, staff initiatives and dealing with performance issues. Formal introduction of upward feedback was under review.

- In the remaining three departments reviewed, the annual review form includes space to record whether upward feedback was provided. In practice, the Department of Health and Children does not record instances or content of feedback. It is the policy in both the Department of Enterprise, Trade and Innovation and the Department of Social Protection to record instances of upward feedback. In the Department of Social Protection, there are no recorded instances of upward feedback having been given. On the other hand the Department of Enterprise, Trade and Innovation report that 64% of staff have given upward feedback, which ranges from 52% at Clerical Officer and equivalent grades up to 79% at Principal Officer and equivalent grades.

10.60 Generally, the focus group believed jobholders were reluctant to give upward feedback to their managers due to personal inhibitions. The more junior the grade of the jobholder, the less likely were they to give upward feedback.

Conclusion – PMDS and Performance

Surveys by the Department of Finance raise questions about whether the competencies being identified in the course of the PMDS process related to the job and the effectiveness of development follow up where competencies were identified. It would be useful to evaluate the impact of development initiatives on team performance.

Only 19% of respondents to the survey felt that their department was managing performance appropriately.

The distribution of ratings indicates that a very low percentage of staff are rated in the two lower bands. This suggests a risk that underperformance is not being tackled.

Views of the Accounting Officer

10.61 In commenting on the report, the Accounting Officer of the Department of Public Expenditure and Reform noted that the most important measurement of effectiveness of a performance management system was how well the system was contributing to performance improvement and staff development.

10.62 He stated that the Mercer Evaluation of PMDS in 2005 assessed the extent to which PMDS was contributing to improved individual performance and therefore organisational performance. The survey covered specific criteria including the PMDS process, implementation, effectiveness, fairness and consistency, whether training and development needs are met and how performance is assessed. The Department repeated this survey in 2010. He stated that the responses in the survey had given the Department a good indicator of how well PMDS was working and that the findings had informed the development work currently being undertaken to improve PMDS.

10.63 The Accounting Officer also informed me that the Public Service Agreement 2010 – 2014 and associated Civil Service Action Plans set out the measures to be taken by the Department of Public Expenditure and Reform to address the main difficulties with PMDS. These include

- increasing the focus on tackling underperformance through providing training and guidelines on how to address underperformance to HR and training units in all departments /offices
- introduce measures to strengthen links between PMDS and the disciplinary process
- pro-active monitoring of and promotion of better technical structures for the completion of PMDS throughout the civil service.

10.64 Measures addressing the objectives has been approved by the Minister and a letter setting out proposals for PMDS has been issued to Secretaries General in June 2011. Negotiations with unions on strengthening PMDS have commenced.

10.65 The Accounting Officer stated that changes to PMDS will happen on a phased basis.

- The first stage includes streamlining the civil service PMDS to make it a more useful tool for managing performance, introducing a sanction for non-compliance of managers with PMDS and developing a more proactive role for the Department of Public Expenditure and Reform in supporting HR units in promoting and strengthening performance management.
- The second phase will see the development of a framework for fairness and consistency in relation to ratings and development of guidelines and tools for HR units and managers to continue supporting a performance management culture.

10.66 Certain measures to tackle underperformance have already been rolled out. Focus group sessions were held in November 2010 to identify how to address underperformance. Workshops were held in March 2011 with HR units to train staff on tools for managing underperformance, and guidelines were published in May 2011 on ways in which to tackle underperformance, including the use of the (civil service) Disciplinary Code in this process. It is intended that departments will roll out training on how to manage underperformance to line managers.

10.67 Finally, steps were taken to improve compliance and consistency by gathering data on compliance with a view to publishing the rates of compliance by departments and offices across the Civil Service. A year-on-year increase in compliance of 13% recorded in 2010 shows that there has been some success in this area.

Conclusion

The distribution of personal ratings set out for the civil service in 2005 was designed to reflect an expected ‘norm’. This has not turned out to be the case. More higher ratings and fewer lower ratings are being awarded by managers than expected in the 2005 norms.

Appropriate and effective competency development is critical to organisational success. PMDS has now been in operation in the civil service for over ten years and its implementation entails a significant resource commitment. It may be timely to conduct a rigorous review of how well this aspect of staff development has worked and how the process may be improved for organisations and staff alike. More thought also needs to be given to the development of the specific competencies that will positively impact on performance.

The relatively low number of ratings awarded at the bottom end of the scale may indicate unaddressed underperformance.

The Department should consider reviewing whether the existing PMDS processes for dealing with underperformance are sufficient and if they distinguish adequately those cases that may be dealt with through a personal development plan from those requiring some disciplinary actions. Consideration might be given to the provision of a more structured personal development process whereby managers and jobholders affected by underperformance can seek to avoid the path to disciplinary procedures.

In the absence of an agreed approach to the management of underperformance, there is a risk that it would become embedded in an organisation’s culture.

Annex A The PMDS Competency Framework

The competency framework developed for use in the context of PMDS distinguishes between

- **Knowledge** – the knowledge or information required by a post holder in order to do the job. This includes information about a case or situation being dealt with, as well as specialised knowledge such as relevant legislation or required educational or professional qualifications.
- **Skills** – the things a post holder needs to be able to do in the specific job e.g. use of a computer system, how to perform a specific form of analysis, ability to drive or to speak Irish. Skills can often be developed through formal training, through guidance from a coach or through practice on the job.
- **Behaviour** – ways the post holder acts in the work context that influence the effectiveness of his/her performance. Seventeen behavioural competencies were identified as being of relevance generally in the civil service environment. These were grouped into four general behaviour areas, as set out below.

Personal Effectiveness	Group and Interpersonal Effectiveness
Self confidence	Networking and influencing
Achievement drive and commitment	Interpersonal understanding
Initiative	Customer service
Teamworking	Managing and developing people
Communications	Leadership
Managing for Results	**Thinking and Problem Solving**
Managing budgets and resources	Analytical thinking
Information seeking and management	Conceptual thinking
Concern for clarity and work quality	Decision making and judgement
	Specialised expertise

Chapter 11

Revenue Outturn 2010

Office of the Revenue Commissioners

Revenue Outturn 2010

11.1 The net proceeds of taxes and duties collected on behalf of the Exchequer for the year was €31.75 billion (€33.11 billion in 2009).

11.2 The forecast for taxes and duties receivable by the Exchequer was €31.05 billion. Overall, tax revenues in 2010 exceeded the levels forecast by €703 million. The performance against forecast on individual taxheads is set out in Figure 49.

Figure 49 Revenue Paid to Exchequer compared to Forecast 2010

Taxhead	Forecast	Payments to Exchequer	Excess/(Shortfall)	
	€m	€m	€m	%
Income Tax	11,530	11,276	(254)	(2.2%)
Value Added Tax	10,090	10,101	11	0.1%
Excise	4,514	4,678	164	3.6%
Corporation Tax	3,160	3,924	764	24.2%
Stamp Duties	975	960	(15)	(1.5%)
Custom Duties	200	228	28	14.0%
Capital Acquisitions Tax	240	238	(2)	(0.8%)
Capital Gains Tax	340	347	7	2.1%
Total	**31,049**	**31,752**	**703**	**2.3%**

Source: Department of Finance Cumulative Profile of Expected Exchequer Tax Revenue Receipts in 2010 and Account of the Receipt of Revenue of the State collected by the Revenue Commissioners in the year ended 31 December 2010

Audit of Revenue Account

11.3 Under the Comptroller and Auditor General (Amendment) Act 1993 I am required to examine the account of revenue received and paid over to the Exchequer by the Revenue Commissioners (the Revenue Account) in order to satisfy myself as to its completeness and accuracy and to report to Dáil Éireann on the results of my examination.

11.4 I form an opinion on the completeness and accuracy of the Revenue Account on the basis of the examination and testing carried out by my Office on the various receipting, repayment and accounting systems within Revenue. I also take assurance from the systems work which is carried out on a cyclical basis on Revenue’s collection mechanisms.

Audit Conclusion

The Revenue Account together with my opinion thereon is set out in Annex A to this chapter. I have given a clear report on that account.

Revenue Collection Systems

11.5 In addition to examining the Revenue Account, I carry out further 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.

11.6 On a cyclical basis, I examine Revenue's systems for the assessment and collection of tax. I report, by exception, on those general matters arising out of my systems examinations that I consider merit examination by the Committee of Public Accounts of Dáil Éireann.

Chapter Focus

The rest of this chapter examines

- the outturn on Revenue collection in 2010
- the trends in tax receipt compared with national output
- the trend in repayments by Revenue in recent years
- the trend in payment methods adopted by taxpayers.

Revenue Collection and Repayment

11.7 The gross amount collected by Revenue declined from €50.7 billion in 2009 to €47.6 billion in 2010. When amounts collected on behalf of other departments and agencies are excluded, €38.2 billion of the 2010 gross collection was attributable to the core revenue of the State (€41.3 billion in 2009). The total gross collection, the amounts attributable to other agencies and repayments for the years 2007 to 2010 are summarised in Figure 50.

Figure 50 Collection and Repayment of Revenue 2007-2010

	2007 €m	2008 €m	2009 €m	2010 €m
Gross collection	66,148	60,061	50,744	47,559
Less receipts attributable to other Departments and Agencies				
PRSI[a]	(9,480)	(9,779)	(9,291)	(9,196)
Tobacco Levy[b]	(168)	(168)	(168)	(168)
Environmental Levy	(22)	(26)	(24)	(19)
Other	(7)	(5)	(3)	(5)
Gross taxes and duties collected	56,471	50,083	41,258	38,171
Less repayments of taxes and duties	(9,137)	(9,178)	(8,148)	(6,420)
Net Taxes and Duties Collected[c]	**47,334**	**40,905**	**33,110**	**31,751**

Source: Account of the Receipt of Revenue of the State collected by the Revenue Commissioners in the year ended 31 December 2010

Notes:

a PRSI comprises a social insurance contribution and the health levy. Residual amounts of the now abolished Employment and Training Levy are also included here. Net PRSI receipts were €9,110 million (€9,209 million in 2009) after taking account of repayment of €86 million (€82 million in 2009).

b Section 3 of the Appropriation Act 1999 (as amended) provides that each year an amount determined by the Minister for Finance shall be paid to the Health Service Executive from the proceeds of Tobacco Excise. The Minister for Finance has determined that the amount payable should be the maximum amount permissible under the Act – €167. 6 million.

c Net taxes and levies include some €43 million collected in 2010 as part of the various special investigations being carried out by Revenue (see Chapter 16).

11.8 The gross collection, repayments and net collection for each taxhead are set out in Figure 51 together with the percentage change in net receipts in 2010.

Figure 51 Net Receipts by Taxhead

Taxhead	2010 Gross Receipts €m	2010 Repayments €m	2010 Net Receipts €m	2009 Net Receipts €m	Percentage Change 2010[a]
Income Tax[b]	13,945	(2,680)	11,265	11,839	(5%)
Value Added Tax	12,744	(2,642)	10,102	10,638	(5%)
Excise	4,721	(54)	4,667	4,734	(1%)
Corporation Tax	4,920	(976)	3,944	3,890	1%
Stamp Duties	985	(23)	962	1,001	(4%)
Custom Duties	230	(1)	229	208	10%
Capital Acquisitions Tax	243	(6)	237	256	(7%)
Capital Gains Tax	383	(38)	345	544	(37%)
Total	**38,171**	**(6,420)**	**31,751**	**33,110**	**(4%)**

Source: Account of the Receipt of Revenue of the State collected by the Revenue Commissioners in the year ended 31 December 2010

Notes: a Reductions are in brackets.

b PAYE accounts for €9.25 billion of net Income Tax receipts – €7.8 billion tax and €1.45 billion in respect of the Income Levy. The comparative figures for 2009 were €8.5 billion tax and €1.0 billion in respect of the Income Levy.

11.9 Overall, net tax receipts fell by 4% between 2009 and 2010. In the case of Income Tax and VAT which together account for 67% of the net receipts the fall was 5% in both cases.

11.10 Features of Income Tax administration in 2010 included the following

- Income Tax receipts in 2010 include an estimated €1.45 billion in respect of an Income Levy introduced the previous year[99].
- Included in Income Tax repayments is €308 million in respect of an Age Related Health Insurance Tax credit introduced in 2009[100]. The overall impact of the repayment is offset by a related levy on health insurance companies, the proceeds of which are included in Stamp Duties[101] (€318 million). The credit and related levy are temporary measures for the three years to 2011 and are intended to be revenue neutral over that period.

99 Section 2, Finance Act 2009.

100 Section 22, Health Insurance (Miscellaneous Provisions) Act 2009.

101 Section 26, Health Insurance (Miscellaneous Provisions) Act 2009.

11.11 Features of VAT administration included

- the standard rate of VAT decreased from 21.5 % to 21% with effect from 1 January 2010
- with effect from I January 2010, a Margin Scheme for second-hand goods[102] was extended to include the supply by taxable dealers of second-hand means of transport and second-hand agricultural machinery.

11.12 In the case of Corporation Tax, a three-year exemption from Corporation Tax on profits and capital gains for new companies (with a tax liability of less than €40,000 per year) which applied to new start-up companies in 2009 was extended to new start-up companies in 2010.

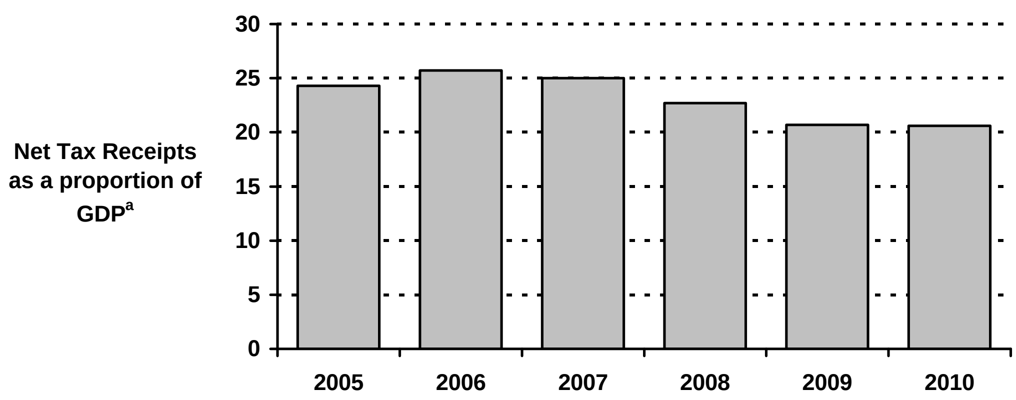
11.13 The main features of Excise Duty administration were the imposition of additional carbon charges in respect of Mineral Oil Tax for petrol and diesel from December 2009, the extension of carbon taxation to other mineral oils from 1 May 2010 and a car scrappage scheme[103].

Tax and National Output

11.14 Taking Gross Domestic Product (GDP)[104] as a measure of the output of the economy, the State took a smaller proportion of national output in 2010 than in previous years. The relationship between net tax receipts and GDP for the period 2005 to 2010 is set out in Figure 52.

11.15 Net tax receipts as a proportion of GDP has fallen from a high of 26% in 2006, to a level of 21% in 2009 and 2010. In 2008, while GDP decreased by 5%, net tax receipts dropped by 13.6%.

Figure 52 Net Tax Receipts as a Proportion of GDP, 2005-2010



Source: Central Statistics Office Quarterly National Accounts, Quarter 4 2010

Note: a Gross Domestic Product is measured at current prices.

[102] The Margin Scheme was introduced as a means of reducing the likelihood of double taxation in the context of the sale of second-hand goods. It allows dealers in certain second-hand goods, works of art, antiques and collectors' items to pay VAT on the difference between the sale price and the purchase price of goods. If the dealer chooses not to operate the scheme, normal VAT rules apply.

[103] Introduced in January 2010, this scheme provided for VRT relief of up to €1,500 on registration of a new passenger car with CO_2 emissions of not more than 140g/km when another passenger car, more than 10 years old, is scrapped.

[104] Gross Domestic Product represents the total value added (output) in the production of goods and services in the country.

11.16 I sought the views of the Accounting Officer on the factors that led to the Revenue Commissioners collecting 5% less of domestic output, by way of taxes and duties, in 2009 and 2010, when compared with 2006 yields. The Accounting Officer stated that during the period of economic growth between 2001 and 2007, the composition of GDP in Ireland changed as property and construction related activities grew as a result of the 'property bubble'. Those activities contributed to the investment component of GDP and grew faster than other components that make up GDP[105].

11.17 Investment, which accounted for 21% of GDP in 2002, grew to 27% of GDP by 2006, and fell back to 11% of GDP in 2010. The Accounting Officer noted that even if GDP had not increased between 2002 and 2010, this compositional change would have altered the Tax/GDP ratio, as the construction and property sectors[106] yield relatively high levels of tax receipts compared to other sectors.

11.18 Tax receipts had increased by 56% between 2002 and 2006 while GDP only increased by 36% and the Tax/GDP ratio went from 22% to 26% over the same period. Since the downturn in 2007, construction and property related activities have decreased at a much more rapid rate than the overall economy as these sectors suffer the worst of the recession. This is illustrated by the decline in Stamp Duty and Capital Gains Tax receipts, from 15% of total receipts in 2006 to 4% in 2010.

Refunds and Repayments

11.19 Entitlement to refunds and repayments is statutorily underpinned[107]. Since 2003, repayments are subject to a valid claim being made to Revenue within four years from the end of the period to which the claim relates. This four-year limit replaced previous limits, the longest of which was ten years.

11.20 €6.4 billion of the gross collection was repaid to taxpayers in 2010 (€8.1 billion in 2009). These repayments represented 17% of gross taxes and duties collected (20% in 2009). The repayment under each tax heading over the past five years is set out in Figure 53.

Figure 53 Repayments by Revenue 2006 - 2010

Payments	2006	2007	2008	2009	2010
	€m	€m	€m	€m	€m
Income Tax	3,075	3,206	3,398	3,229	2,680
VAT	4,358	4,729	4,560	3,325	2,642
Corporation Tax	586	936	975	1,445	976
Capital Gains Tax	35	64	70	62	38
Stamp Duties	42	65	49	23	23
Custom Duties	6	7	15	4	1
Capital Acquisitions Tax	12	6	8	12	6
Excise	138	124	103	48	54
Total	**8,252**	**9,137**	**9,178**	**8,148**	**6,420**
% of Gross Yield	**15%**	**16%**	**18%**	**20%**	**17%**

Source: Account of the Receipt of Revenue of the State collected by the Revenue Commissioners in the year ended 31 December 2010

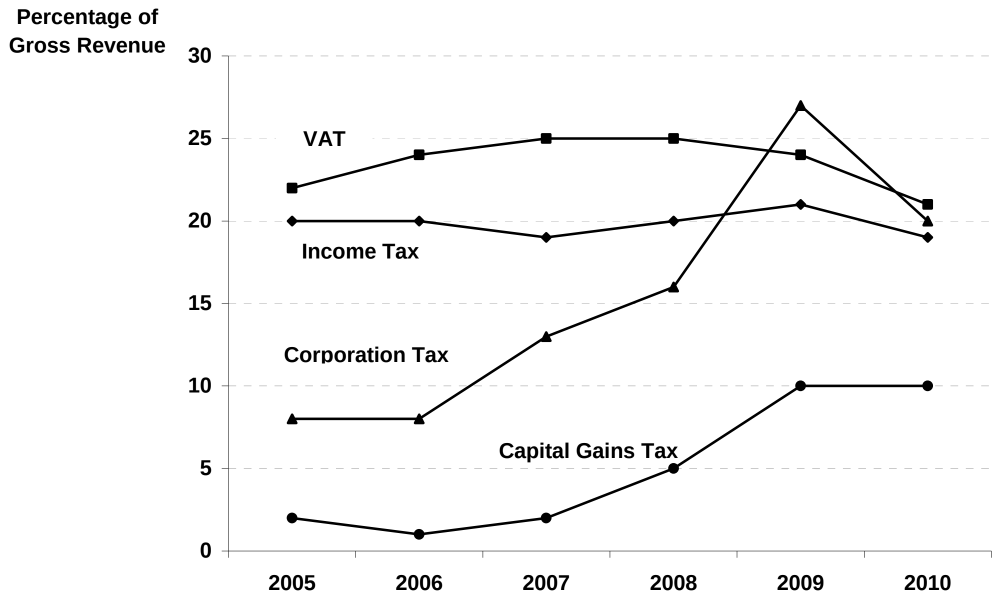
105 Using the expenditure approach to calculate GDP, the economy is divided into four sectors, consumption (expenditure of the household sector), investment (expenditure of the business sector), government purchases (expenditure of the public sector) and net exports (the difference between exports and imports).

106 Accounted for in the investment component of GDP.

107 Section 865, Taxes Consolidation Act 1997.

11.21 Figure 54 displays the relationship of tax repayments to gross receipts over the period 2005 to 2010 in respect of the taxes that accounted for the greatest repayment levels in recent years.

Figure 54 Tax Repayments as a Proportion of Gross Revenue Receipts 2005 – 2010



11.22 Repayments to customers in 2010 in the case of Income Tax, Corporation Tax and VAT represented approximately one-fifth of the gross take under those taxheads. Repayments as a proportion of gross tax yield fell in all three taxes.

11.23 In the case of Corporation Tax, particular factors related to the basis of payment of preliminary tax in the current downturn are at play. These give rise to repayments when company tax computations are finalised. Based on a sample of cases administered by two of the sectoral business units in Revenue's Large Cases Division, the causes of repayments are set out in Figure 55. The result suggests that overpayment of preliminary tax (based mainly on prior year outcomes) gave rise to nearly two-thirds of the amount repaid.

Figure 55 Cause of Corporation Tax Repayments, 2010

Reason for Repayment	%
Overpayment of Preliminary Tax	64
Repayment of Professional Services Witholding Tax	13
Setback of Losses	14
Revision of Corporation Tax Computation	4
Other[a]	5
Gross Yield %	**100**

Source: Office of the Revenue Commissioners

Note: a Other includes overpayments under €50,000 which were not analysed.

11.24 In relation to VAT repayments, the Accounting Officer noted that the decrease is likely to be related to a number of factors, the more important of which were

- absolute and relative decline of the construction industry
- the VAT reverse charge on construction services introduced in 2008, which had the effect of increasing the number of VAT repayment claims but reducing their value

- the level of stock being carried by traders in recession is likely to be down and this could have an impact on input credits, which could in turn reduce VAT repayments.

Methods of Payment

11.25 In the year 2010, a variety of payment methods were used by taxpayers to pay taxes and duties to the Collector General. The means of payment and the trend towards electronic payment methods is depicted in Figure 56.

Figure 56 Payment Methods Collector General's Office 2007-2010

Payment Mechanism	Proportion of Gross Receipts[a]		
	2008	**2009**	**2010**
Revenue On Line Service	44.9%	60.7%	70.2%
Cheques	32.3%	21.3%	14.6%
Direct Debits/Giro and SDA[b]	22.3%	17.5%	14.8%
Sheriff	0.4%	0.4%	0.3%
Solicitor	0.1%	0.1%	0.1%
Total	**100%**	**100%**	**100%**

Source: Office of the Revenue Commissioners

Notes: a This analysis accounts for approximately €39.4 billion of tax receipts collected by the Collector General's Office, and excludes taxes and duties paid to Divisions other than the Collector General's Office.

b The single debit authority (SDA) is a facility whereby the taxpayer provides details of his/her bank account on the payslip portion of the relevant tax form. This is valid for a single debit and only for the amount specified.

11.26 This shows that taxpayers are increasingly using online mechanisms to pay taxes and duties. In 2010, over two thirds of receipts, in value terms, were processed through the Revenue On-Line Service (ROS). There was a corresponding decrease in the amounts paid by way of cheques and direct debits or giros.

11.27 The data set out in Figure 56 shows the payment mechanisms used by taxpayers where payments are made with the Collector General's Office (compromising 83% of gross receipts). The remaining receipts primarily relate to Excise Duties, Customs Duties, Capital Acquisitions Tax, Stamp Duties and also include payments relating to certain taxes made through local offices.

11.28 I sought the Accounting Officer's assessment of the relative timeliness and security of the payment process through ROS and the effectiveness and availability of the system. The Accounting Officer stated that

- ROS allows for the payment and return of all major and minor taxes[108], over a two/three day cycle.
- Payment information is exchanged with the banks using encryption technologies.
- Revenue has invested heavily in the security of the payment process. It is subject to ongoing review and upgrades and communication with Revenue using ROS is fully secure and confidential.
- In the context of a self-assessment system, all customers are subject to the same obligations for any vouching documentation.

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108 The Accounting Officer noted that taxpayer or agent responsibility for record maintenance remained unchanged.

Conclusion

Revenue continued to drop in 2010 but at a lesser rate. Net taxes and duties of €31.8 billion were collected in the year. The two principal taxes, Income Tax and VAT, which account for two thirds of the collection both fell by 5%.

Revenue as a proportion of national output (as measured by GDP) now stands at 21% by comparison with a 26% level in 2006. The reduction has been attributed to the decrease in construction and property related activities. Because these activities yield relatively higher levels of tax than those in other sectors a reduction in output impacts disproportionately on tax yields. Chapter 12 looks at sectoral performance in more detail.

The level of repayments, which peaked at 20% of the gross yield in 2009 has fallen back to pre-2009 levels, standing at 17% for 2010.

Revenue has made considerable strides in moving to electronic payment methods for the bulk of the collection.

Annex A Account of the Receipt of Revenue of the State collected by the Revenue Commissioners in the year ended 31 December 2010

Statement by Accounting Officer on Internal Financial Controls

Responsibility for System of Internal Financial Control

As Accounting Officer I acknowledge my responsibility for ensuring that an effective system of internal financial control is maintained and operated by the Office. This responsibility is exercised in the context of the resources available to me and my other obligations as Head of Office. Also, any system of internal financial control can provide only reasonable and not absolute assurance that assets are safeguarded, transactions authorised and properly recorded, and that material errors or irregularities are either prevented or would be detected in a timely manner. Maintaining the system of internal financial controls is a continuous process and the system and its effectiveness are kept under ongoing review.

The position in regard to the financial control environment, the framework of administrative procedures, management reporting and internal audit is as follows:

Financial Control Environment

I confirm that a control environment containing the following elements is in place:

- financial responsibilities have been assigned at management level with corresponding accountability
- reporting arrangements have been established at all levels where responsibility for financial management has been assigned
- formal procedures have been established for reporting significant control failures and ensuring appropriate corrective action
- there is an Audit Committee to advise me in discharging my responsibilities for the internal financial control system.

Administrative Controls and Management Reporting

I confirm that a framework of administrative procedures and regular management reporting is in place including segregation of duties and a system of delegation and accountability and, in particular, that

- there are regular reviews by senior management of periodic and annual financial reports which indicate financial performance against forecasts
- a risk management system operates within the Office
- there are systems aimed at ensuring the security of the ICT systems.

Internal Audit

I confirm that the Office has an internal audit function with appropriately trained personnel, which operates in accordance with a written charter which I have approved. Its work is informed by analysis of the financial risks to which the Office is exposed and its annual internal audit plans, approved by me, are based on this analysis. These plans aim to cover the key controls on a rolling basis over a reasonable period. The internal audit function is reviewed periodically by me and the Audit Committee. I have put procedures in place to ensure that the reports of the internal audit function are followed up.

Josephine Feehily

Accounting Officer

Office of the Revenue Commissioners

31 March 2011

Account of the Receipt of Revenue of the State collected by the Revenue Commissioners in the year ended 31 December 2010

Report of the Comptroller and Auditor General

I have examined the financial statements relating to the receipt and disposal of Revenue of the State during the year 2010 collected by the Revenue Commissioners set out on pages 152 to 158 under Section 3(7) of the Comptroller and Auditor General (Amendment) Act 1993.

The financial statements, which have been prepared under the accounting policies therein, comprise the Accounting Policies, the Account of the Receipt of Revenue of the State collected by the Revenue Commissioners and the related notes.

Respective Responsibilities of the Revenue Commissioners and the Comptroller and Auditor General

The Revenue Commissioners are responsible for preparing the financial statements and for ensuring the regularity of transactions.

My responsibility is to examine the financial statements in accordance with the relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

I report my opinion as to whether the financial statements are properly presented in accordance with the Accounting Policies. I also report whether in my opinion proper books of account have been kept. In addition, I state whether the financial statements are in agreement with the books of account.

I report any material instance where the transactions do not conform to the authorities governing them.

I also report if I have not obtained all the information and explanations necessary for the purposes of my examination.

Basis of Opinion

In the exercise of my function as Comptroller and Auditor General, I conducted my examination of the financial statements in accordance with International Standards on Auditing (UK and Ireland) issued by the Audit Practices Board and by reference to the special considerations that attached to State bodies in relation to their management and operation. My examination was conducted on a test basis that reviewed evidence relevant to the amounts and disclosures and regularity of the financial transactions included in the financial statements. It also included an assessment of the significant estimates and judgements made in the preparation of the financial statements, and of whether the accounting policies were appropriate, consistently applied and adequately disclosed.

I planned my examination so as to obtain all the information and explanations that I considered necessary in order to provide me with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming my opinion I also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In my opinion, the financial statements properly present the receipt and disposal of the revenue collected for the year ended 31 December 2010 and the residual balances at that date.

In my opinion, proper books of account have been kept by the Revenue Commissioners. The financial statements are in agreement with them.

John Buckley

Comptroller and Auditor General

7 September 2011

Account of the Receipt of Revenue of the State collected by the Revenue Commissioners in the year ended 31 December 2010

Accounting Policies

1. This Account presents the collection and allocation of taxes and duties by the Revenue Commissioners, and the transfer of the proceeds to the Exchequer. The Account has been prepared pursuant to Section 3(9) of the Comptroller and Auditor General (Amendment) Act 1993.

2. Except for the costs of outsourced services for the collection of Vehicle Registration Tax, no charge is included in this Account for the administration or operational costs of the Office of the Revenue Commissioners. Funds for this purpose are voted by the Oireachtas and accounted for in the annual Appropriation Account for Vote 9 - Office of the Revenue Commissioners.

3. Amounts received in respect of penalties and interest imposed by the Revenue Commissioners are brought to account with the related tax and duty settlements. Court fines and penalties are brought to account as Appropriations-in-Aid of Vote 9.

4. The Account also presents the receipts collected by the Revenue Commissioners for other government departments and agencies as follows:

- Department of Social Protection (PRSI Contributions).
- Health Service Executive (Health Levy and Tobacco Levy).
- Department of Environment, Community and Local Government (Environmental Levy on Plastic Bags).
- Department of Enterprise, Trade and Innovation (Employment and Training Levy).
- Commissioners of Irish Lights (Light Dues).
- Department of Transport (Marine Fees).
- Fee Stamps in respect of Registry of Deeds, Arbitration Fees and Fee Stamps in respect of Companies Registration Fees (paid to the Department of Finance as Miscellaneous Revenue).

5. A charge is levied by the Revenue Commissioners for the collection of PRSI Contributions, the Environmental Levy on Plastic Bags and Light Dues. Amounts received in respect of those charges are not included in this Account but are accounted for as Appropriations-in-Aid of Vote 9.

6. The Account has been prepared on a cash basis in accordance with the principles of Government Accounting. Except where described at paragraph 7, the Account shows the actual amounts received and paid in the year. Where further amounts of taxes, duties, etc. are received in subsequent years or where amounts received in the current or earlier years are repaid, such items are recorded in the year of receipt or repayment.

7. Certain customs and excise duties and VAT on imports are accounted for on an accruals basis in that they are recorded as receipts in the year to which they relate even though they are not received until after the year-end. The corresponding asset is included in accrued income in the Statement of Balances.

8. The gross receipts and repayment figures for each taxhead include offsets i.e. cases where the repayment is not directly paid to the taxpayer but offset against other outstanding taxes.

Account of the Receipt of Revenue of the State collected by the Revenue Commissioners in the year ended 31 December 2010

Account of the Receipt and Disposal of Revenue collected

	Notes	2010	2009
		€000	**€000**
Gross Receipts			
Taxes and Duties collected	1	38,338,924	41,425,690
Receipts collected on behalf of Other Departments/Agencies	2	9,220,222	9,318,329
Total Gross Receipts of Revenue Collected		**47,559,146**	**50,744,019**
Repayments			
Repayment of Taxes and Duties	3	(6,420,498)	(8,148,354)
Repayment of Receipts collected on behalf of Other Departments/Agencies	6	(86,190)	(82,027)
Total Repayments		**(6,506,688)**	**(8,230,381)**
Net Receipts			
Taxes and Duties collected	4	31,918,426	33,277,336
Receipts collected on behalf of Other Departments/Agencies	6	9,134,032	9,236,302
Total Net Receipts of Revenue Collected		**41,052,458**	**42,513,638**
Disposal of Net Receipts			
Taxes and Duties Transferred to the Exchequer	5	(31,752,074)	(33,041,960)
Transfer of Tobacco Levy to Health Service Executive	5	(167,605)	(167,605)
Transfer of Receipts to Other Departments/Agencies	6	(9,141,581)	(9,236,044)
Total Disposal of Receipts of Revenue Collected		**(41,061,260)**	**(42,445,609)**
Net Receipts retained at Year End		(8,802)	68,029
Opening Balance on the Account of Receipt and Disposal of Revenue at 1 January		(120,258)	(188,287)
Closing Balance on the Account of Receipt and Disposal of Revenue at 31 December		**(129,060)**	**(120,258)**

Any apparent discrepancies in totals are due to rounding of constituent figures

William Funnell ***31 March 2011***

Accountant General

Office of the Revenue Commissioners

Josephine Feehily ***31 March 2011***

Accounting Officer

Office of the Revenue Commissioners

Account of the Receipt of Revenue of the State collected by the Revenue Commissioners in the year ended 31 December 2010

Statement of Balances

	Notes	2010	2009
		€000	**€000**
Assets			
Cash at Bank and in Hand	7	56,255	161,182
Accrued Income	8	16	15,230
Advances for Revenue Purposes	9	56	63
Amounts due from Government Departments	10	609	898
Total Assets		**56,936**	**177,373**
Liabilities			
Amounts Awaiting Receipting and Allocation	11	(42,132)	(159,897)
Deposits Held	12	(143,864)	(137,734)
Total Liabilities		**(185,996)**	**(297,631)**
Net Liabilities		**(129,060)**	**(120,258)**
Represented by:			
Closing Balance on the Account of Receipt and Disposal of Revenue			
Balance of Taxes and Duties owing from the Exchequer	5	(132,899)	(131,646)
Balance of Receipts collected and due to other Departments/Agencies	6	3,839	11,388
		(129,060)	**(120,258)**

Any apparent discrepancies in totals are due to rounding of constituent figures

The Accounting Policies and Notes 1 to 12 form part of this Account

William Funnell ***31 March 2011***

Accountant General

Office of the Revenue Commissioners

Josephine Feehily ***31 March 2011***

Accounting Officer

Office of the Revenue Commissioners

Account of the Receipt of Revenue of the State collected by the Revenue Commissioners in the year ended 31 December 2010

Notes to the Account

Note 1. Gross Taxes and Duties collected	**2010**	**2009**
	€000	**€000**
Income Tax	13,945,794	15,068,374
Value Added Tax	12,743,817	13,962,910
Corporation Tax	4,919,889	5,335,053
Excise Duty	4,888,819 [a]	4,949,536
Stamp Duties	984,791	1,023,426
Capital Gains Tax	383,240	606,420
Capital Acquisitions Tax	242,675	267,996
Customs Duty	229,899	211,975
	38,338,924	**41,425,690**

a This is stated net of a deduction of €322,432 relating to the net collection costs of outsourced services for Vehicle Registration Tax for the period September to December 2010.

Note 2. Gross Receipts collected on behalf of Other Departments/Agencies

	2010	**2009**
	€000	**€000**
Department of Social Protection	9,008,403	9,168,364
Health Service Executive	187,793	121,011
Department of Environment, Community and Local Government	19,218	24,165
Commissioner of Irish Lights	4,284	3,426
Department of Enterprise, Trade and Innovation	523	1,280
Department of Finance (Miscellaneous Revenue)	1	82
Department of Transport (Marine Fees)	-	1
	9,220,222	**9,318,329**

Account of the Receipt of Revenue of the State collected by the Revenue Commissioners in the year ended 31 December 2010

Notes to the Account

Note 3. Repayment of Taxes and Duties

	2010	2009
	€000	€000
Income Tax	(2,680,217) [b]	(3,229,019)
Value Added Tax	(2,641,300)	(3,325,047)
Corporation Tax	(976,302)	(1,445,602)
Excise Duty	(54,211)	(48,192)
Stamp Duties	(23,206)	(22,558)
Capital Gains Tax	(38,118)	(61,754)
Capital Acquisitions Tax	(6,170)	(12,378)
Customs Duty	(974)	(3,804)
	(6,420,498)	**(8,148,354)**

b Includes an amount of €10,784,022 relating to Tax Relief at Source repayments awaiting final disbursement in early January 2011. The corresponding bank balance has not been included in the Statement of Balances.

Note 4. Net Receipts of Taxes and Duties

	Gross Receipts	Repayments	Net Receipts	Net Receipts
	2010	2010	2010	2009
	€000	€000	€000	€000
Income Tax	13,945,794	(2,680,217)	11,265,577	11,839,355
Value Added Tax	12,743,817	(2,641,300)	10,102,517	10,637,863
Corporation Tax	4,919,889	(976,302)	3,943,587	3,889,451
Excise Duty	4,888,819	(54,211)	4,834,608	4,901,343
Stamp Duties	984,791	(23,206)	961,585	1,000,869
Capital Gains Tax	383,240	(38,118)	345,122	544,666
Capital Acquisitions Tax	242,675	(6,170)	236,505	255,618
Customs Duty	229,899	(974)	228,925	208,171
	38,338,924	**(6,420,498)**	**31,918,426**	**33,277,336**

Account of the Receipt of Revenue of the State collected by the Revenue Commissioners in the year ended 31 December 2010

Note 5. Taxes and Duties Transferred to the Exchequer

	Balance at 1 January 2010	Net Receipts	Total Transfers	Balance at 31 December 2010
	€000	€000	€000	€000
Income Tax	(2,537)	11,265,577	(11,276,092)	(13,052)
Value Added Tax	745	10,102,517	(10,101,284)	1,978
Corporation Tax	(3,966)	3,943,587	(3,923,637)	15,984
Excise Duty	(138,039)	4,834,608	(4,845,574) [c]	(149,005)
Stamp Duties	7,187	961,585	(960,091)	8,681
Capital Gains Tax	2,173	345,122	(346,711)	584
Capital Acquisitions Tax	1,836	236,505	(237,769)	572
Customs Duty	955	228,925	(228,521)	1,359
	(131,646)	**31,918,426**	**(31,919,679)**	**(132,899)**

c The amount of €4,845,574,000 includes €167,605,000 which was paid from the proceeds of Tobacco Excise Receipts to the Health Service Executive under Section 3 of the Appropriation Act 1999, as amended by the Appropriation Act 2005.

Note 6. Transfer of Receipts to Other Departments/Agencies

	Balance at 1 January 2010	Net Receipts	Total Transfers	Balance at 31 December 2010
	€000	€000	€000	€000
Department of Social Protection	7,515	8,922,219 [d]	(8,927,814)	1,920
Health Service Executive	2,471	187,793	(188,657)	1,607
Department of Environment, Community and Local Government	1,220	19,212 [e]	(20,270)	162
Commissioner of Irish Lights	77	4,284	(4,275)	86
Department of Enterprise, Trade and Innovation	84	523	(544)	63
Department of Finance (Miscellaneous Revenue)	20	1 [f]	(20)	1
Department of Transport (Marine Fees)	1	-	(1)	-
	11,388	**9,134,032**	**(9,141,581)**	**3,839**

d The amount shown of €8,922,218,341 is net of repayments of €86,184,406

e The amount shown of €19,212,325 is net of repayments of €5,668

f The amount shown of €1,070 is net of repayments of €220

Account of the Receipt of Revenue of the State collected by the Revenue Commissioners in the year ended 31 December 2010

Notes to the Account

Note 7. Cash at Bank and in Hand

	2010	2009
	€000	€000
Balance in Revenue Accounts at Central Bank	17,177	20,837
Cash in Hand	39,078	140,345
	56,255	**161,182**

Cash at Bank and in Hand represents amounts held in Revenue bank accounts pending completion of processing through Revenue's accounting systems.

Note 8. Accrued Income

Accrued Income represents amounts due to Revenue which are proper to 2010 for which payment was received after the year end.

Note 9. Advances for Revenue Purposes

Advances for Revenue purposes arise due to the operation of a local accounting procedure in Districts for Customs and Excise Duties whereby a shortfall in the collection of monies arising from items such as an unpaid cheque is temporarily met through the mechanism of an 'advance' drawn on a Revenue account. These 'advances' are subsequently cleared when payment is received from the trader.

Note 10. Amounts due from Government Departments

Where a liability arises as a result of the importation of goods by Government Departments, the goods are released without immediate payment of duties or taxes and the Department is subsequently charged for the amount due.

Note 11. Amounts Awaiting Receipting and Allocation

	2010	2009
	€000	€000
Unallocated Tax Deposits	(17,177)[g]	(20,837)
Tax receipts awaiting transfer and allocation	(41,368)	(141,368)
Miscellaneous	16,413[h]	2,308
	(42,132)	**(159,897)**

g Unallocated Tax Deposits (UTD) comprise mainly of payments made on account during tax audits and audit settlements for which accounting instructions have not been completed. Consequently, the payments cannot be allocated to the appropriate taxheads and are held by Revenue in a UTD account in the Central Bank.

h Includes an amount of €16,477,018 which represents the net impact of residual balances following the cessation of the former Stamping system. Detailed analysis is ongoing to confirm the position and adjustments will be incorporated into future accounts.

Account of the Receipt of Revenue of the State collected by the Revenue Commissioners in the year ended 31 December 2010

Notes to the Account

Note 12. Deposits Held

	2010	2009
	€000	**€000**
Stamps	- [i]	(1,311)
C&E Collectors	(5,611)	(7,845)
Automated Entry Processing system (AEP) Deposits	(138,253)	(128,578)
	(143,864)	**(137,734)**

Deposits held represent amounts paid by taxpayers for transactions not yet processed through Revenue's accounting systems.

i Stamps Deposits no longer arise since the introduction of an electronic Stamping system at end 2009.

Chapter 12

Collection by Sector

Collection by Sector

12.1 Information in relation to the amounts of taxes and duties collected between 2007 and 2010 is set out in Chapter 11. This shows that over the period the net amount collected dropped by almost one third. This chapter examines the tax take by sector and tax type over the period 2007 to 2010.

12.2 A breakdown by sector[109] is available for domestic VAT, PAYE, PRSI in respect of employees[110], self-assessed Income Tax, Corporation Tax and Capital Gains Tax. Over the period, 2007 to 2010, these accounted for between 77% and 79% of net tax collected.

12.3 The Income Levy paid by PAYE employees and the self employed, which was introduced from 1 January 2009 has been excluded from the sectoral analysis to provide for comparison on a like for like basis of tax collection over the period. All further analysis in this chapter is based on the sectoral analysis available, excluding the Income Levy. The element of tax collection amenable to analysis on a sectoral basis for the period 2007 to 2010 is set out in Figure 57.

Figure 57 Tax Receipts, 2007 – 2010[a]

Taxhead	2007 €m	2008 €m	2009 €m	2010 €m
Net tax receipts	47,334	40,905	33,110	31,752
Add PRSI receipts[b]	9,406	9,708	9,209	9,111
Total tax and PRSI receipts	**56,740**	**50,613**	**42,319**	**40,863**
Less Income Levy	–	–	(1,138)	(1,446)
Total	**56,740**	**50,613**	**41,181**	**39,417**
Sectoral analysis available	**43,879**	**39,586**	**32,448**	**30,774**

Source: Office of the Revenue Commissioners

Notes: a The payments received by Revenue in respect of PAYE and self-assessed Income Tax on which this analysis is based include amounts in respect of the Income Levy which cannot be separately identified for each sector. Therefore, the levy has been deducted from the amounts allocated to each sector for these taxheads in the same proportion as total receipts for the taxheads.

b PRSI comprises a social insurance contribution and the health levy. Residual amounts of the now abolished employment and training levy are also included here.

12.4 Net tax and PRSI receipts (excluding the Income Levy) for this element of revenue fell by €13.1 billion over the period – just under 30%. The extent to which the drop impacted on each taxhead is set out in Figure 58.

109 The sectoral analysis is an estimate of the yield by sector based on information in relation to the payments by each taxpayer contained in Revenue's Integrated Taxation Processing system.

110 A breakdown by sector is not available for PRSI paid by self-employed persons.

Figure 58 Tax Receipts by Tax Type, 2007 – 2010

Taxhead	2007	2008	2009	2010	Change 2007-2010
	€m	€m	€m	€m	€m
Domestic VAT	12,978	12,065	9,628	9,030	(3,948)
Capital Gains Tax	3,097	1,424	544	345	(2,752)
Corporation Tax	6,393	5,071	3,890	3,944	(2,449)
PAYE	10,155	10,069	8,488	7,777	(2,378)
Self Assessed Income Tax	2,309	1,657	987	957	(1,352)
PRSI	8,947	9,300	8,911	8,721	(226)
Total	**43,879**	**39,586**	**32,448**	**30,774**	**(13,105)**

Source: Office of the Revenue Commissioners

12.5 The greatest decrease in absolute terms was in domestic VAT where receipts between 2007 and 2010 fell by just under €4 billion.

12.6 The greatest relative decrease was in Capital Gains Tax which fell by €2.75 billion between 2007 and 2010 and where the collection in 2010 stood at just 11% of the levels collected in 2007.

Tax Receipts by Sector

12.7 The classification of tax to sectors is based on NACE codes that are used in the European Union to classify economic activities for statistical purposes. The NACE code assigned to each registered taxpayer is based on the primary economic activity undertaken by that registration.

12.8 Over two thirds of the drop in net tax receipts was accounted for by four sectors

- construction sector – a decrease of €2.8 billion
- wholesale and retail trade – a decrease of €2.7 billion
- real estate, renting and business activities – a decrease of €2.1 billion
- manufacturing – a decrease of €1.4 billion.

12.9 The change in tax receipts by sector is set out in Figure 59.

Figure 59 Change in Tax Receipts by Sector, 2007-2010

	2007 €m	Change 2007–2010 €m	2010 €m	Percentage Change
Construction	3,619	(2,809)	810	(78%)
Wholesale and retail trade	8,871	(2,749)	6,122	(31%)
Real estate, renting and business activities	7,741	(2,142)	5,599	(28%)
Manufacturing	5,823	(1,406)	4,417	(24%)
Not classified[a]	1,436	(1,222)	214	(85%)
Financial intermediation	4,515	(1,095)	3,420	(24%)
Agriculture, hunting and forestry	817	(643)	174	(79%)
Transport, storage and communication	2,198	(435)	1,763	(20%)
Hotels and restaurants	1,500	(393)	1,107	(26%)
Other[b]	4,728	(297)	4,431	(6%)
Public administration and defence	2,631	86	2,717	3%
Overall movement	**43,879**	**(13,105)**	**30,774**	**(30%)**

Source: Office of the Revenue Commissioners

Notes: a This refers to tax collected where a sector has not been assigned.

b This includes the following sectors, mining and quarrying, community social and personal services, fishing, activities of households, extra territorial organisations, electricity, gas and water supply, education, health and social work.

12.10 By comparison with receipts in the preceding year, net tax receipts decreased by 10% in 2008, 18% in 2009 and 5% in 2010. The changes in both absolute and percentage terms is set out in Figure 60.

Figure 60 Tax Proceeds by Sector 2007 - 2010

	Change 2008		Change 2009		Change 2010	
	€m	%	€m	%	€m	%
Construction	(854)	(24%)	(1,637)	(59%)	(318)	(28%)
Wholesale and retail trade	(482)	(5%)	(1,936)	(23%)	(331)	(5%)
Real estate, renting and business activities	(992)	(13%)	(1,246)	(18%)	96	2%
Manufacturing	(241)	(4%)	(919)	(16%)	(246)	(5%)
Not classified[a]	(618)	(43%)	(522)	(64%)	(82)	(28%)
Financial intermediation	(519)	(11%)	(471)	(12%)	(105)	(3%)
Agriculture, hunting and forestry	(533)	(65%)	(206)	(73%)	96	123%
Transport, storage and communications	(26)	(1%)	(218)	(10%)	(191)	(10%)
Hotels and restaurants	(167)	(11%)	(143)	(11%)	(83)	(7%)
Public administration and defence	159	6%	221	8%	(294)	(10%)
Other[b]	(20)	—	(61)	(1%)	(216)	(5%)
Total	**(4,293)**	**(10%)**	**(7,138)**	**(18%)**	**(1,674)**	**(5%)**

Source: Office of the Revenue Commissioners

Notes: a This refers to tax collected where a sector has not been assigned.

b This includes the following sectors, mining and quarrying, community social and personal services, fishing, activities of households, extra territorial organisations, electricity, gas and water supply, education, health and social work.

12.11 While a decline in tax receipts occurred in almost all sectors in each year, the following is evident from a year on year comparison.

- Tax receipts from the construction sector continue to decrease at a faster rate than the rest of the economy. Tax receipts in 2010 stood at just 22% of the levels occurring in 2007.
- Receipts from the wholesale and retail trade continued to fall in 2010, but at a slower rate than in previous years.
- Receipts from two sectors – real estate, renting and business activities as well as agriculture hunting and forestry have started to recover in 2010 with increases in tax receipts being recorded in these sectors in 2010.
- Receipts from the public administration and defence sector began to decrease for the first time in 2010 as a result of factors such as pay cuts.

Sectoral Trends by Tax Type

12.12 The decrease in receipts had different impacts across the different categories of taxes. The main sectors contributing to decreases in receipts from the individual taxes is set out in Figure 61.

Figure 61 Sectors Contributing to Decreases in Receipts, by Tax 2007 – 2010

Tax Decrease 2007 - 2010	Main Sectors contributing to decrease
Domestic VAT – €3.95 billion	Wholesale and retail trade – €1.9 billion
	Construction – €986 million
	Manufacturing – €888 million
Capital Gains Tax – €2.75 billion	Unclassified – €843 million[a]
	Real estate, renting and business activities – €798 million
	Agriculture, hunting and forestry – €450 million
Corporation Tax – €2.5 billion	Financial intermediation – €1.17 billion
	Construction – €342 million
	Wholesale and retail trade – €328 million
PAYE – €2.4 billion	Construction – €570 million
	Real estate, renting and business activities – €446 million
	Public administration – €334 million
	Manufacturing – €254 million
	Wholesale and retail trade – €232 million
Self Assessed Income Tax – €1.35 billion	Real estate, renting and business activities – €497 million
	Construction – €334 million
	Agriculture, hunting and forestry – €129 million
PRSI – €226 million	Construction – €492 million
	offset by increases in PRSI receipts from
	Health and social work – €177 million
	Public administration and defence – €141 million

Source: Office of the Revenue Commissioners

Note: a It is likely that the high level of Capital Gains Tax allocated to the unclassified sector is a result of payment of this tax by those who are not registered for other self assessed taxes and have therefore not been allocated a sector code.

Conclusion

A sectoral analysis is available for around four-fifths of the tax collection (including PRSI). There has been a reduction of €13.1 billion or just under 30% in this element of the collection since the end of 2007.

Over half of that drop was accounted for by decreases in the property and retail sectors with the construction sector showing a decrease of €2.8 billion, wholesale and retail trade – €2.7 billion and real estate, renting and business activities – €2.1 billion.

Tax receipts from almost all of the sectors decreased in each of the years except for the

- real estate, renting and business activities sector[111] and the agriculture, hunting and forestry sector where receipts increased in 2010 after two consecutive years where decreases were recorded
- public administration and defence sector where tax receipts had increased in 2008 and 2009 but fell off significantly in 2010.

[111] Real estate, renting and business activities sector includes 'business activities' which in turn extends to professional services not related to real estate or renting such as accounting and legal services.

Chapter 13

Revenue Debt Collection

Office of the Revenue Commissioners

Revenue Debt Collection

13.1 Within Revenue, primary responsibility for debt management rests with the Collector General's Office. That Office is responsible for the collection of taxes and duties and their allocation to the appropriate taxpayer account. The purpose of its debt management function is to ensure the timely collection of most of the business and personal taxes for which Revenue has responsibility. While a number of tax districts currently have a limited role in debt collection, arrangements are being finalised to centralise debt management in the Collector General's Office.

Chapter Focus

This chapter reviews Revenue's debt collection function and, in particular

- how it is organised and resourced
- the debt collection objectives it set the organisation in 2010 and the extent of their achievement
- an analysis of the debt outstanding at 31 March 2011
- the extent of write-off of debt in the year.

Resources and Objectives

13.2 Revenue's debt management programme as set out in its 2010 Output Statement is carried out by 700 staff, assigned to collection and compliance work. The objectives of the programme for the year were to

- optimise the effective collection of taxes and duties
- minimise compliance slippage in 2010, in particular for large and medium sized cases
- reduce collectible or uncontested debt not otherwise the subject of agreed payment arrangements or enforcement proceedings by 25% in the course of 2010.

Organisation of Tax Collection

13.3 Currently, there are 21 debt management units within the Collector General's Office. The key functions of those debt management units include

- identification of arrears cases
- addressing arrears through normal collection activities or enforcement[112].

[112] Enforcement actions include the application of interest charges, using the sheriff or solicitor to enforce the debt or the use of other enforcement actions, which include attachment, liquidation or bankruptcy.

13.4 Tax collection is managed as follows

- The management of cases generally is split over 20 debt management units. The scope of each unit's activity is determined by reference to case size or the average annual amount of tax paid[113] by individual taxpayers. These are categorised into tiers.
- A Dedicated Pursuit Unit manages cases linked by common directors where the debt exceeds €250,000 (the Commonality Unit) and Phoenix cases (the Phoenix Unit). The operation of this Unit is considered separately in Chapter 15.
- Staff are allocated to the various debt management units on the basis of the value of the tax at risk. Large cases, with the highest value payments have the highest ratio of staff to taxpayers.

13.5 As a result of limitations in its IT systems, Revenue is not in position to extract information in relation to the value of debt and the number of taxpayers managed in each of the tiers. For the purpose of this examination, Revenue has provided estimates of the debt and taxpayer breakdown. This is set out by tier in Figure 62.

Figure 62 Organisation of Debt Collection 2010

Tier	Average annual tax	No. of units	Average staff (WTE) 2010	Cost for 2010[a]	Number of taxpayers managed	Debt at 31 March 2011[b]
	€000			€m		€m
One	In excess of 480	1	16	1	6,396	147
Two	300 – 480	2	21	1	7,681	144
Three	43 – 300	8	130	7	65,076	594
Four	6 – 43	6	83	5	142,155	534
Five	<6	3	34	2	294,972	659
Dedicated Enforcement Unit	Combined debt >250 or Phoenix	2	23	1	n/a[c]	n/a[c]
Special Projects and Compliance Units	Various	11	143	8	n/a[c]	n/a[c]
Total		**33**	**450**	**25**	**516,280**	**2,078**

Source: Office of the Revenue Commissioners

Notes:
a Staff costs are based on average salary for the relevant grade and includes overheads and employer PRSI. An additional €0.5 million in overtime costs, not included above, was incurred in 2010.
b Revenue does not maintain records for each tier. The estimates in this column were provided by the Collector General based on its work distribution model.
c Information in relation to the case numbers and debt amounts for these units is not available and is included within the tier structure data.

13.6 The Accounting Officer stated that the tiered structured approach, which assigns resources in line with risk levels associated with non-compliance on a case size basis, was introduced at the start of 2009 and further consolidated in 2010. She stated that this approach ensures that those cases that pose the highest risks, are targeted in a timely manner.

[113] Case size is a factor of the average annual tax liability based on a weighted mixture of 'fiduciary' taxes (VAT, Employer PAYE/PRSI, Relevant Contracts Tax), Corporation Tax and Personal Income Tax.

Taxes and PRSI Outstanding

13.7 Figure 63 shows the amount of tax outstanding for each category of tax and summarises the charges raised, the payments made and the amounts written off in the twelve-month period ended on 31 March 2011. Total tax outstanding at the end of March 2011 has decreased by €34 million to €2,078 million when compared to the same period in 2010.

Figure 63 Outstanding Taxes and PRSI[a]

Tax or Levy	Balance at 31 March 2010	Net charges raised[b]	Paid	Written off	Balance at 31 March 2011
	€m	€m	€m	€m	€m
VAT	633	9,293	9,203	135	588
PAYE	173	10,529	10,528	35	139
PRSI	254	8,796	8,777	52	221
Income Tax (excl PAYE)	426	2,311	2,239	30	468
DIRT	–	442	442	–	–
Corporation Tax	315	3,527	3,498	13	331
Capital Gains Tax	244	339	310	4	269
Capital Acquisitions Tax	3	256	256	0	3
Abolished Taxes [c]	5	(5)	–	–	–
Relevant Contracts Tax [d]	59	13	(9)	22	59
Total	**2,112**	**35,501**	**35,244**	**291**	**2,078**
Debt as a proportion of net charges raised	**5.4%**				**5.8%**

Source: Office of the Revenue Commissioners

Notes:

a The figures exclude those taxes which are not the subject of deferred collection, including Customs, Excise, Stamp Duties and that element of VAT associated with Customs and Excise. Tax is regarded as outstanding from the date the liability is placed on the taxpayer's record – usually, as a result of the receipt of a return or the raising of an estimate.

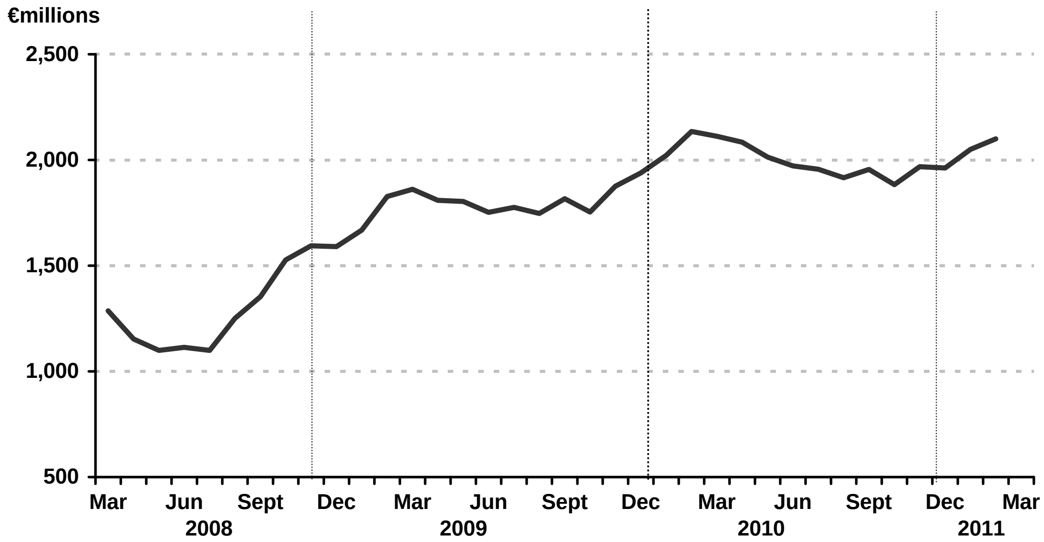
b Net charges raised include estimates in cases of non-filing. The corresponding charges in the year to March 2010 were reported by Revenue at €38.9 billion.

c The opening balance of €5 million for Abolished Taxes was eliminated during 2010 as related debts, following investigation, could not be substantiated.

d Relevant Contracts Tax net charges raised comprises assessments and declarations relating to principal contractors of €272.15 million, less claims of €259.34 million from sub-contractors. The net repayment of €9.44 million comprises €260.82 million received from principal contractors and €270.26 million repaid to sub-contractors (or offset against other tax liabilities).

13.8 Over the three years to March 2011, tax outstanding has increased to 162% of the level at March 2008 as depicted in Figure 64.

Figure 64 Monthly Debt Outstanding



Source: Office of the Revenue Commissioners

Management Approaches

13.9 The debt outstanding may be managed through

- normal collection activities
- payment agreements
- enforcement arrangements.

13.10 The debt outstanding at 31 March 2011 can be categorised into the debt management categories as set out in Figure 65.

Figure 65 Collection Status of Tax and PRSI, March 2011

Tax or Levy	Total debt €m	Under appeal €m	Under enforcement €m	Payment agreement €m	Other debt[a] €m
VAT	588	104	209	56	219
PAYE	139	12	9	9	109
PRSI	221	2	17	19	183
Income Tax (excl PAYE)	467	159	98	21	189
Corporation Tax	331	245	4	12	70
Capital Gains Tax	269	160	47	6	56
Capital Acquisitions Tax	3	–	–	–	3
Relevant Contracts Tax	60	7	18	3	32
Total March 2011	**2,078**	**689**	**402**	**126**	**861**
Comparator March 2010	**2,112**	**669**	**378**	**119**	**946**

Source: Office of the Revenue Commissioners

Note: a This category of debt comprises debt which is not under appeal and is not the subject of enforcement proceeding or payments agreements with the taxpayer.

13.11 €689 million, accounting for about one third of the total debt outstanding is the subject of an appeal by the taxpayer and, while the appeals are being disposed of, Revenue is prevented from seeking to collect it. This is an increase of €20 million over the amount under appeal twelve months previously.

13.12 In relation to the remaining debt which is available for collection – €1,389 million

- 29% of the debt is the subject of enforcement proceedings by Revenue (26% in March 2010).
- Revenue has concluded payment agreements in respect of 9% of the debt outstanding (8% at March 2010).
- Uncontested debt, which was not covered by agreements with the taxpayer or had not progressed to enforcement totalled €861 million, accounting for 62% of the collectible debt (€946 million – 66% of collectible debt in March 2010).

13.13 Revenue had adopted a target to reduce collectible or uncontested debt, not otherwise the subject of agreed payment arrangements or enforcement proceedings, by 25% during 2010. This category of debt stood at €880 million at end 2009 and had fallen to €815 million by end 2010 – a decrease of 7.4%[114]. The Accounting Officer is satisfied with this achievement in light of the extremely challenging economic and financial environment in which businesses have been operating.

13.14 Figure 66 sets out an aged analysis of the balance outstanding at 31 March 2011 in respect of taxes and duties due in relation to periods up to end 2010. It indicates that 20% of the amount outstanding related to the most recent tax period (26% in March 2010). Some 66% of the amount outstanding relates to tax periods prior to 2009 (the comparative percentage in relation to debt at March 2010 was 57%).

[114] The figures in Figure 65 differ due to the fact that Figure 65 gives a later position (March 2011).

Figure 66 Aged Analysis of Pre 2011 Debt at 31 March 2011

Taxhead	Total tax outstanding €m	2010 €m	2009 €m	2006 to 2008 €m	Prior to 2006 €m
VAT	588	198	111	170	109
PAYE	139	57	27	34	21
PRSI	221	109	50	47	15
Income Tax	467	1	84	160	222
Corporation Tax	331	17	17	68	229
Capital Gains Tax	269	1	10	85	173
Capital Acquisitions Tax	3	–	–	–	3
Relevant Contracts Tax	60	26	4	22	8
Total	**2,078**	**409**	**303**	**586**	**780**
Comparator[a]	**2,112**	**550**	**363**	**478**	**721**

Source: Office of the Revenue Commissioners

Note: a These are the corresponding amounts outstanding for periods ending twelve months previously.

Write-Offs of Tax and PRSI

13.15 €300 million of taxes and PRSI was written off during the year ended 31 December 2010, €261 million or 87% of which was in respect of fiduciary taxes[115]. Taxes written off have more than doubled between 2008 and 2010. The main increases in 2010 as compared with 2009 were as follows

- VAT written off increased by €33 million
- Income Tax written off increased by €15 million
- PRSI written off increased by €14 million
- PAYE written off increased by €6 million.

13.16 A breakdown by taxhead, of the total amount written off, is shown in Figure 67.

13.17 €298.2 million of the 2010 write-off was assessed on a case-by-case basis. The remaining €1.4 million, relating to 113,360 cases with balances of less than €1,000, which were considered uneconomic to pursue, was written off on an automated basis.

115 The fiduciary taxes are VAT, PAYE/PRSI and Relevant Contracts Tax and are collected by businesses on behalf of Revenue and held in trust until paid to Revenue.

Figure 67 Taxes Written Off

Taxhead	2008 €000	2009 €000	2010 €000
Fiduciary taxes written off			
Value Added Tax	57,710	101,530	134,539
PAYE	19,831	37,145	43,535
PRSI	25,438	47,610	61,480
Relevant Contracts Tax	12,581	16,617	21,875
	115,560	**202,902**	**261,429**
Direct taxes written off			
Income Tax	5,310	10,305	25,001
Corporation Tax	3,016	3,889	8,259
Capital Gains Tax	985	2,610	3,498
Automatic Write-Offs	4,125	1,842	1,398
	13,436	**18,646**	**38,156**
Total tax written off	**128,996**	**221,548**	**299,585**

Source: Office of the Revenue Commissioners

13.18 In 2010, there was a 17% increase in PAYE write-off and a 29% increase in PRSI write-off. In response to my inquiries in this regard, the Accounting Officer noted that an internal review of debt written off in cases relating to insolvency in 2010 revealed that, while the number of insolvencies remained very much the same in the construction and services sectors, the number of insolvencies in the hospitality sector increased by 26%. Revenue noted that the hospitality sector is associated with lower paid employment and, as the PAYE/PRSI ratio is higher in such employments, this would have contributed to the comparatively higher PRSI write-off in 2010.

13.19 Figure 68 sets out the number of cases and the amount written off by category. Approximately 87% (€259 million) of the amount written off arose in cases where businesses had ceased or encountered difficulties. The balance of €40 million relates to cases where the amount outstanding was not collected due to factors such as an inability to locate the taxpayer, a decision by Revenue that the amount outstanding did not warrant committing resources to collecting it and compassionate grounds.

Figure 68 Reasons for Write-Off

Reason	2009		2010	
	Number of cases	Amount written off €000	Number of cases	Amount written off €000
Business cessation/difficulty				
Liquidation/receivership/bankruptcy	1,260	131,876	1,739	165,979
Ceased trading – no assets	1,000	47,533	2,032	77,205
Uncollectible due to financial circumstances of taxpayer	233	7,148	305	8,369
Examinership	28	7,497	32	6,974
Deceased and estate insolvent	49	746	74	869
Other reasons				
Cannot be traced/outside jurisdiction	209	6,409	563	10,916
Uneconomic to pursue[a]	76,067	18,961	120,953	27,544
Compassionate grounds	76	1,197	135	1,575
Unfounded liability	20	181	17	154
Total	**78,942**	**221,548**	**125,850**	**299,585**

Source: Office of the Revenue Commissioners

Note: a Includes 113,360 cases written off automatically (74,111 in 2009).

13.20 The largest single amount written off in 2010 was €3.82 million in respect of PAYE/PRSI (€3.15 million) and VAT (€0.67 million). There were 16 other cases where the amount written off was greater than €1 million.

13.21 The Internal Audit Branch in Revenue undertakes an annual examination of tax write-offs. Its 2010 audit examined a sample of 255 cases, representing 17.3% (€51.5 million) of the total value of non-automated write-offs (€298 million). Internal Audit was satisfied that all write-offs were in accordance with the criteria prescribed. Internal Audit also examined the results of the automatic write-offs in 2010 and verified that the authorised selection criteria were correctly applied.

13.22 Figure 69 outlines the breakdown of amounts written off under each taxhead, for all cases where more than €1 million was written off in 2010. In all but one case, the write-off of tax related to business cessation or insolvency.

Figure 69 Tax Write-Offs in excess of €1 million – 2010

Reason	**No. of cases**	**Fiduciary Taxes**[a]	**Direct Taxes**[b]
Creditors voluntary liquidation	7	8,898,619	1,830,750
Revenue court liquidation	3	6,441,443	585,112
Ceased trading – no assets	2	4,889,002	—
Examinership	2	2,735,187	12,148
Cannot be traced – outside jurisdiction	1	2,793,340	—
Insolvency – adjudicated bankrupt	1	—	2,231,570
Company was wound up	1	1,237,879	—
Total	**17**	**26,995,470**	**4,659,580**

Notes: a PAYE/PRSI, VAT, Relevant Contracts Tax.
b Income Tax, Corporation Tax and Capital Gains Tax.

Conclusion

At the end of March 2011, debts owing to Revenue amounted to €2.1 billion. Outstanding debt now represents just short of 6% of the corresponding charges raised.

In 2010, Revenue aimed to reduce the level of uncontested debt, not subject to enforcement proceedings or payment agreements with the taxpayer, by 25% – the actual reduction achieved was 7%.

The value of taxes written off continues to increase. There was a significant increase in the value of tax written off in 2010 when compared with 2009 and 2008. Write-offs increased by 72% in 2009, when compared with 2008. A further increase of 35% was recorded in 2010.

The largest amount of tax written off in a single case in 2010 was €3.8 million. In sixteen other cases, debts in excess of €1 million were written off. In all but one case, the write-offs were related to business cessation or insolvency.

Chapter 14

Taxpayer Compliance

Office of the Revenue Commissioners

Taxpayer Compliance

14.1 All taxes and duties collectible by Revenue are self-assessed with the exception of PAYE and PRSI (which is initially assessed by employers) and Vehicle Registration Taxes on second-hand vehicles which is assessed by the National Car Testing Service[116].

14.2 In a tax administration that is based on self-assessment there are certain risks that tax may not be fully collected. These include the risk that

- all potential taxpayers will not be identified
- missing returns from identified taxpayers will not be pursued
- incomplete or inaccurate returns will not be identified.

14.3 It is important for Revenue to be in a position to track compliance trends in these areas and position itself to address any emerging issues. The risks outlined are likely to impact on the Revenue collection based on the following

- the Irish shadow economy is estimated to be of the order of 13% of Gross Domestic Product (GDP)
- audits show a consistent rate of non-compliance in a random sample of the taxpayers
- the results of special investigations show a historic pattern of evasion
- the Department of Social Protection undertakes a programme of employer inspections to ensure the correct operation of PRSI. This programme identified a non-compliance rate of 15% in 2010 (20% in 2009). There is likely to be some cross-over between PAYE and PRSI compliance.

Chapter Focus

This chapter reviews

- what the result of random audit is suggesting about general taxpayer compliance
- whether Revenue is in a position to review the timeliness of payment compliance
- the emerging risks to compliance and how Revenue is responding to them
- the trend in identified major non-compliance in the recent past.

116 On 1 September 2010, the National Car Testing Service took over a range of registration functions on behalf of Revenue in accordance with provisions included in the Finance Act 2010.

Random Audit

14.4 Revenue has operated a Random Audit Programme since 1993. Around 400 random audits are selected for completion annually. The extent of completion of the Random Audit Programmes for 2007 to 2010 as at 31 March 2011 is shown in Figure 70.

Figure 70 Random Audit Programmes, 2007 - 2010

	2007	2008	2009	2010
Number of Cases				
Sample selected	401	403	400	400
Completed cases	397	395	361	293
Dropped cases	2	1	–	–
Incorrect period audited	1	–	–	–
Other[a]	–	2	–	–
Cases on hand at March 2011	1	5	39	107

Source: Office of the Revenue Commissioners

Note: a Cases already assigned to Anti-Avoidance and Investigation and Prosecutions Divisions. They are not audited under the Random Audit Programme.

14.5 The results of the random audits conducted in the period 2007 to 2010 are set out in Figure 71.

Figure 71 Results of Random Audit, 2007 - 2010

	2007	2008	2009	2010[a]
Base year yield	**€**	**€**	**€**	**€**
Tax	571,765	836,381	631,302	279,646
Interest and penalties	236,728	334,840	237,089	77,569
	808,493	***1,171,221***	***868,391***	***357,215***
Yield for other years	**€**	**€**	**€**	**€**
Tax	735,799	1,096,343	791,772	165,993
Interest and penalties	452,542	351,848	294,592	61,123
	1,188,341	***1,448,191***	***1,086,364***	***227,116***
Total yield	**1,996,834**	**2,619,412**	**1,954,755**	**584,331**
Audits completed	397	395	361	293
Average yield for base year	2,037	2,965	2,406	1,219
Average yield for all years	5,030	6,631	5,415	1,994
Yielding cases as % of completed cases	**33%**	**30%**	**34%**	**33%**

Source: Office of the Revenue Commissioners

Note: a The programme for 2010 has not yet been completed. The experience in previous years is that the yield increases as the later cases are finalised.

14.6 Overall, the results indicate that

- the number of yielding cases is around 32%
- the average yield from the audit is between €5,000 and €6,600
- when non-yielding cases are excluded, the average yield from the 2007 to 2009 programmes varied between €15,200 and €22,200.

14.7 During the audit, the original declared liability was compared with the audit yield for all audits completed under the 2009 Random Audit Programme. The results are set out in Figure 72.

Figure 72 Compliance Rates based on 2009 Random Audit Programme

	Yielding cases	Non-yielding cases[a]	Total
Number of cases completed	121	240	361
Total original declared liability[b]	€9,674,938	€26,024,592	€35,699,530
Additional tax in base year as a result of audit	€631,302	-	€631,302
Additional tax in other years as a result of audit	€578,682	€213,090	€791,772
Proportion of undeclared tax in 2007	6.5%	-	1.8%
All undeclared tax as a proportion of declared liability in 2007[c]	12.5%	0.8%	4.0%

Notes: a This column refers to cases with no base year yield. Some had yields in other years.

b Original liability was calculated by subtracting the audit yield, interest and penalties from the final declared liability on Revenue's Integrated Taxation Processing System.

c The 2007 liability has been used as a measure of the amount of tax due in a representative year.

14.8 The value of tax undeclared was 1.8% for a single year and, overall, random audits identified additional undeclared tax equivalent to 4% of the base year liability.

Compliance by Taxhead

14.9 During a review by my Office, compliance was examined on the basis of individual taxheads in respect of audits completed under the 2009 Random Audit Programme. The results are set out in Figure 73.

Figure 73 Compliance by Taxhead based on Results of 2009 Random Audit Programme

		Income Tax	VAT	Employers PAYE/PRSI	Corporation Tax	Other[a]	Total
		€000	**€000**	**€000**	**€000**	**€000**	**€000**
Original declared liability		1,174	10,209	17,156	7,081	–	35,620
Base year yield		162	351	71	29	18	631
Additional year yield		96	455	122	2	117	792
Total audit yield		**258**	**806**	**193**	**31**	**135**	**1,423**
Base year tax underdeclared	%	13.8	3.4	0.4	0.4	–	1.8
Total tax underdeclared[b]	**%**	**22.0**	**7.9**	**1.1**	**0.4**	**–**	**4.0**

Notes: a The 'Other' category includes Capital Gains Tax and Relevant Contracts Tax. However, the sample is too small to draw any conclusions in respect of the level of tax underdeclared.

b The 2007 liability has been used as a measure of the amount of tax due in a representative year.

14.10 The results would suggest that the taxes that are significant from an underdeclaration viewpoint are

- VAT because even a small non-compliance rate has implications for yield due to the size of overall liabilities
- Income Tax because of the high percentage of the original liability underdeclared.

14.11 The results reported in Figure 73 are based on a single year. As an aid in focusing Revenue's efforts it would be desirable to combine the results of a number of years so as to isolate those taxheads where the impact of non-compliance is greatest and those where non-compliance is most prevalent.

Compliance by Sector

14.12 During a review by my Office, the results of the 2007 to 2010 Random Audit Programmes were combined and examined on a sectoral basis to establish the extent of variation in compliance between sectors. The results are set out in Figure 74.

Figure 74 Compliance by Sector based on 2007 - 2010 Random Audit Programmes

	Number of audits completed	Proportion of yielding cases	Average yield – all cases	Average yield – yielding cases
		%	€	€
Hotels and Restaurants	46	50	6,372	12,743
Manufacturing	66	35	3,870	11,105
Wholesale and Retail Trade	118	40	3,043	7,639
Real Estate, Renting and Business Activities	341	30	1,443	4,730
Construction	191	38	1,518	3,971
Transport, Storage and Communications	107	42	1,166	2,773
Agriculture, Hunting and Forestry	227	25	622	2,478
All Other Sectors[a]	350	26	1,039	3,953
All Sectors	**1,446**	**32**	**1,604**	**4,998**

Note: a Includes activities of households, all other sectors/unknown, community, social and personal services, education, financial intermediation, fishing, health and social work, public administration and defence, mining and quarrying.

14.13 Overall, the highest rate of non-compliance and the highest levels of yield were in the hotel and restaurant sector.

14.14 It is a requirement of the Random Audit Programme that a comprehensive audit be completed. The review examined a sample of 50 cases to establish

- whether a comprehensive audit[117] had been completed in each case and review the documentation available to evidence the work completed and the basis for the audit conclusion
- how the agreed settlement[118] compared with the auditor's quantification of liability.

14.15 In the majority of cases the documentation on file evidenced the completion of a comprehensive audit. However, in two of the 50 cases examined, while the taxpayer was registered and active for a number of taxheads, the evidence on the audit file suggested the audit was limited to examining only one taxhead.

14.16 There was a significant degree of variation in the quality of the audit files reviewed. Good practice examples included instances where the audit report outlined the type of business, the principals involved, the main sources of income, a summary of the work completed on audit and a clear basis for the audit conclusion reached. In other cases, there was no audit report and a review of the documentation on file did not provide adequate evidence in relation to the audit conclusion reached. In response, Revenue has stated that developments to its case management systems have been made to assist in the implementation of quality standards in relation to case selection, audit preparation and reporting.

14.17 In order to provide a true measure of compliance the yield reported would need to be broadly equivalent to the undeclared liability detected. The agreed settlement was compared with the assessed liability for the sample. In 23[119] cases no additional liability was identified. In relation to the remaining 27 cases where additional liability was assessed that additional liability agreed with the settlement in 24 cases. In the final three cases the assessed liability was greater than the settlement amount as the taxpayer had claimed inability to pay the amounts due. In one of those cases, Revenue raised a liability on the taxpayers file while, in the other two, no record of the liability was entered on the taxpayers record.

14.18 Audit yield is defined as settlement amounts. As a result using audit yield to assess the extent of underdeclaration underestimates the level of non-compliance. Revenue has acknowledged this and its settlement recording is being amended from July 2011.

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117 A comprehensive audit is one which normally covers Income Tax or Corporation Tax and any significant risks associated with other taxes the individual or company is registered for.

118 The settlement represents the amount agreed between the taxpayer and Revenue as being payable.

119 Includes one case where the audit identified an issue, however the impact on the taxpayers liability was not quantified.

Conclusion – Random Audit Programme

The Random Audit Programme has the potential to yield significant information that would inform Revenue's compliance strategy by

- giving an indication of the tax gap and taxpayer compliance rates
- helping to identify the impact and incidence of non-compliance by taxhead
- identifying sectors where greater amounts of tax are at risk.

Revenue does not currently carry out this type of analysis. My review, while based on limited samples, demonstrates, in my opinion, that this type of analysis is both feasible and useful. It would help Revenue to extract valuable information from the programme in order to inform its compliance work and would lead to a greater transparency around the cost of non-compliance which is ultimately borne by compliant taxpaying citizens.

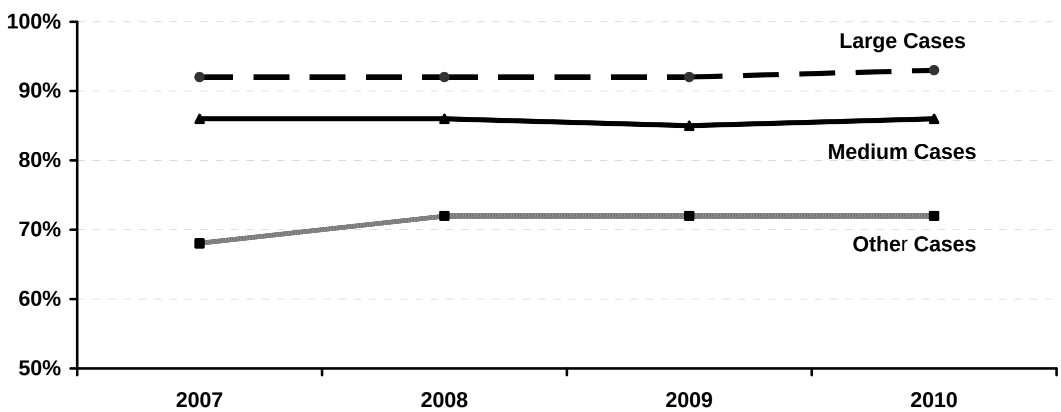
One of the objectives of the Random Audit Programme is to measure and track compliance with tax legislation. The tax underdeclared and the original declared liability should be reported in all cases examined in the course of the Random Audit Programme. This would facilitate provision of an estimate of the audit gap (the tax collectible if all returns were audited) through a comparison of additional liabilities detected by the audit with the original liability.

Timely Compliance

14.19 The measurement of filing and payment compliance are important elements in Revenue's tracking of taxpayer compliance. Revenue currently monitors filing and payment compliance using a composite indicator that measures the proportion of taxpayers that have submitted a return or a payment as a proportion of the total number of returns issued. The measure is calculated by aggregating within bands based on three case sizes (large, medium and other), the compliance rate for each taxhead on a weighted basis. The weighting is based on the annual yield for each taxhead.

14.20 Compliance rates are calculated for the due month and one month after the due date – due month plus 1. Performance using this measure for the period 2007 to 2010 is set out in Figure 75.

Figure 75 Due Month Compliance Rates[a], 2007 - 2010



Source: Office of the Revenue Commissioners

Note: a This is a composite compliance measure which takes account of compliance in relation to PAYE/PRSI, VAT, Corporation Tax, Income Tax and Relevant Contracts Tax (RCT). The definition of case sizes changed in 2008. The comparative figures for due month compliance in 2007 have been restated.

14.21 As the relatively stable compliance rates for large and medium sized cases over the period are at odds with a rising level of tax owed to the Revenue Commissioners, which had increased from €1.1 billion at the end of 2006 to €2.1 billion at March 2011, I asked the Accounting Officer to provide details of the debt at 31 March 2011 by case size and to indicate the number of cases in each category. The Accounting Officer stated that she was not in a position to provide this information.

14.22 Monitoring payment compliance is critical to ensure that Revenue maximises the funds made available to the Exchequer. I asked the Accounting Officer to disaggregate the composite measure in order to measure separately return and payment compliance. Revenue attempted to disaggregate the measure for the main business taxes including VAT, PAYE/PRSI and RCT. As a result of limitations in its current IT systems, the Accounting Officer stated that Revenue was not in a position to present separate payment and filing compliance indicators in relation to PAYE and PRSI[120]. Revenue used a five tier[121]categorisation for the purpose of the analysis.

14.23 In relation to VAT, separate return and payment rates were calculated which measured compliance on the month the return/payment was due and again at one, two and three months after the due date. Overall, payment compliance lags the level of reported overall compliance as indicated in Figure 76.

Figure 76 Payment and Composite Compliance - VAT

	Composite Measure	Payment Measure	Difference
	%	%	%
Due month	60.2	58.0	2.2
Due month plus 1	73.9	71.1	2.8

Source: Office of the Revenue Commissioners

14.24 Payment compliance lagged compliance reported on a composite basis by between 2.2% and 3.3% depending on the timescale and in some tiers by as much as 5.5%. Overall payment compliance reached 80.5% after four months and ranged between 73.3% for Tier 5 up to 98.3% for Tier 1.

14.25 The differential between the composite measure and payment compliance is more marked in Tiers 3 and 4 suggesting a need for more intensive intervention in relation to debt management in those areas. The gap between payment and composite compliances decreases when debts below €100 are excluded but with Tiers 3 and 4 showing the highest deviations[122].

[120] The data analysis tool used does not record the receipt of the monthly PAYE/PRSI Return in instances where the return indicates tax due without an accompanying payment.

[121] Revenue classifies its caseload according to the size of the taxpayers average annual amount of tax paid ranging from Tier 1 for larger cases and Tier 5 for small cases.

[122] RCT also shows a deviation for some tiers of over 3%.

Conclusion – Timely Compliance

Revenue needs to address its capacity to capture and report payment compliance across all major taxheads and report results consistently. The measures it currently reports are based on a count of returns in defined categories. This needs to be supplemented with information on debt by case size. Both the amount of credit and the period of credit taken by taxpayers needs to be kept under review.

A positive feature of performance is the maintenance of high levels of filing compliance in the higher tiers.

14.26 In response, Revenue noted the comments relating to expanding its compliance reporting and stated that a new reporting infrastructure was being developed designed to enhance its capabilities in this area. In particular, it is intended to produce more detailed debt reports containing analyses of the debt both by case size and by age.

Emerging Risks

14.27 Since the onset of the economic and financial crisis that began in 2008 Irish GDP has decreased. In the 36 months to the end of 2010 it decreased by 19%. The State took a smaller share of this reduced level of national output in that net taxes and duties as a percentage of GDP decreased by 4% since end 2007.

14.28 The environment in which Revenue authorities operate is constantly changing. Some of these environmental factors contribute to increased collection risk. These include, increasing complexity and innovation in business structures, new financial products, e-commerce developments and changes in economic conditions[123]. In addition, the risk of non-compliance increases in an economic downturn. In downturns, it is inevitable that a proportion of businesses will have losses or reduced profits. Behaviours that become more pronounced in recessions include non-reporting, under-reporting, illicit claim refunds, tax withholding and resorting to the cash economy. The reduction in liquid assets also increases the likelihood of businesses delaying the payover of fiduciary taxes[124] they are obliged to collect under legislation and of using them as a source of short-term funding.

Revenue Response to Shadow Economy

14.29 The shadow economy comprises all economic activities that would have been taxable were they reported to revenue authorities. It includes both criminal activity and unreported legal activities. Ireland's underground economy which has been provisionally estimated at 13% is broadly in line with the OECD average of 14%[125]. Unreported tax relating to those activities comprises two main elements

- unregistered businesses and activities not captured on Revenue's systems
- registered businesses who do not remit their full share of taxes.

[123] Compliance Risk Management Guide, 2010, European Commission Directorate General Taxation and Customs Union.

[124] The fiduciary taxes are VAT, PAYE/PRSI and Relevant Contracts Tax and are collected by businesses on behalf of Revenue and held in trust until paid to Revenue.

[125] The Influence of the Economic Crisis on the Underground Economy in Germany and other OECD countries in 2010: A (further) increase, Friedrich Schneider, January 2010.

14.30 In response to my inquiries the Accounting Officer stated that, with the downturn in the economy, an increasing focus for Revenue is on the shadow economy. The shadow economy ranges from the under-reporting of sales and profits by businesses within the system to business activity taking place outside the system, often by those who are also on social welfare.

14.31 She stated that each Revenue region and district has a focus on businesses operating outside the system. In 2010, additional business registrations amounted to just over 4,500. Measures taken include projects to identify cases not on record with significant deposit interest and high value vehicles. Projects undertaken are often in co-operation with the Department of Social Protection, the National Employment Rights Authority and the Gardaí. Revenue carried out town/streetscape operations, visits to construction sites where a single house is being built and visits to markets.

14.32 In regard to its monitoring of the environment the Accounting Officer informed me that Economic Outlook reports prepared for its management consider the macro-economic environment on a regular basis as well as examine economic indicators related to the performance of individual taxheads. The analysis that has been carried out to date indicates that reductions in the various taxes are generally consistent with the decline in overall economic performance. The influences on the various taxes are complex and multifaceted and although there is, in general, a broad consistency in the direction in which yields move, there are discrepancies in their comparative movements.

14.33 An approach of specific value in addressing shadow economy issues is the on-going identification of cases which are not on Revenue's PAYE or Income Tax database but have indicators of economic activity identified from third party data. This third party data would include asset purchases and suspicious transactions.

Non-Compliance Patterns – General Features

14.34 From an historic context, Ireland has attempted to address non-compliance which was a major concern until the late 1990s through a combination of tax amnesties and follow-up investigations.

14.35 Tax amnesties in 1988 and 1993 yielded €988 million. A condition of the amnesties was that taxpayers who availed of them would make full and total disclosure of their liabilities. Notwithstanding this, it was found in the course of follow-up investigations that taxpayers continued to shelter income from the Revenue authorities sometimes with the aid of agents.

14.36 The investigations to date have centred around taxable income held as assets by way of

- domestic bank deposits
- foreign bank deposits
- single premium insurance schemes
- discretionary trusts combined with foreign bank deposits.

14.37 The capacity to address evasion that used these methods was limited because, in general, the assets and underlying income were outside Revenue's line of sight due to

- lack of power to compel disclosure by agents of the taxpayers,
- lack of audit powers to confirm agent compliance and
- absence of rights to seek court orders in relevant cases.

14.38 Overall, despite amnesties, over €2.65 billion has been recovered in these subsequent targeted investigations. This compares with the yield from audit and assurance in the same period of €2.9 billion[126]. Features of the drives included, in most cases, the enactment of legislation to strengthen the information flow to Revenue and give it inspection rights.

14.39 The Accounting Officer summarised the general lessons learned from Revenue's special investigations as follows

- Weak Revenue powers will be exploited.
- Access to third party information is essential to effective tax administration. Revenue now receives a very broad range of third party information automatically.
- Powers to apply to the Courts for a class or classes of information is very useful especially when that information covers past years.
- Public awareness that Revenue has powers and access to information, and will use them, is an important deterrent. In the context of the special investigations, once Revenue showed that it would use its new powers to get information and that it would then use the information, the rate of engagement with Revenue under the Voluntary Disclosure phases of subsequent investigations increased.
- It was unlikely that the scale of the investments and use of structures could have been achieved without the active encouragement of professional advisers and, on the offshore aspect of tax evasion, it is clear that most taxpayers do not transfer funds offshore without help. Using legislation to place reporting responsibilities on advisers and intermediaries at the stage where certain structures are being put in place may be a useful deterrent.
- Revenue's capability in terms of skills and capacity to confront are critical, as well as a capacity to handle and analyse large volumes of sometimes complex data safely, efficiently and intelligently. Public awareness of Revenue's activities and results is an important factor.
- Because the special investigations covered a broad span of years, the experience suggests that while the prevalence and level of tax evasion can be influenced by varying positive or negative economic factors, it is reasonable to conclude that there exists a predisposition to tax evasion that is inelastic in respect of these forces.

Non-Compliance Patterns – Audit Results

14.40 At the level of general compliance deliberate underdeclaration continues to be a feature of taxpayer behaviour. Information collected during the random audit programme provides useful insights into the client behaviours which gave rise to the underdeclaration. These can include, intentional underdeclaration by the taxpayer, incorrect technical treatment of a particular issue or lack of knowledge.

14.41 As noted earlier (see Figure 71) around one-third of all taxpayers who are randomly audited are found to owe some additional tax. In the course of audit 27 cases were examined where the Revenue audit had established additional liabilities under the 2009 Random Audit Programme. The audit sought to categorise the behaviour which gave rise to the underdeclaration. The results are set out in Figure 77.

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[126] This includes the yield from all audits conducted (excluding special investigations) in the period 1998 to 2010.

Figure 77 Taxpayer Behaviour and Non-Compliance - 2009 Random Audit Programme

Number of cases	
Deliberate behaviour	9
Careless behaviour with significant tax consequences	12
Careless behaviour without significant tax consequences	6
Total	**27**

14.42 The examination found that one third of cases displayed characteristics associated with deliberate behaviour including

- omissions of casual workers from PREM[127] returns
- claiming significant non eligible personal expenditure in respect of Income Tax
- failing to make returns with respect to Capital Gains Tax liabilities
- not holding a valid Relevant Contracts Tax payments card when making payments to a Subcontractor with a valid C2 certificate
- claiming a Section 23 relief[128] when not eligible
- invoices not issued in respect of income received.

Conclusion - Non-Compliance Patterns

Since economic activity and, therefore, the business environment in which Revenue operates is cyclical there may be lessons from taxpayer behaviours and system failures during previous downturns.

Historically the behaviour on the part of taxpayers and their agents that gave rise to the evasion and avoidance that led to the special investigations suggests

- amnesties did not induce complete and accurate disclosure on the part of all taxpayers
- taxpayers will evade tax in instances where Revenue do not have a clear line of sight in terms of audit rights
- agents may facilitate evasion either through the misclassification of taxpayers status (e.g. classifying residents as non-resident) or through the creation of schemes designed to accommodate taxpayers seeking to conceal untaxed income.

Around one-third of a sample of random audit cases that yielded additional tax were found to have been the result of apparently deliberate non-compliance. Revenue should consider a comprehensive analysis of the cause of identified underdeclaration so as to inform its compliance drives.

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127 PREM is employers PAYE/PRSI.

128 Section 23 Relief is a tax relief that applies to rented residential property in a tax incentive area. It is available to a person who has incurred expenditure on the purchase, construction, conversion or refurbishment of a qualifying property and who lets that property, having complied with certain conditions.

14.43 While most of the methods used to facilitate avoidance or evasion were relatively simple in concept the risk is that, given the experience of amnesty administration and follow up investigations, more complex financial instruments and structures may be created with a view to achieving the same ends.

14.44 The Accounting Officer stated that a close examination is required to understand the true nature of complex structures so that risks can be identified and remedial action proposed. She noted that Revenue has secured High Court orders which are giving it access to information going back ten years in relation to transfers from Irish clearing banks to and from five foreign jurisdictions. Section 896A of the Finance (No. 2) Act 2008 now imposes a reporting obligation on professional advisers and financial institutions regarding settlements involving Irish settlors and non-resident trustees. She added that a further new provision, Section 149 of the Finance Act 2010 requires practitioners to tell Revenue if they promote or use certain transactions that will, or are intended to, provide the user with a tax advantage. Revenue is also getting information from the National Asset Management Agency.

Conclusion

The effectiveness of the Revenue collection process is impacted upon by both the efficiency of its systems and the behaviours of taxpayers within the current economic environment. This chapter focused on some aspects of taxpayer behaviour and the tax collection environment.

Since the onset of the economic and financial crisis that began in 2008 Irish GDP has decreased. In the 36 months to the end of 2010 it decreased by 19%. The State took a smaller share of this reduced level of national output in that net taxes and duties as a percentage of GDP decreased by 4% since end 2007.

While this reduction is ascribed to the impact of a decline in the construction and property sectors there would be merit in attempting to analyse the key elements that contributed to the reduction so as to ensure that any compliance response is focused.

A positive feature of performance is the maintenance of high levels of filing compliance in the higher tax tiers.

A key means of gauging taxpayer compliance is through random sampling. Revenue's Random Audit Programme has the potential to yield significant information that would inform its compliance strategy by

- giving an indication of the tax gap and taxpayer compliance rates
- helping to identify the impact and incidence of non-compliance by taxhead
- identifying sectors where greater amounts of tax are at risk.

Revenue does not currently carry out this type of analysis.

Revenue needs to address its capacity to capture and report payment compliance across all major taxheads and report results consistently. The measures it currently reports are based on a count of returns in defined categories. This needs to be supplemented with information on debt by case size. Both the amount of credit and the period of credit taken by taxpayers needs to be kept under review.

Up to one-third of a sample of random audit cases that yielded additional tax were found to have been the result of apparently deliberate non-compliance. Revenue should consider a comprehensive analysis of the cause of identified underdeclaration so as to inform its compliance drives.

Chapter 15

Managing Related Tax Cases

Office of the Revenue Commissioners

Managing Related Tax Cases

15.1 Effective debt collection involves the coordinated pursuit of the tax liabilities of related entities in order to combat

- the emergence of unsustainable tax liabilities without the prospect of recovery
- tax abuse associated with the Phoenix Syndrome[129]
- any failure to pay over fiduciary taxes[130].

Commonality Checking

15.2 A risk to debt collection arises where businesses are linked through principals who

- have involvement with other existing businesses that have significant tax debts or non-compliance or
- have links to a failed business where the protection of limited liability might have been deliberately used to evade the payment of fiduciary taxes.

15.3 To address this risk, the Revenue Commissioners engage in a process of commonality checking in order to identify entities with common directors or participants and where appropriate

- manage the collective debt as well as pursuing each individual taxpayer
- identify businesses that have relationships with failed businesses[131] in order to identify cases for close monitoring and more active pursuit of debts.

15.4 In order to identify related entities Revenue searches for businesses with common principals using information held on its own systems as well as by the Companies Registration Office[132]. The checks (which Revenue treat as mandatory) are conducted by Revenue's debt management and new tax registration units. Commonality checks are conducted in the case of all new registrations for tax and in instances where the declared (or estimated) tax arrears or tax liability exceeds €50,000, or where a write-off of tax in excess of €50,000 is being proposed.

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129 See Annex A.

130 The fiduciary taxes are VAT, PAYE/PRSI and Relevant Contracts Tax and are collected by businesses on behalf of Revenue and held in trust until paid to Revenue.

131 These include, businesses with the same address as the failed entity or operating in the same locality, operating the same business as the failed entity or within the same field, having a director that is common to both the new business and the failed entity or instances where there is either family or employer links between the directors in the new and failed entity.

132 Information held by the Companies Registration Office allows Revenue to identify other companies with which individuals are or were a director.

Pursuit of Debt in Commonality Cases

15.5 Where relationships with other entities are established and a heightened compliance risk exists, either due to a significant combined debt or the existence of a connection with a previous failed business, further debt management is conducted by a Dedicated Pursuit Unit located in the Collector General's Office. The Dedicated Pursuit Unit has two sub-units

- a Commonality Unit responsible for managing the debt and compliance of cases related through common directors where the total debt exceeds €250,000
- a Phoenix Unit responsible for managing the debt and compliance of cases related to a failed entity.

15.6 The Commonality Unit manages groups of cases with debts in excess of €250,000. The objective is to make a timely debt collection impact through the use of appropriate enforcement measures. Where a business and its related entities remains compliant for a period of two years the group of businesses is removed from management by the Commonality or Phoenix Units. In 2010, there were 24 cases removed from the Commonality Unit and 42 cases removed from the Phoenix Unit.

15.7 The aim of the Phoenix Unit is to combat the emergence of what is called the Phoenix Syndrome – the characteristics of which are set out at Annex A. Key functions of the Phoenix Unit are to establish the circumstances of the prior business failure and where it is established that it is not genuine[133] ensure that the new entity makes its returns and payments on time and manage any tax arrears which may have built up prior to the case being referred.

15.8 Collection enforcement carried out by both the Commonality and Phoenix Units accounted for 3% of Revenue's total collection enforcements in 2010 and

- The Commonality Unit had 3,637 cases on hand at the end of 2010. 2,466 (68%) of those cases were compliant. A case is deemed compliant where the outstanding liability is nil. While cases are managed in the Unit by cluster no information was available on cluster compliance.
- The Phoenix Unit had 675 cases on hand at the end of 2010 and 395 (59%) of those cases were substantially compliant. Substantial compliance, in this instance, is where the liability in the case is less than €5,000.

[133] Revenue guidelines on the "Identification of Phoenix Cases" provide that genuine business failure is not a reason to monitor a case as "phoenix".

Chapter Focus

The effectiveness of the commonality checking process depends on the accurate identification of all relevant cases and their referral as appropriate for enhanced debt management.

The audit set out to examine

- whether commonality checks are carried out in appropriate cases and the results recorded
- in respect of cases checked, the accuracy of those checks in identifying all relevant relationships
- whether appropriate cases are being referred to the Dedicated Pursuit Unit and the relevant debt management unit.

Conduct of Commonality Check

15.9 Where commonality checking detects a common link between the principals in businesses, the details of each relationship should be noted on Revenue's Common Registration System (CRS). The recording is a two stage process

- a marker is placed on the individual case to show that a commonality check has been conducted
- the actual relationships identified are noted in a relationship and/or customer notes section in each individual case.

15.10 A sample of cases meeting the criteria for a commonality check was examined in the course of audit. Cases were selected at random from VAT registrations, arrears greater than €50,000 and cases considered for write-off greater than €50,000 in 2010. The focus of the review was on determining whether the checks had been conducted and whether the results had been accurately recorded on CRS. A sample of 110 cases was examined. There was no evidence that the required commonality checks had been conducted in 18% of cases. The results are set out in Figure 78.

Figure 78 Commonality Checks

	Number	Proportion
Check completed and results recorded on CRS[a]	90	82%
No evidence that a check was conducted	20	18%
Total cases sampled	**110**	**100%**

Note: a The audit treated the check as recorded if a commonality marker was inserted or the computerised case notes recorded evidence of the check. In 75 cases, a commonality marker was present on the case. A further 15 cases were identified where the case notes showed evidence that a commonality check had been conducted. In five of those cases the check was completed six months after the date required.

15.11 A review conducted by Revenue of the Commonality Programme in September 2009 also raised concerns in relation to the absence of commonality checks in some cases. In relation to checks by debt management units, the review concluded that commonality checks were not always conducted where warranted and as a result, cases were not being referred for pursuit at the earliest juncture. The Revenue review found that 47% of the clusters being managed, at that time, in the Commonality Unit had debts in excess of €500,000 by the time the case was referred.

15.12 The same review of the Commonality Programme also noted that Revenue's Central Write-Off Unit reviews the conduct and recording of commonality checks in a sample of write-off cases being submitted to the Chairman for formal sign-off. The review noted that the exercise conducted by the Central Write-Off Unit also identifies cases where there is no record of the commonality check having been performed[134].

15.13 Internal Audit examines all write-off cases and its reviews identify shortcomings in the conduct of commonality checks in cases where tax debts in excess of €50,000 are being written off. Matters identified included cases where

- the commonality check was not completed or recorded in the proper location on Revenue's systems
- the check was conducted even though the debts were less than €50,000 and
- debts in excess of €250,000 were not referred to the Commonality Unit.

15.14 The 2010 review of write-off cases conducted by Internal Audit found that commonality checks were properly recorded in 57% of cases.

Accuracy of Recorded Checks

15.15 Where Revenue had conducted a commonality check, the audit reviewed the results of those checks with a view to establishing whether all of the relationships with other entities were properly identified and recorded in CRS. In order to do this, the commonality check was reperformed by reference to data held by the Companies Registration Office and on Revenue's systems.

15.16 Three cases in the sample were excluded on the basis that the cases are currently monitored by the Large Cases Division[135]. In the remaining 87 cases, the audit concluded that no relationships existed in 45 of the cases while in 42 of the cases examined relationships existed.

15.17 In those cases where relationships were identified during the audit the Revenue commonality check conducted had

- accurately concluded on the relationships in 21 cases
- identified some of the relationships in 8 cases
- identified none of the relationships in 13 cases.

15.18 The audit concluded that Revenue had not identified relevant relationships in 15% of cases with identified commonality features and had done so incompletely in a further 9% of cases.

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[134] There are no records maintained of the extent of this but Revenue staff stated that in up to 50% of write-off cases examined a commonality check had not been completed.

[135] In excess of 100 relationships were identified in each of these cases.

Referral of Cases

15.19 The identification of commonality features may call for referral to special units charged with debt pursuit.

15.20 Where commonality links are established, the extent of the debt of the related cases is examined by reviewing the compliance record[136] on Revenue's Integrated Taxation Processing system.

15.21 In instances where the case that triggered the commonality check is a new registration the process is as follows

- where the case is related to a business that ceased or abandoned trade with significant tax debts i.e. debt greater than €50,000 and meets a number of criteria related to phoenix companies, the case is referred to the Phoenix Unit
- where relationships are found and there are no links to a failed entity the case is allocated to the appropriate debt management unit.

15.22 In cases, other than new registrations

- Where the combined debt is greater than €250,000, the related cases are referred as a group to the Commonality Unit[137].
- Where the combined debt is between €50,000 and €250,000, the case worker responsible for the case with the highest debt becomes a liaison officer for all of the related cases. This officer is responsible for agreeing a strategy for collecting the outstanding debt and monitoring the related cases with the other caseworkers.
- Where the combined debt is less than €50,000, there are no changes to the debt management process i.e. the case continues to be debt managed in the relevant debt management unit as normal.

15.23 In order to function effectively the units charged with follow up would need to have all relevant cases referred to them and a process to ensure that non-relevant cases were excluded or filtered.

15.24 Of the 110 cases examined, 8 were appropriate for referral to the Dedicated Pursuit Unit since they had links to a failed entity (one case) and, in the remainder, had debt above the relevant threshold for referral at April 2011[138]. Figure 79 sets out the extent to which the cases were referred.

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136 In reviewing the compliance record of an entity a caseworker checks for any returns outstanding, unpaid tax or previous tax written off.

137 One exception to this is in cases where the appropriate decision is to liquidate the company. The debt management unit continues with the action and the remaining cases are referred to the Commonality Unit.

138 The combined debts were assessed in each case at April 2011 based on information from Revenue's Integrated Taxation Processing system. Cases were then compared to the list of cases on hand in the enforcement units for the same period to determine whether the case had been referred.

Figure 79 Referral of Commonality Cases to Dedicated Pursuit Unit

Feature	Unit	Suitable for referral to Pursuit Unit[a]	Referred cases	Not referred
Related to failed entity with debt > €50,000	Phoenix Unit	1	1	-
Combined debt of entity > €250,000	Commonality Unit	7[a]	5	2
Total		**8**	**6**	**2**

Note: a Two further cases were identified that exceeded the debt thresholds and on further investigation there was only one entity suitable for referral as the remaining related entities were in liquidation.

15.25 Effective pursuit of cases is dependent upon the extent to which Revenue has identified all of the relevant relationships. While, on one hand, one quarter of appropriate cases were not referred for pursuit, on the other hand, it appears that inappropriate cases were, at the same time, being referred. Both the Commonality Unit and the Phoenix Unit conducted reviews of the suitability of cases referred to them in 2010. Figure 80 sets out the number of clusters referred to both units during 2010 and the proportion deemed suitable.

Figure 80 Groups Referred to Commonality Unit 2010

Unit	Total referrals	Suitable referrals	Not suitable referrals
Commonality Unit	462	279	183
Phoenix Unit	406	209	197
Total	**868**	**488**	**380**

Source: Commonality Unit, Collector General's Office

15.26 Overall, just over half of the cases referred were suitable for further pursuit. The reasons cases were deemed unsuitable in the case of the Phoenix Unit have only been recorded from June 2010 onwards and they show that just under half of the cases were not in fact phoenix cases and over one third of cases were below the debt threshold. In addition, 87% of the unsuitable cases received by the Commonality Unit were also found to be below the debt threshold. This has implications for the effectiveness of the referral process.

15.27 In instances where the case that triggers the commonality check is in liquidation, connected cases should be referred for pursuit since risk features are associated with the combined group debt. Revenue guidelines on commonality checks provide that 'where a case is being managed by a debt management unit and the only appropriate decision in the case is to liquidate the company by issuing a letter under Section 214 of the Companies Act 1963, that unit should continue with the action in the case and refer, where appropriate, all other cases in the cluster to the Commonality Units.'

15.28 Revenue's guidelines specify that referrals must contain at least two businesses or partnerships currently registered for tax. The result is that in cases where one entity in a group continues to trade and the related entities are in liquidation, the case is not referred to the Commonality Unit.

Administrative Matters

15.29 In 2010, Revenue reviewed the effectiveness of the commonality check in identifying the emergence of phoenix companies and it concluded that there is an increase in cases in the Phoenix Unit due to the economic downturn. The review also drew attention to the fact that the commonality check as currently conducted does not identify a phoenix company where the director of the failed entity acts as a shadow director in a newly formed phoenix entity.

15.30 It recommended that the Phoenix Unit should work proactively with Revenue Districts and agencies who share information with Revenue to identify possible phoenix cases where shadow directors are operating.

Management Information

15.31 In regard to the administration of the Commonality Programme the audit noted that the management information systems appeared to be deficient in that

- the Dedicated Pursuit Unit does not currently have a list of phoenix cases on hand – this militates against controlled management of this category of cases
- a fully accurate figure on the debt outstanding in commonality and phoenix cases could not be supplied due to discrepancies in information held on cases by the Unit.

15.32 In response to my inquiries in this regard, the Accounting Officer stated that there are robust management controls and evaluation systems in place within the Phoenix and Commonality Units. Revenue has scheduled an IT development to place a marker on cases to identify them as being managed in the Dedicated Pursuit Unit. The absence of this marker means that the process of producing lists of cases and associated debt is a manual and labour intensive process.

Views of the Accounting Officer

15.33 The Accounting Officer accepted that challenges arise with systems wholly reliant on checks being undertaken manually. She drew attention to an initiative introduced as part of a move to electronic registration for customers. Revenue has introduced an automated commonality check (auto-commonality) in 2011 which is conducted on all new VAT and Relevant Contracts Tax registrations before the registration is approved. Auto commonality will in time apply to all new tax registrations.

15.34 She stated that Revenue has also undertaken a series of training workshops for staff on how and when to complete the commonality check. In 2011, 270 Revenue staff attended these workshops.

15.35 In relation to instances where appropriate cases are not referred, the Accounting Officer stated that while Revenue has taken and will continue to take all reasonable steps to ensure optimal operation of the programme through the full operation of the commonality checks (as evidenced by the training workshops and the introduction of auto-commonality checking), nevertheless she was satisfied that the working of the cases in the debt management units even where commonality issues are not fully identified in accordance with Revenue guidelines is giving effective management of cases with significant compliance and/or debt issues.

15.36 She noted that while there are some deficiencies and ongoing efforts are being applied to overcome them, issues of real substance in terms of tax foregone do not arise from those deficiencies. Where Revenue had not identified all relevant relationships or where no relationships were identified, the follow up review conducted by Revenue of the cases concerned shows that the normal debt management case working had ensured that the tax debts had been fully controlled.

15.37 The Accounting Officer stated that the large number of cases referred to the Commonality Unit below the debt threshold arose due to challenges for registration units in identifying the lead debt management unit. As a result, a practice developed whereby cases between €50,000 and €250,000 were referred to the Commonality Unit which then distributed the cases to the relevant debt management unit. This practice was formalised in 2011.

15.38 The Accounting Officer considers that the build up of debts in excess of €500,000 before referral does not necessarily reflect a failing of the conduct of commonality checks. It can occur where

- connected entities submit several overdue returns without payments to Revenue at the same time
- where a case is already undergoing active enforcement by a debt management unit and is not, therefore, the subject of immediate referral to the Dedicated Pursuit Unit until that enforcement has been concluded.

Conclusion

Revenue's commonality approach is a useful way of addressing debt collection with specific risk features that attach to related entities. However, its effectiveness depends on completeness in the performance of checks, recording related parties identified in the course of that checking and referring appropriate cases for pursuit. The audit found that

- there was no evidence of checks in 18% of cases where they should have been conducted
- where they were conducted, relevant relationships were not identified in 15% of cases and incompletely identified in a further 9% of cases
- some cases appropriate for referral to the Dedicated Pursuit Unit were not referred.

The efficiency and effectiveness of commonality checking and follow up is hampered by deficiencies in case recording and the referral of unsuitable cases to pursuit units.

In cases where relationships are identified with companies in liquidation, the debts of the trading entity are not referred to the Commonality Unit for monitoring. In light of the increased risk of non-collection of debts, in such instances, there may be merit in referral of those cases to the Commonality Unit.

Annex A Characteristics of Phoenix Companies

In 2004, the International Association of Insolvency Regulators[139] published a survey - "The Regulation of Phoenix Companies". The survey was completed by 13 members and set out their experience in dealing with the Phoenix Syndrome. The report outlined the typical characteristics of phoenix companies and specific characteristics with respect to companies in Ireland.

Phoenix Characteristics identified by the Survey

Failed Entity

- Undercapitalised normally having a minimum share capital.
- Insolvent.
- Depletion of assets shortly before cessation.
- Operated to evade some or all of its prior liabilities.

Phoenix Company (General)

- Formed with nominal share capital.
- Operates in the same or related business area.
- Commences operation immediately prior to cessation of the trade of the failed entity or within a short period (no more than 12 months).
- Directors/Managers/Controllers also operated the previous business.
- Employees of the former business proceed to work for the phoenix company.
- The assets of the failed entity are transferred by the directors at a below market value to the phoenix company.
- Preferential payments i.e. commitments relating to the payment of outstanding liabilities are made by directors to a number of the creditors of the insolvent company prior to ceasing trading.
- Substantial liabilities (e.g. tax due to state authorities) are left behind with the insolvent company which has limited assets to meet these liabilities.

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139 The International Association of Insolvency Regulators is an international body that brings together the collective experiences and expertise of government insolvency regulators from jurisdictions around the world.

Phoenix Company (Ireland)

- One or two shareholders.
- Minimum share capital (normally two shares of €1 each with a nominal absolute maximum of 100 shares of €1 each).
- One or two directors.
- Employees are the same as is the premises from which the company trades.
- Business name on occasion is maintained by the controller of the company and may be transferred by way of licence to the new entity.

The report also notes that phoenix activity in Ireland appears in industries which require few assets but considerable input from employees. The primary sectors in which phoenix companies arise were

- construction
- transportation
- licensed premises.

Chapter 16

Revenue Compliance Measures

Office of the Revenue Commissioners

Revenue Compliance Measures

16.1 Revenue attempts to detect non-compliance using risk focused audits and seeks to deter those who do not meet their obligations using prosecutions and publication of defaulters. Revenue's audit programme comprises audits that

- are conducted in Revenue districts
- emanate from Revenue's special investigations or
- are conducted by its Large Cases Division.

16.2 In recent years, Revenue has introduced a risk evaluation and profiling methodology (REAP[140]). This is designed to focus the selection of cases for audit on those areas of greatest risk. However, other factors also impact on the choice of cases and in practice, taxpayers are selected for audit using different criteria depending on where a case originates.

Chapter Focus

Chapter 14 dealt, *inter alia*, with random audit which is useful in giving a view of the overall compliance level and the risk factors in the population as a whole.

This chapter examines

- the organisation and results of Revenue's other audits and investigations
- pre-audit screening and assurance checks.

It also reviews measures to deter non-compliance.

Audit Activity

16.3 Between 2007 and 2010, the yield from audit activity decreased by almost one third. This was due in part to

- the declining yield from special investigations which comprised 11% of audit yield in 2010 as compared with 23% in 2007
- a decline in the number of audits conducted in Revenue districts, which was counterbalanced to some extent by higher average audit yields.

16.4 The levels of audit coverage and associated audit yield recorded on Revenue's Audit Case Management System (ACM) between 2007 and 2010 are set out in Figure 81.

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140 REAP (Risk Evaluation Analysis Profiling system) is a computerised risk profiling system which rates taxpayers, relative to one another, using information from Revenue's other systems as well as information from third parties such as the Health Service Executive, the Department of the Environment, Community and Local Government and the Taxi Regulator.

Figure 81 Audit Activity[a], 2007 - 2010

	2007		2008		2009		2010	
	Cases	Yield €m	Cases	Yield €m	Cases	Yield €m	Cases	Yield €m
Normal Audits								
Districts	11,534	296	10,721	304	10,441	334	9,552	293
Large cases	547	193	543	132	418	186	446	81
Investigations Prosecution Division	–	–	11	2	16	7	30	9
	12,081	**489**	**11,275**	**438**	**10,875**	**527**	**10,028**	**383**
Special Investigations								
Districts	850	143	499	78	357	62	178	25
Large cases	2	–	2	–	–	–	–	–
Investigations Prosecution Division	–	–	16	13	48	7	104	23
	852	**143**	**517**	**91**	**405**	**69**	**282**	**48**
Total Audit Activity	**12,933**	**632**	**11,792**	**529**	**11,280**	**596**	**10,310**	**431**

Note: a In earlier years, not all audits were recorded on Revenues Audit Case Management System (ACM). As a result Revenue's reported audit results for those years are higher than those shown in Figure 81. By 2010, the majority of audits were recorded in ACM.

Audits in Revenue Districts

16.5 In practice, Revenue districts use a variety of mechanisms to select cases for audit. These include

- REAP – The results of REAP runs conducted on a quarterly basis are made available to case managers in selecting cases for audit.
- Specific projects aimed at targeting evasion on a sectoral basis. In 2010, projects were aimed in particular at individuals involved in the taxi, construction and cash based industries.
- Local knowledge – Cases selected based on local intelligence and other information.

16.6 Case selection methods have been changing as REAP is used more. One way of gauging the success of these changes in the mix of selection methods is by monitoring changes in average audit yield. Revenue does not currently measure average audit yield, in a way that excludes the effects of special investigations and random audits. During the audit this measure was calculated for all audits completed in Revenue districts between 2007 and 2010. The results are set out in Figure 82.

Figure 82 Average Yield from Audits[a] Conducted in Revenue Districts, 2007 - 2010

Region	Average yield			
	2007 €	2008 €	2009 €	2010 €
Dublin	25,900	30,300	39,600	34,400
South west	25,500	34,100	31,000	24,544
BMW region	27,600	28,200	30,000	30,600
East/South East	23,700	21,000	24,500	32,400
Average[b]	**25,700**	**28,300**	**31,990**	**30,600**

Notes: a Excludes special investigations and random audits.

b The national average is the average for all audits completed at Revenue district level.

16.7 Between 2007 and 2010, the average yield per case audited increased by 19%. This was made up of an increase of 24% up to 2009 followed by a drop of 4% in 2010.

Conclusion – Audits in Revenue Districts

Revenue currently focuses on the number of yielding audits, without distinction by type, as an indicator of its success in targeting. It would be useful to supplement this with the average monetary yield from those audits that have been selected on the basis of risk. This would allow the financial impact of its profiling to be gauged and regional trends tracked.

The increase in average yield per audit suggests that Revenue's increased focus on targeting those cases that present the highest risk is effective. However, the identification of cases with substantial yields must be balanced against the spread of audit activity. There has been a 17% decrease in audit activity at district level since 2007.

The increases in average yield was not uniform across the four Revenue regions. Dublin and East/South East experienced significant increases over the period. The increase in yield in the BMW region was comparatively less. The South West region had large increases between 2007 and 2009 but audit yield decreased again in 2010, to below 2007 levels.

Revenue should investigate these trends and relate them to the selection of cases and the focus of audits in each area.

Special Investigations

16.8 A number of special investigations have been carried out by Revenue in the past number of years. Five of the investigations involved a voluntary disclosure element. In those cases, taxpayers were allowed to come forward voluntarily and pay the relevant taxes and duties.

16.9 Figure 83 sets out the cumulative amounts received to the end of April 2011 as a result of each investigation. Two investigations – Life Assurance Products and Undisclosed Funds in Irish Bank Accounts – were extended in 2009. An investigation into trusts and other offshore structures began in 2009. It focused on identifying undeclared tax liabilities by persons who had transferred or settled property, assets or funds to any trusts and other similar off-shore structures. At the end of April 2011, the yield from this investigation was €38.15 million in respect of 197 cases.

Figure 83 Special Investigations - Revenue Collected to April 2011

Investigation	Year commenced	Number of cases	Receipts 2010[a] €m	Receipts to April 2011 €m
DIRT - Look Back Audits (financial institutions)	1999	37	-	225
DIRT Underlying Tax				
Voluntary Disclosure Scheme	2001	3,675	-	227
Post Voluntary Disclosure Investigations	2001	8,500[b]	1.3	421
NIB – Offshore Investment Schemes	1998	465	0.1	60
Ansbacher-type Schemes	1999	289	0.1	107
Pick Me Up Schemes	1998	71	-	1
Tribunal-related reviews	1998	49	-	41
Offshore Assets	2004	14,948	8.0	964
Undisclosed Funds – Life Assurance Products	2005	5,526	6.0	484
Undisclosed Funds in Irish Bank Accounts	2008	1,255	8.7	86
Trusts and Offshore Structures	2009	197	19.0	38
Total		**35,012**	**43.2**	**2,654**

Source: Office of the Revenue Commissioners

Notes: a This relates to actual cash received in the year. It differs from the information set out in Figure 81 as audit yield is only recognised when a case is closed. The yield in 2010 is greater than the cash receipts as it is taking account of cash received in earlier years.

b This is an estimated figure.

Conclusion – Special Investigations

The amount collected on foot of investigations in 2010 was €43 million. Of the €2.65 billion collected to date from all investigations, some €1.57 billion or 59% was collected from the voluntary disclosure schemes which formed part of five of the investigations[141] and 68% of the total cases involved in all investigations were individuals that availed of voluntary disclosure initiatives.

No new investigations were commenced in 2010.

141 Voluntary disclosure schemes were available for the investigations into DIRT Underlying Tax, Offshore Assets, Life Assurance Products, Undisclosed Funds in Irish Bank Accounts and Trusts and Offshore Structures.

Audits by Large Cases Division

16.10 Many of the companies managed in the Large Cases Division are part of a group structure[142]. Case managers deal with all cases in a group. The Division has eleven business units of which ten are organised on a sectoral basis. The remaining business unit deals with high wealth individuals. In 2009, almost half of the gross receipts in taxes and duties emanated from the Large Cases Division.

16.11 The numbers of audits conducted and the associated yield is set out in Figure 84.

Figure 84 Audits by Large Cases Division[a], 2007 - 2010

		2007	2008	2009	2010
Number of audits conducted		547	543	418	446
Yield	€m	193	132	186	81
Average yield	€	352,232	243,762	444,161[b]	180,906

Notes: a Special Investigations and random audits are excluded from this analysis.

b In 2009, one audit yielded €33.5 million in respect of VAT. The average audit yield in respect of the remainder of cases stood at €363,923.

Conclusion – Audits by Large Cases Division

The number of audits completed in Large Cases Division has decreased since 2007 and the yield in 2010 had halved by comparison with 2007.

16.12 In light of the drop in the number of audits conducted and the average yield per case, I asked the Accounting Officer to outline the reasons for the decreased level of audit activity and the processes in place to ensure that audit resources in Large Cases Division are deployed towards those cases presenting the highest risk since REAP is not used to select cases for audit.

16.13 The Accounting Officer informed me that notwithstanding the pressure on resources due to the loss of some senior auditing staff and the ongoing rebuilding of audit capability, including targeted recruitment of personnel with specific skill sets, Large Cases Division has continued to carry out a substantial compliance programme involving audits and assurance checks. The main issue that contributed to the decreased yield, was the economic downturn.

16.14 She stated that a structured approach to risk analysis is used to select the right issues for audit or intervention and then focus effort on them. Selected issues are generally those involving the greatest risk of non-compliance. The aim is to reduce the possibility that significant risks will go undetected. Large Cases Division is continuously working to improve the effectiveness of its risk analysis and compliance improvement programme, including its audit activity.

16.15 A significant difference in the administration of Large Cases Division cases is that the businesses file manual accounts which provide the case managers with comprehensive data for case profiling while other cases provide an extract of accounts.

16.16 The risk-focused audit programme takes into account the scale of company operations, business complexity and developments in the sector. Specific sector-wide projects are undertaken as appropriate.

[142] These groups comprise holding companies, subsidiary companies and associated companies.

16.17 She stated that compliance assurance in the Large Cases Division involves

- ongoing review of tax strategies and risks to identify issues for intervention
- industry research and intelligence gathering and analysis to inform case selection
- issue management, e.g. a legislative change or interpretative guidance to assist other taxpayers to comply
- systems based computer audits
- monthly monitoring of trends in audit results – numbers completed, underway and commencing, age profile of audits, yields, issues involved and time taken
- regular review of audits for probity, quality and lessons learned
- working in 'real-time', auditing the current year and other real-time interventions
- ‘locking in’ future compliance for all taxes, customs and duties.

Assurance Checks and Screening

16.18 Revenue attempts to minimise the cost of resource intensive audit by seeking assurance that the customer is broadly compliant in the areas that are the subject of the check and in addition, seeking to focus audits on the cases of greatest risk using REAP.

Assurance Checks

16.19 Assurance checks include

- verification of documentation and requests for additional information
- checks of customs documentation
- excise checks including Vehicle Registration Tax
- checks arising from suspicious transactions reports
- eligibility checks arising from special investigation voluntary disclosure schemes
- queries which examine a single aspect of a case for the purpose of testing an apparent risk highlighted by REAP.

16.20 Revenue has recorded a total of 454,796 assurance checks in 2010 that yielded €58 million (361,480 checks in 2009 with a yield of €68.5 million). The bulk of the yield (€42 million) arose out of documentation checks and requests for further information. 6% of the cases that were followed up yielded some additional tax. Large Cases Division conducted 12,315 of those checks (2.7% of the total) resulting in an additional yield of €13 million (22% of the total).

Risk Profiling

16.21 REAP is a computerised rules-driven system for evaluating risk within the taxpayer population[143] being risk rated on a quarterly basis. The information used is derived from Revenue's own information system, and third party information provided by bodies such as the Health Service Executive, the Department of Environment, Community and Local Government, the Taxi Regulator and from designated persons obliged to submit suspicious transaction reports under anti-money laundering legislation. Revenue has been piloting an extension of REAP to the PAYE area.

16.22 The system includes over 250 risk elements which derive, for example, from instances such as where returns are filed late, where information in the accounts suggest inconsistent profit margins or there is no record of declared income when third party information suggests there should be or there is a suspicion of tax evasion shown on a suspicious transaction report.

16.23 Since 2008, there has been a requirement that districts use REAP in the selection of cases for audit and Revenue has set a target that at least 60% of all cases audited will come from the top 20% risk category. In this regard, Revenue does not set targets nor measure performance in relation to the different categories of audit – special investigations, large cases audits or audits conducted at District level. Overall, an increasing proportion of cases audited are in the top 20% risk category. The results for the period 2008 to 2010 are set out in Figure 85.

Figure 85 Cases Audited in Top Risk Category[a], 2008 to 2010

	2008	2009	2010
	%	%	%
Proportion of cases audited in top 20% risk category	58	71	67

Source: Office of the Revenue Commissioners

Note: a Figures are based on audits settled in Revenue's Audit Case Management System with a risk ranking. Not all audits are recorded on that system.

16.24 Revenue has succeeded in its objective of auditing over 60% of cases that are in the top 20% of risk in 2010. However, this does not necessarily mean the cases were selected for audit for that reason. Reasons recorded on Revenue's case management system are set out in Figure 86.

143 The population consists of all live companies and sole traders, partnerships and company directors who are registered for Income Tax or Corporation Tax and other taxpayers with a live VAT, PAYE/PRSI or Relevant Contracts Tax registration.

Figure 86 Audits by Selection Reason and Region, 2010

	Region				
Selection Reason	**Dublin**	**South West**	**BMW**	**East/ South East**	**Percentage**
REAP	1,132	1,064	1,200	983	**46%**
Returns and claims reviews	957	579	564	466	**27%**
Special projects	181	230	132	227	**8%**
Voluntary disclosure/information	200	230	222	174	**9%**
Other[a]	341	223	221	226	**10%**
Total	**2,811**	**2,326**	**2,339**	**2,076**	

Note: a Other selection reasons include Random Audit Programme, local knowledge, information gained from other audits, re-audit, suspicious transactions reports and special compliance projects.

16.25 A key indicator of the effectiveness of the system is the extent to which non-yielding cases are decreasing. Figure 87 sets out the proportion of those cases in the past three years.

Figure 87 Proportion of Non-Yielding Cases[a], 2008 to 2010

	2008	**2009**	**2010**
	%	**%**	**%**
Proportion of cases with nil yield	36.7	29.5	28.2

Source: Revenue Commissioners Annual Performance Reports, 2008 to 2010

Note: a Includes all cases audited and all categories of audit including random audits, special investigations and audits conducted by districts and Large Cases Division.

16.26 While the trends are indicative of a greater use of risk profiling and more effectiveness in identifying the potential yielding cases there is still scope for further improvement. For instance, the minutes of meetings of an internal liaison and advisory group held in 2009 and 2010 noted

- There were differences in the approaches being adopted to the selection of cases using REAP. Some areas had a central screening unit at regional level, where the riskiest cases were initially screened and then selected for audit. Other areas had these units at district level. Other areas were in the process of piloting central screening units.
- In some regions profiling interventions and assurance checks were conducted on cases to resolve some of the issues identified as part of the screening process.
- While there was overall commitment to select 60% of cases from the top 20% risk rating, the actual use of REAP varied greatly from district to district.

16.27 It is apparent, however, that the REAP system does not yet have general applicability. This is demonstrated by the experience of Large Cases Division where a review was conducted in 2010 to assess the applicability of REAP to its selection of audits.

16.28 While working with the REAP team to understand the cases highlighted as risky, one Business Unit found that of the 20 REAP triggers that had resulted in cases being assessed as high risk, three were found to be factually incorrect, 15 were inappropriate or the thresholds were too small given the average case sizes in this Division. Only two of the triggers were found to have some relevance.

16.29 The review concluded that

- More comprehensive information was, in fact, available to caseworkers in the Division than was used by REAP.
- Some of the data being used by REAP was old and it was felt that the Division had a more up to date position.
- REAP triggers that were based on certain thresholds were inappropriate for most cases in the division. (For example, capital allowance claimed in excess of €40,000).

Conclusion – Assurance Checks and Risk Profiling

6% of cases which were the subject of lower intensity assurance checks yielded additional tax. The Revenue risk profiling system appears to be contributing to audit effectiveness since a greater proportion of audits are yielding additional tax than heretofore. However, some scope for improvement still exists.

As is indicated by the findings of internal reviews, the risk profiling system has not proved effective with its current rules and parameters for use in the area where the most significant tax is managed – Large Cases Division.

It is acknowledged that REAP was not specifically designed around the type of cases dealt with by Large Cases Division and that it has limitations where scale and group structures apply. Revenue has commenced a process to refine the system based on the experience of its Large Cases Division.

Measures to Deter Non-Compliance

16.30 Revenue's deterrence provisions fall into two main categories – civil penalties and criminal proceedings. In certain cases, it publishes details of persons who have defaulted on their Revenue obligations. In the case of late filing loss relief may be restricted.

Civil Penalties

16.31 Where incorrect returns are made fraudulently or negligently, penalties are generally imposed. These mainly arise out of Revenue audits. Civil penalties imposed as a result of 2010 audits amounted to €33 million (€45 million in 2009).

16.32 Revenue can also impose civil penalties for failing to submit returns on time.

- In 2010, Revenue imposed penalties of €1.9 million in 526 cases that did not submit the 2009 P35 return on time (€ 1.7 million in respect of 519 cases in 2009 in respect of the 2008 P35 returns). Due to a change in legislation in the context of the Human Rights Convention, which necessitated some fundamental changes in penalty processes, civil proceedings in respect of cases that did not pay this penalty were not taken in 2009 or 2010. However, 40 of these cases where the penalty was not paid for 2009 are now awaiting a court hearing date. Court proceedings will be taken in respect of suitable unpaid 2010 cases during the remainder of 2011.
- Penalties totalling €244,000 were imposed in 61 cases for failure to submit VAT returns.

Criminal Proceedings

16.33 Criminal proceedings arise in relation to the non-filing of returns, summary prosecutions for various other tax and customs and excise offences and prosecutions for serious evasion.

Non-Filing of Returns

16.34 Criminal prosecutions of cases that failed to file VAT returns resulted in 103 cases being heard in court in 2010 and fines of €701,600 being imposed. There were 1,217 convictions for failure to file Income Tax and Corporation Tax returns with €2.8 million in fines imposed. In addition, 60 convictions were obtained for failure to file Intrastat and Vat Information Exchange System (VIES) returns and fines of €112,200 were imposed.

Summary Prosecutions for Customs and Excise Offences

16.35 There were 509 convictions in respect of summary prosecutions for customs and excise offences in 2010 resulting in fines of €1.1 million. 19 custodial sentences were imposed, 13 of which were suspended. These included cases of cigarette and alcohol smuggling, cigarette selling, marked oil, excise licence and VRT offences.

Summary Prosecutions for Tax Offences

16.36 There were ten convictions for tax offences other than non-filing of returns, with fines totalling €33,015 imposed. The offences included failure to furnish books and records, forging documentation and providing a false name to a Revenue Officer.

Prosecutions for Serious Tax Evasion

16.37 111 cases of serious tax evasion were at various stages of the investigation and prosecution process at the end of 2009. In 2010, a further 40 cases were determined to be suitable for investigation with a view to prosecution (23 in 2009). Convictions were obtained in seven cases decided in court in 2010. The details of the seven cases are set out in Figure 88. Six of these cases were originally identified as being suitable for investigation with a view to prosecution as a result of Revenue audits and checks.

Figure 88 Convictions in 2010 for Serious Tax Evasion

Occupation/ activity	Fine	Estimated tax at risk	Offence
	€	€	
Locksmith[a]	None	613,000	Failure to furnish returns, submitting incorrect tax returns, failure to keep books and records
Doctor	1,250	50,000	Failure to furnish returns
Doctor	3,500	250,000	Failure to furnish returns
Company Director[b]	None	550,000	Submitting incorrect returns, failure to remit tax
Electrician	8,250	36,000	Failure to furnish returns, submitting incorrect returns, obtaining a VAT repayment to which he was not entitled
Director/Tax Consultant[c]	None	70,000	Claiming an Income Tax repayment to which he was not entitled, submitting incorrect returns
Haulier[d]	None	Unknown	Filing incorrect VAT returns, claiming VAT repayments to which he was not entitled, producing incorrect invoices

Source: Annual Revenue Performance Report 2010

Notes:
a A two year suspended sentence was imposed.
b Three concurrent sentences of one year, nine months and four months were imposed (suspended for three years).
c A 15 months imprisonment was imposed in respect of each of the seven charges (to run concurrently).
d A three year sentence was imposed on each of 15 charges, suspended on condition of 240 hours community service.

16.38 Seven cases were closed during 2010 leaving 137 cases at various stages of the investigation and prosecution process at the end of 2010. By the end of April 2011 a further five cases had been closed and an update of the status of the 137 cases is shown in Figure 89.

Figure 89 Status of Serious Tax Evasion Cases at April 2011

Status	Number of cases
Under investigation	66
With the Revenue Solicitor's Office	10
Submitted to the Director of Public Prosecutions	3
Directions issued by the Director of Public Prosecutions to prosecute	29
Before the court	18
Closed	5
Convictions obtained	6
Total	**137**

Source: Office of the Revenue Commissioners

16.39 51% of these cases were identified as being suitable for investigation as a result of Revenue audits and checks, 20% arose from Revenue investigations, 15% were identified from suspicious transaction reports and 14% were based on information provided by other agencies and individuals.

Prosecutions for Serious Customs and Excise Offences

16.40 There were six convictions for serious Customs and Excise offences in 2010. Fines of €2,500 and €850 were imposed in two cases. Four suspended custodial sentences, each of two years, were imposed.

Publication of Defaulters

16.41 Details of audit settlements are published where Revenue accept a specified sum in excess of €33,000 in settlement of any additional liability for tax, interest and penalties. Cases are not published where

- a 'qualifying disclosure' is accepted
- the settlement is less than €33,000
- the penalty does not exceed 15% of the tax ultimately due.

16.42 Figure 90 sets out the total amounts of tax, interest and penalties in published cases settled between 2007 and 2010.

Figure 90 Cases of Non-Compliance Published, 2007 - 2010

Status	Number of cases	Total tax, interest and penalties €m
2007	555	144
2008	401	75
2009	356	97
2010	305	68

Source: Office of the Revenue Commissioners

Loss Relief Restriction

16.43 Revenue has estimated that the future tax impact of losses restricted as a result of audits conducted in 2010 at €127 million (€290 million in 2009).

16.44 In addition, the Taxes Consolidation Act 1997 provides for restrictions on the use of losses where returns are not filed on time (within nine months of the end of the company's accounting period).

16.45 In cases where the return is filed more than two months after the due date, loss relief is restricted by 50% up to a maximum of €158,715. The restriction is reduced to 25% with a maximum restriction of €31,740 where the return is filed late, but within two months of the due date. The tax value of the losses in the case of filing delay is not forgone but is postponed to a later claim period.

Conclusion – Deterrence Measures

Penalties arising out of audits amounted to €33 million. In the case of litigation, penalties tend to be smaller. Civil cases yielded €2.1 million and criminal cases yielded €4.7 million. Over 150 cases of serious tax evasion were being pursued during 2010. The rate of disposal of these cases is low with only seven finalised in court in 2010 and a further seven dropped.

Conclusion

While the behaviour of taxpayers is best gauged by means of random sampling as outlined in Chapter 14, the efficiency of collection is likely to be optimum where a risk based approach is employed.

Audits selected on a risk basis in Revenue districts yielded €293 million of the total yield of €431 million in 2010. A further €58 million was collected following lower intensity assurance checks.

Overall, an upward trend in the audit yield over time suggests that Revenue's computerised risk assessment and profiling system has increased its effectiveness in identifying cases with material financial non-compliance. In addition, less cases selected for audit are non-yielding which also suggests improvement in profiling. However, the number of audits conducted in Revenue districts has decreased by 17% since 2007.

In view of variations noted on audit, it would be useful for Revenue to track the average audit yield by region.

The number of audits completed in Large Cases Division has decreased since 2007 and the yield in 2010 had almost halved in comparison with 2007. There were resource pressures in this area. Revenue is taking steps to rebuild its audit capability.

No new special investigations were commenced in 2010. €43 million was collected from existing investigations.

Penalties arising out of audits amounted to €33 million. In the case of litigation, penalties tend to be smaller. Civil cases yielded €2.1 million and criminal cases yielded €4.7 million. Over 150 cases of serious tax evasion were being pursued during 2010. The rate of disposal of these cases is low with only seven finalised in court in 2010 and a further seven dropped.

Chapter 17

Impact of Losses

Office of the Revenue Commissioners

Impact of Losses

17.1 The profit of a trading undertaking as presented in its financial statements is the difference between its revenue and expenses. In general, costs incurred wholly and exclusively for the purpose of trade can be offset against revenues in computing taxable profit.

17.2 Loss relief can apply in the case of companies, sole traders and persons who are trading as partnerships. The main focus of this chapter is on losses of companies which account for the bulk of losses claimed.

Corporation Tax Loss Relief

17.3 Companies are liable for Corporation Tax in respect of all profits arising from either income or gains. These are taxable as follows

- Trading income is taxed at a rate of 12.5%.
- Non-trading income[144] is taxed at 25%.
- Some manufacturing companies have their profits taxed at an effective rate of 10%[145].
- Capital gains are chargeable to Corporation Tax at a rate of 25%.

17.4 Where following the determination of the taxable result of a company there is a net loss, that loss can be utilised to reduce Corporation Tax in the current, preceding or subsequent accounting periods.

- In the current accounting period, trading losses can be set off against trading and non-trading profit, including chargeable gains[146]. Relief on non-trading profit and chargeable gains is provided on a value basis[147].
- Group relief allows one company in a group to surrender its trading loss in the current accounting period to another group member for offset against profits in the corresponding accounting period.
- Carry back of losses[148] allows trading losses to be carried back against profits in the previous tax period. This type of relief allows a cash flow benefit to the company concerned through the repayment of tax already paid.
- Any unused trading losses can be carried forward against future profits of the same trade indefinitely but must be used against the earliest available profits.
- Where a trade is discontinued, a trading loss incurred in the last 12 months of the discontinued trade, may be carried back and set against trading income in the same trade in the preceding three years, resulting in a reduction of the tax liability or repayment of tax.

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[144] Non-trading income includes Case III income including discounts, interest and foreign income, Case IV income, including patent royalties and miscellaneous income and Case V income, which includes rental income from land and buildings in the State. Also included at this rate is trading income from 'excepted trades', which includes dealing in land and trading income from mining and petroleum operations.

[145] This is no longer available since 31 December 2010.

[146] Overall, annual results are netted and losses in the year on one activity can be netted against another.

[147] This ensures that the value of any loss relief allowed remains the same irrespective of the rates of tax that apply to the activities concerned.

[148] Carry back of losses is only available to companies chargeable to Corporation Tax. It is not available to sole traders and partnerships where the persons are chargeable to Income Tax.

17.5 In some cases companies can claim capital allowances (as an offset against profit) in relation to certain types of capital expenditure. A loss created or augmented by capital allowances is treated as a trading loss. A full list of capital allowances available is set out at Annex A.

17.6 My 2009 report examined the extent of loss relief in relation to Corporation Tax. However, because of deficiencies in Revenue's information systems it was not in a position to generate information in relation to the amount of losses actually used in any year and was unable to provide information in relation to the value of losses unused and available for carry forward to future years.

17.7 During 2010, Revenue introduced changes to the assessing system to allow it to estimate the amount of losses and capital allowances that were not used in a particular tax period. However, due to the structure of the tax returns, it is not yet in a position to differentiate between unused losses and unused capital allowances.

Restrictions on Loss Utilisation

17.8 The extent to which reported losses are utilised is dependent on the generation of profits against which to offset them. In addition, the utilisation of loss relief is limited in circumstances where

- a return is submitted late
- a trade is discontinued
- the company is one of the credit institutions participating in the NAMA scheme.

17.9 Where a tax return is submitted late, the offset of losses is restricted. The restrictions are graded by reference to the delay in filing and there is a monetary cap on the level of each restriction[149]. The restrictions apply to the offset of losses against profits in the current and immediately preceding accounting period. The restriction does not amount to a complete denial of loss reliefs since losses can be offset against later accounting periods. The adverse effect on a company failing to submit its return on time will be a cash flow one.

17.10 Normally, the transfer of a trade from one company to another constitutes the discontinuance of that trade and trading losses are not available for carry forward. However, unused losses of a trade that is transferred from one company to another may be used by that other company where it carries on the same trade and an interest in the trade of not less than 75% is held by the same persons before and after the change.

17.11 In the case of participating[150] institutions in accounting periods commencing after the passing of the National Asset Management Agency Act[151], the maximum amount of losses carried forward that can be used in each period is half of the excess of group trading profits over group trading losses for that period, so that a minimum of 50% of group trading profits will remain chargeable to tax in each period. This restriction effectively lengthens the period of time over which loss relief may be used by the participating institutions.

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[149] Where a return is more than two months late, the use of losses is restricted to 50%, subject to a maximum restriction of €158,715. Where the return is less than two months late, the restriction is reduced to 25% or a maximum of €31,740.

[150] There are five credit institutions participating in the NAMA scheme – three banks and two building societies.

[151] The National Asset Management Agency Act 2009 amended the Taxes Consolidation Act 1997 to restrict the use of losses.

Chapter Focus

This chapter reports the results of a review that set out to establish

- the trend in the value of losses reported, by sector, in respect of accounting periods between 2007 and 2009
- the extent of utilisation of losses and capital allowances in 2009 which was the last full year for which tax returns have been submitted
- the level of unused losses and capital allowances being carried forward in 2009.

While it focused specifically on Corporation Tax, information is also included on Income Tax loss relief.

Information on Losses

17.12 In the case of companies, Revenue does not have information on the extent of losses incurred until nine months after the end of the relevant accounting period, at which point Corporation Tax returns are filed. For example, Corporation Tax returns for accounting periods ending December 2009[152] were required to be submitted by September 2010.

Trading and Manufacturing Losses

17.13 In relation to tax returns submitted in respect of accounting periods ending in 2007, 2008 and 2009, Revenue compiled details for each year that showed

- the unused losses brought into that accounting period
- the losses reported in that period.

These are set out, by sector, in Figure 91.

[152] The accounting period is a period chosen by the taxpayer.

Figure 91 Trading and Manufacturing Losses – Corporation Tax Returns 2007 to 2009[a]

Sector	2007		2008		2009	
	Losses forward €m	Losses in period €m	Losses forward €m	Losses in period €m	Losses forward €m	Losses in period €m
Financial Intermediation	1,546	8,815	5,777	9,024	13,941	22,989
Real Estate, Renting and Business Activities	1,705	1,120	2,992	3,710	2,815	3,182
Construction	358	436	390	998	855	1,319
Wholesale and Retail Trade	596	497	553	841	1,154	1,140
Manufacturing	579	1,569	762	1,465	1,171	1,907
Other[b]	1,069	1,544	1,221	1,344	1,721	1,515
Total	**5,853**	**13,981**	**11,695**	**17,382**	**21,657**	**32,052**

Source: Office of the Revenue Commissioners

Notes: a This information was derived from Corporation Tax returns, due in September 2010 in respect of accounting periods ending in 2009.

b Other includes agriculture, hunting and forestry, fishing, mining and quarrying, electricity, gas and water, hotels and restaurants, education, health and social work, public administration and defence, other community, social and personal service activities, activities of households, extra territorial organisations and bodies and all other sectors unknown.

17.14 There is an upward trend in the losses disclosed in the relevant tax returns. The losses incurred have risen from €14 billion in 2007 to €32 billion in 2009. Similarly the losses brought into the year have increased from €6 billion in 2007 to €22 billion in 2009.

17.15 Unsurprisingly, the biggest increase in trading losses reported in the 2009 tax returns is in the financial intermediation sector where losses totalling €23 billion were reported – making up 72% of the total losses disclosed.

Losses Available for Offset against Profits

17.16 The current structure of the Corporation Tax return does not allow for the identification of

- the actual level of losses utilised in the year
- losses and capital allowances that are surrendered for group relief
- the value of losses unused and available for carry forward to future years.

17.17 In 2009, a total of €69.5 billion was available for offset against profits (the equivalent figure for 2008 was €43.2 billion). This comprised

- trading losses brought into the year of €21.1 billion as well as €0.6 billion in respect of manufacturing losses
- trade and manufacturing losses incurred of €30.9 billion and €1.2 billion respectively
- capital allowances totalling €15.7 billion.

Utilisation and Carry Forward of Losses

17.18 Revenue has calculated the amount of unused losses and capital allowances available for carry forward to future years from 2009 based on available information and estimates of the level of losses utilised in relation to group relief. It was estimated that approximately €49.6 billion by way of losses and capital allowances was available for carry forward and offset against profits for 2010 and subsequent years. This estimate was based on the data set out in Figure 92.

Figure 92 Losses Available for Carry Forward, 2009 Tax Returns

	Basis of calculation	€m
Current year losses and capital allowances ***not used*** before surrendering as group relief and prior to offset against prior years tax	Actual	36,290
Losses brought forward from an earlier year that have not been used	Actual	16,784
Less — Losses set off against prior years tax	Actual	(868)
Less — Losses/Capital Allowances surrendered via Group relief	Estimated	(2,573)
Estimated Losses and Capital Allowances available for carry forward to future years		**49,633**

Source: Office of the Revenue Commissioners

17.19 Using this estimate of €49.6 billion in relation to the value of unused losses at the end of 2009, together with information on the level of losses available for use in 2009 (€69.5 billion), it is estimated that approximately €19.9 billion of losses and capital allowances were offset against profits in 2009. The breakdown by sector is shown in Figure 93.

Figure 93 Estimate of Losses Available, Utilised and Unused[a]

Sector	Total Losses and Capital Allowances available 2009	Estimated amount utilised 2009	Estimated amounts unused at end 2009
	€m	€m	€m
Financial Intermediation	39,057	4,752	34,305
Real Estate, Renting and Business Activities	12,803	6,571	6,232
Manufacturing	5,708	3,551	2,157
Wholesale & Retail Trade	3,377	1,645	1,732
Transport, storage and Communications	2,922	1,204	1,718
Construction	2,472	601	1,871
Other[b]	3,207	1,589	1,618
Total	**69,546**	**19,913**	**49,633**

Notes: a This information was derived from Corporation Tax returns, due in September 2010 in respect of accounting periods ending in 2009.

b Other includes agriculture, hunting and forestry, fishing, mining and quarrying, electricity, gas and water, hotels and restaurants, education, health and social work, public administration and defence, other community, social and personal service activities, activities of households, extra territorial organisations and bodies and all other sectors unknown.

17.20 Around €34.3 billion of losses are available for offset against future profits in the financial intermediation sector. Just over half of this relates to three institutions participating in NAMA. Legislative provisions included in the National Asset Management Agency Act 2009 effectively mean that for those institutions that return to profitability, only 50% of profits in any year can be offset against available losses.

International Context

17.21 A recent OECD report estimated that it may take some three to eight years for the overall stock of bank losses to be utilised[153]. The report drew attention to the increased risk faced by revenue bodies as a result of those losses. These included

- the increased risks of inappropriate transfer pricing[154] in the case of loss-making banking groups and of loss making affiliates within profit-making banking groups.
- the risk that corporate reorganisation could be used inappropriately to transfer profits or losses between different locations and allow an unintended use of losses.
- the risk that financial instruments would be utilised to transfer losses to entities or branches within a group in order to utilise losses, this would include the use of call or put options[155] and the purported transfer of risks through swaps, other derivatives and debt waivers.

17.22 The report noted that new avoidance techniques were emerging as some loss-making banks try to maximise the use of their commercial losses for tax purposes. The report concluded that tax audits should continue to play a key role in detection, deterrence and prevention of aggressive tax loss planning supported by international exchange of information and cooperation between revenue bodies.

Income Tax Loss Relief

17.23 There is also provision to allow for the offset of losses against Income Tax. Loss relief can be granted in the current and subsequent years. Terminal loss relief is also available in the case of discontinuance of a trade or profession.

17.24 Total Income Tax trading losses used in 2009 were €520 million (€535 million in 2008). In addition, relief for trading losses of €791 million were unused in 2009 (€557 million in 2008) and was available for carry forward to future years.

17.25 Unused rental losses carried forward to 2009 from earlier periods for those liable to self-assessed Income Tax totalled €1.8 billion in 2009. The comparative figure for 2008 was €1.7 billion.

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153 OECD, Addressing Tax Risks involving Bank Losses 2010.

154 Transfer pricing which relates to the charges made between related parties for goods, services or the use of property (including intangible property) is a key risk area in international taxation both in profit making and loss making contexts. The report recommended that Revenue bodies verify the consistency of claims under the arms length principle. Under the arms length principle, the remuneration of a subsidiary or profit allocation to a branch that is part of a multinational banking group has to reflect the functions performed, taking into account the risks assumed and the assets used by it.

155 Put/call options are contracts that give the purchaser of the option the right, but not the obligation, to buy (a call option) or to sell (a put option) a particular financial instrument or commodity at a predetermined price (strike price) within a specific time span or on a specific date.

Accounting Officers Views

I asked the Accounting Officer

- for Revenue's estimate of the overall impact of losses on future tax revenues and the results of any profiling exercises conducted by Revenue in this regard
- for her views in relation to the losses in the financial intermediation sector, Revenue's estimate of the timescale involved in utilisation of these losses and the restrictions imposed in relation to utilisation of losses by institutions participating in NAMA.

Impact of Future Tax Revenues

17.26 The Accounting Officer stated that it is difficult to estimate the future impact on tax yield of any overhang of unused losses. The use of losses depends on the capacity of companies to generate profits to absorb those losses and on the number of companies with significant losses that may never be absorbed because they will cease trading.

17.27 She stated that the profile of Corporation Tax payers is also a factor since

- A very significant proportion of Corporation Tax yield is concentrated in a small number of consistently profitable companies – mainly subsidiaries or branches of large multinationals. The yield from these companies will be unaffected by losses.
- A large majority of companies filing Corporation Tax returns either pay no Corporation Tax or a relatively small amount.

17.28 Given these factors, the Accounting Officer stated that it is unlikely that the overhang of losses will ever be fully absorbed and the amount of unused losses is likely to remain very significant.

Losses in the Financial Intermediation Sector

17.29 The Accounting officer noted that while the OECD report on tax risks involving bank losses estimates that it could take three to eight years for the overall stock of bank losses to be utilised, this estimate was based on aggregate data from 17 countries with varying rules in regard to the utilisation of tax relief on losses, including some that impose time limits on the carry forward of losses. Because of the uncertainties in this area, Revenue could not produce an estimate with an acceptable degree of reliability.

17.30 She noted that the OECD report on bank losses emphasises that the extent of governments' exposure to bank tax losses depends to a large extent on the likely availability of future bank profits against which these losses can be offset. In this regard

- A large proportion of the estimated unutilised losses of €34.3 billion at the end of 2009 are confined to a very small number of companies. Just five companies account for €28 billion (or 82%) of the unutilised losses at December 2009 – three are NAMA entities.
- In looking at the future impact of the losses it needs to be taken into account that two of the five institutions (accounting for about 45% of unutilised losses) are in the process of a 'wind down' over the next ten years and will not be allowed to take on any new business activities.

17.31 In relation to restrictions on the utilisation of losses in respect of institutions participating in the NAMA scheme, the Accounting Officer stated that the provisions in the NAMA Act do not include any restriction on participating institutions in relation to offsetting losses against previous years' profits and the normal rules apply whereby a company incurring a trading loss in an accounting period can carry that loss back for offset against the profits of its immediately preceding accounting period (of the same length).

Conclusion

Reported losses have increased substantially between 2007 and 2010. Based on analysis of company tax returns due by September 2010, in respect of accounting periods ending in 2009, just under €20 billion in losses and capital allowances was utilised in 2009 and about €50 billion was unused.

€34 billion of the losses available for offsetting against profits related to the financial intermediation sector. A recent OECD report estimated that it may take three to eight years for the overall stock of bank losses to be utilised. Revenue was not in a position to provide an estimate of the timescale involved or the extent to which such losses would be utilised in relation to companies in the financial intermediation sector in Ireland.

However, based on its assessment of the profile of loss making entities it is Revenue's view that it is unlikely that a large proportion of the loss overhang will be absorbed since certain loss making banks are being wound down and are unlikely to have profits against which the accumulated losses can be offset.

Nonetheless, losses will have a significant impact on future tax revenues. The main tax collection impact would be in the financial intermediation and construction sectors where 88% and 76% of the cumulative losses available in 2009 were not utilised. By comparison, utilisation of losses was much higher in other sectors where, on average, over half of the available losses was utilised.

Net receipts of €3.94 billion were received in 2010 in relation to Corporation Tax. In 2009, 29% of the available losses were utilised. It is estimated that the utilisation of losses and capital allowances as set out in Figure 93 reduced the tax take by approximately €2.5 billion[156].

[156] An effective tax rate of 12.5% was used to estimate the effect of losses utilised in 2010.

Annex A Capital Allowances

The categories of capital allowances and the relevant offset that can be claimed are set out below.

Capital Allowances, Categories of Expenditure and Tax Relief Allowed

Category of Expenditure	Rate of Write-Off
Plant & Machinery	12.5% per annum over an 8 year period.
Taxis	40% on reducing balance basis.
Motor Vehicles	12.5% on a straight line basis - maximum qualifying cost is €24,000.
Industrial Buildings	Annual allowance of 4%, in respect of buildings used for manufacturing.
Market Gardening, Intensive Production of Livestock	10% per annum for 10 years.
Hotels and Holiday Camps	Allowance of 4% per annum over 25 years, 15% in certain specified circumstances.
Holiday Cottages	10% per annum over 10 years where the expenditure was incurred by 31 July 2008.
Guest Houses, Holiday Hostels, Caravan & Camping Sites	Annual Allowance of 4% over 25 years.
Certain Rented Residential Accommodation	15% per annum on a straight line basis for years 1 to 6 and 10% in year 7 for refurbishment expenditure incurred on multi-unit residential accommodation up to 31 July 2008.
Student Accommodation	100% allowance against rental income in the first year the property is let. Deadline for incurring qualifying expenditure under this scheme was 31 July 2008.
Section 23 Relief for Rented Residential Accommodation in qualifying areas	100% allowance against rental income in the first year the property is let. Deadline for incurring qualifying expenditure under this scheme was 31 July 2008.
Childcare Facilities	15% per annum on a straight-line basis for years 1 to 6 and 10% in year 7 where expenditure is incurred by 31 March 2012. 100% accelerated capital allowances are also available.
Private Nursing Homes, Convalescent Homes, Mental Health Centres	15% per annum on a straight-line basis for years 1 to 6 and 10% in year 7 where expenditure was incurred by 30 June 2011.

Category of Expenditure	Rate of Write-Off
Nursing Home Residential Units	15% per annum on a straight-line basis for years 1 to 6 and 10% in year 7 where expenditure was incurred by 30 April 2010.
Private Hospitals	15% per annum for years 1 to 6 and 10% in year 7 where expenditure is incurred by 31 December 2013.
Sports Injury Clinics/Third Level Education Buildings	15% per annum for years 1 to 6 and 10% in year 7 where expenditure was incurred by 31 July 2008.
Park & Ride Facilities, Multi Storey Car Parks	In the case of owner-occupiers, 100% accelerated allowances are available. Passive investors are entitled to claim allowances at a reduced rate of 50% in year 1 and 4% per annum thereafter. The termination date for incurring qualifying expenditure was 31 July 2008.
Area Based Schemes	Accelerated allowances of 50% with 4% per annum thereafter. The termination date for incurring qualifying expenditure was 31 July 2008.
Energy-efficient equipment	Allowances of 100% in year of expenditure for certain energy-efficient equipment purchased by companies for use in a trade.
Intangible Assets	Allowances based on accounting depreciation with the option for a straight-line allowance over 15 years. Allowances capped at 80% of trading income of the relevant trade in which intangible assets are used.

Source: Office of the Revenue Commissioners