Comptroller and Auditor General

Annual Report

2004

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

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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.

Report of the Comptroller and Auditor General on the Accounts of the Public Services — 2004

I am required under Article 33 of the Constitution to report to Dáil Éireann at stated periods as determined by law. Under Section 3 of the Comptroller and Auditor General (Amendment) Act, 1993, I am required to report to Dáil Éireann on my audit of the Appropriation Accounts of Departments and Offices and the accounts 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 hereby present the report for 2004 in accordance with Section 3 of the aforementioned Act.

John Purcell
Comptroller and Auditor General

9 September 2005

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Chapter 1

General Matters

1.1 Financial Outturn

The publication *Audited Appropriation Accounts of Departments and Offices for 2004* (Prn.A5/0039) includes a summary which shows the amount to be surrendered as €568.04m. This is arrived at as shown in Table 1.

Table 1 Outturn for the year 2004

	€000	€000	€000
Estimated Gross Expenditure			
Original Estimates	35,806,828		
Supplementary Estimates	166,919	35,973,747	
Deduct:-			
Estimated Appropriations-in-Aid			
Original Estimates	2,865,678		
Supplementary Estimates	33,966	2,899,644	
Estimated Net Expenditure			33,074,103
Actual Gross Expenditure		35,322,512	
Deduct: -			
Actual Appropriations-in-Aid		3,053,378	
Net Expenditure			32,269,134
Surplus for the Year			804,969
Deferred Surrender			236,967
Amount to be Surrendered			**€568,002**

The amount to be surrendered represents 1.72% of the supply grant as compared with 1.01% in 2003.

Extra Exchequer Receipts

Extra Receipts payable to the Exchequer as recorded in the Appropriation Accounts amounted to €211,646,246.

Surrender of Balances of 2003 Votes

The balances due to be surrendered out of Votes for Public Services for the year ended 31 December 2003 amounted to €313.96m. I hereby certify that these balances have been duly surrendered.

Stock and Store Accounts

The stock and store accounts of the Departments have been examined with generally satisfactory results.

Chapter 2

Office of the Revenue Commissioners

2.1 Revenue Account

Basis for Audit

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

I am also required under Section 3 of the Comptroller and Auditor General (Amendment) Act, 1993 to carry out such examinations as I consider appropriate in order to ascertain whether systems, procedures and practices have been established that are adequate to secure an effective check on the assessment, collection and proper allocation of the revenue of the State and to satisfy myself that the manner in which they are being employed and applied is adequate. Sections 2.2 to 2.9 refer to matters arising from this examination.

Revenue Collected

Revenue collected under its main headings in 2004 is shown in Table 2.

Table 2 Revenue Collected[a]

	Gross Receipts €m	Repayments €m	Net Receipts €m	2003 Net Receipts €m
Income Tax	13,189	2,494	10,695	9,156
Value Added Tax	13,635	2,918	10,717	9,716
Excise	5,242	176	5,066	4,736
Corporation Tax	5,707	372	5,335	5,155
Stamps	2,106	36	2,070	1,664
Customs	178	4	174	137
Capital Acquisitions Tax	200	10	190	213
Capital Gains Tax	1,548	20	1,528	1,436
Residential Property Tax	—	—	—	1
Total	**41,805**	**6,030**	**35,775**	**32,214**

[a] Total gross collection amounted to €48.7 billion as levies and fees such as PRSI (€6.7 billion), Health Levy (€129m) and Environmental Levy (€14m) are collected for other Departments.

Of the net receipts of €35,775m, a total of €168m was paid during 2004 under Section 3 of the Appropriation Act, 1999 from the proceeds of tobacco excise to the Vote for Health and Children. €35,572m was paid into the Exchequer which represented a prepayment of €333m. The amount prepaid at the end of 2003 was €368m. Most of the prepayment is due to the transfer into the Exchequer of moneys received from taxpayers as deposits and payments on account pending final settlement of tax liability. Such amounts are rarely repaid to the taxpayer and will subsequently be included in the relevant tax receipts figures as and when liability is finalised. An enhancement to Revenue's systems during 2004, introduced procedures which will allow most payments on account to be allocated and processed as tax receipts.

2.2 Tax Written Off

The Revenue Commissioners have furnished me with details of the €173m of taxes written off during the year ended 31 December 2004. Details of the total amount written off and the distribution according to the grounds of write-off are shown in Table 3 and Table 4.

Table 3 Taxes Written Off

Tax	2004 €000	2003 €000
Value Added Tax	72,369	41,792
PAYE	36,862	17,505
Corporation Tax	8,326	5,895
Income Tax	16,385	34,683
Capital Gains Tax	868	977
Other Taxes	1,120	1,986
PRSI	36,618	16,607
Total	**172,548**	**119,445**

Table 4 Grounds of Write Off

Grounds of write-off	2004 No. of Cases	2004 €000	2003 No. of cases	2003 €000
Liquidation/Receivership/Bankruptcy	2,097	88,519	337	29,442
Ceased trading – no assets	2,760	40,447	2,277	32,390
Deceased and Estate Insolvent	176	1,350	200	2,022
Uneconomic to pursue	19,359	23,162	38,844	39,322
Unfounded Liability	209	1,983	151	1,688
Cannot be traced / Outside Jurisdiction	586	9,615	331	5,978
Compassionate Grounds	248	2,322	81	926
Uncollectable due to financial circumstances of taxpayer	706	5,150	520	7,677
Totals	**26,141**	**172,548**	**42,741**	**119,445**

The increase of €53m in the amount written off is mainly due to a review and write off of old insolvency debt on record (this category of write off increased by almost €60m over 2003). In 2004, €3.3m was written off on an automated basis consisting of cases with small balances (less than €500) which were uneconomic to pursue. Cases under general investigation, potential Ansbacher cases, and cases under the control of the Criminal Assets Bureau are excluded from all write off procedures.

The Internal Audit Branch in Revenue undertakes an annual examination of tax write offs. The 2004 audit examined a sample of 171 cases representing 22% (€37m) of the value of non-automated write offs (€169m). The results of the ten automated write off runs were also examined and the application of the authorised selection criteria was confirmed. Commonality checks are designed to establish, prior to tax being written off, whether related entities have outstanding tax liabilities. Write off procedures provide that where a commonality check identifies related entities with tax liabilities greater than €250,000, the case should be referred to the Collector General's Dedicated Pursuit Unit for review prior to any write

off. Of the cases sampled by Internal Audit, 92 met the criteria for commonality checks but the check was not recorded as being carried out in 29 of those cases. Internal Audit carried out a commonality check on the 92 cases and identified 7 that should have been referred to the Dedicated Pursuit Unit but were not. It was also considered that one of the 171 cases sampled should not have been written off (as there was an overpayment on record that equalled the amount of the outstanding tax but had not been offset) and that another was written off prematurely (before all appropriate avenues of collection had been exhausted). The total amount involved in these two cases was some €76,000 (€25,000 and €51,000 respectively). In the first case the overpayment has been offset against the amount owing and the write off has been reversed. In the second case, the original debt has been reduced by €23,000 following adjustment of estimates incorrectly raised and a further attempt to collect the debt is being made.

2.3 Outstanding Taxes and PRSI

Table 5reflects the activities and transactions in the twelve-month period ended 31 March 2005. Table 6 sets out an aged analysis of the balance outstanding at 31 March 2005. The tables were prepared on the basis of information furnished by the Revenue Commissioners.

Table 5 Outstanding Taxes and PRSI

						Analysis of Balance at 31 March 2005	
Balance at 31 March 2004	**Tax or Levy**	**Net Charges Raised**	**Paid**	**Written Off**	**Balance at 31 March 2005**	**Under Appeal**	**Available for Collection**
€m		**€m**	**€m**	**€m**	**€m**	**€m**	**€m**
346	VAT	9,984	9,985	56	289	64	225
186	PAYE	9,513	9,510	28	161	4	157
198	PRSI	6,579	6,573	28	176	2	174
306	Income Tax (Excluding PAYE)	2,488	2,485	17	292	64	228
—	DIRT	163	163	—	—	—	—
157	Corporation Tax	4,448	4,387	78	140	56	84
150	Capital Gains Tax	1,542	1,544	—	148	88	60
12	Capital Acquisitions Tax	1	10	—	3	—	3
8	Abolished Taxes	—	—	—	8	—	8
1,363	**Total**	**34,718**	**34,657**	**207**	**1,217**	**278**	**939**
3.1%	**Debt as a % of gross collection[a]**				**2.5%**	**0.6%**	**1.9%**

[a] Gross collection in 2003 was €43,968m and in 2004 was €48,705m.

Table 6 Aged Analysis of Debt at 31 March 2005

Tax	**Total tax outstanding at 31 March 2005**	**Amounts outstanding for 2004**	**Amounts outstanding for 2003**	**Due for periods 1990/91 to 2002**	**Due for earlier periods**
	€m	**€m**	**€m**	**€m**	**€m**
VAT	289	49	83	157	—
PAYE	161	88	21	51	1
PRSI	176	99	27	49	1
Income Tax	292	2	69	212	9
Corporation Tax	140	27	25	84	4
Capital Gains Tax	148	3	32	112	1
Capital Acquisitions Tax	3	—	—	3	—
Abolished Taxes	8	—	—	8	—
Total	**1,217**	**268**	**257**	**676**	**16**

2.4 Revenue Audit Programme

Overall Audit Programme

In a self-assessment system returns filed by compliant taxpayers are accepted as the basis for calculating tax liabilities. The validity of returns is established by the auditing of a selection of cases either through reviewing and seeking further verification of particular details or by the examination of documents and records at a taxpayer's premises. The outcome of the 2004 programme of Revenue audits is summarised in Table 7.

Table 7 Revenue Audit Programme

Audit Type	2004		2003	
	No. of audits completed	Yield €m	No. of audits completed	Yield €m
Comprehensive	4,058	382.3	4,359	226.3
Value Added Tax	2,776	50.0	3,951	76.4
PAYE Employers	517	5.1	874	18.1
Relevant Contracts Tax (RCT)	439	7.0	231	1.6
Combined Fiduciary (VAT, PAYE and RCT)	848	18.4	544	13.2
Capital Acquisitions Tax	677	6.3	112	5.6
Verification Audits and Desk Reviews	6,750	76.4	5,695	86.8
Customs Audits[a]	162	2.4	214	0.5
Excise Audits[a]	25	—	45	—
Environmental Levy Audits[a]	59	0.1	13	—
Powers of Inspection Audits[a]	10	1.6	—	—
Investigation Branch	—	—	1	0.4
Anti-Avoidance	—	—	3	0.3
DIRT	—	—	8	0.8
Total	**16,321**	**549.6**	**16,050**	**430.0**

[a] Details of these audit types are included for the first time, 2003 details have been restated.

Comprehensive Audits

The selection of cases for comprehensive audit is made on the basis of such factors as screening of annual returns, re-audit of cases with previous undercharges, other information available to Revenue and random selection. For 2003 and 2004, selection was also based on information relating to bogus non-resident accounts obtained from financial institutions under High Court orders — 1,690 comprehensive audits were completed in bogus non-resident account cases in 2004 (2,460 in 2003). Generally, a settlement is agreed following completion of the audit and any outstanding amount is paid. A number of settlements involve the restriction of losses which may be carried forward against future years' profits. Where an Inspector is unsuccessful in collecting the additional amount of tax and interest arising on audit adjustments, the amounts are referred to the Collector General for collection.

The outcome of the 4,058 comprehensive audits completed in 2004 is detailed in Table 8. The overall yield of €382.3m includes interest charges of €110.5m and penalties of €39.3m.

Table 8 Yield from Comprehensive Audits

	Income Tax		Corporation Tax	
	Number	Yield	Number	Yield
Agreed Settlements:				
€1 to €12,700	1,792	€3.5m	65	€0.8m
€12,701 to €100,000	992	€39.2m	110	€4.8m
€100,001 to €500,000	347	€73.1m	49	€12m
€500,001 to €1m	63	€44.7m	11	€8m
Over €1m	27	€145.5m	10	€31.5m
Other Settlement Activity:				
Returns accepted – no additional tax payable	264	—	308	—
Settled by restriction of losses carried forward to future years	6	€0.2m	3	€18.5m
Referred to Collector General for enforcement action	11	€0.5m	—	—
Totals	**3,502**	**€306.7m**	**556**	**€75.6m**

Random Audits

The traditional random audit programme was not carried out for 2004 due to a change in Revenue strategy as a result of a review of the programme. However, 25 cases selected under the programme for previous years were completed in 2004, 13 of which yielded €155,153 in tax, interest and penalties.

For 2005, Revenue introduced a Taxpayer Compliance Testing Programme. The programme has two primary functions

- To measure and track compliance with all tax legislation, and
- To ensure that all tax payers run the risk of being selected for audit.

The programme selected 400 cases on which full comprehensive audits are being carried out. The cases were selected from those that had a live registration for any of the following taxes — Income Tax, Corporation Tax, VAT, Employer's PAYE/PRSI and Relevant Contracts Tax. Selection was pro rata for each of the regions and the Large Cases Division. The target date for completion of the programme is September 2005 and evaluation of the programme is planned for December 2005.

2.5 Prosecutions

Under Revenue prosecution strategy, Regions and Divisions forward cases to Investigation and Prosecutions Division for investigation with a view to criminal prosecution where there is prima facie evidence of serious revenue offences having been committed. These cases are further evaluated within the Division before commencement of the resource intensive criminal investigation work which can take several years before reaching the Courts. In 2004, 57 cases were referred to the Division for consideration and 31 were accepted for investigation with a view to prosecution. In the one case decided in Court in 2004, an individual was convicted of submitting incorrect Capital Gains Tax returns and a three month sentence was imposed but was suspended on condition that 180 hours community service was served. The individual was also fined €5,000.

The status at July 2005 of the 66 tax cases on hands at the end of 2004 is

- 34 are still under investigation
- 13 have been submitted to the DPP
- The DPP has issued directions to prosecute in 4 cases
- Bench warrants have been issued in 2 cases
- 5 cases are before the court
- Convictions have been obtained in 6 cases and a guilty plea has been entered in 1 further case
- 1 case has been closed.

In addition to prosecutions for serious tax offences, there were 91 convictions for Customs and Excise and Vehicle Registration Tax offences including tobacco smuggling and customs frauds involving counterfeit spirits. Custodial sentences were imposed in 7 of these cases. There were also 180 convictions for unlicensed trading and 149 for marked oil offences.

2.6 Special Investigations

Table 9 sets out the payments made to the end of July 2005 in relation to cases being examined as part of the Revenue Special Investigations. A short summary of progress to date in the investigations follows.

Table 9 Payments arising from Special Investigations

Investigation	Cases Involved	Payments to Date
DIRT — Look Back Audits (financial institutions)	37	€225m
DIRT — Underlying Tax		
Voluntary Disclosure Scheme	3,675	€227m
Post Voluntary Disclosure Investigations	c. 8,300	€362m
NIB	465	€55m
Ansbacher	289	€51m
Pick Me Up Schemes	71	€0.7m
Mahon Tribunal	27	€28m
Moriarty Tribunal	18	€8m
Offshore Assets	c.13,200	€754m
Undisclosed Funds – Life Assurance Products	c.4,600	€329m
Total		**€2,039.7m**

Underlying Tax on Bogus Non-Resident Accounts

A total of 3,675[1] taxpayers paid €227m[1] under the Voluntary Disclose and Pay Scheme whereby the underlying tax relating to funds deposited in bogus non-resident accounts was required to be paid by 15 November 2001. I referred in my 2003 Report to Revenue's liability reviews of a sample of cases. 37 of the 268 liability reviews have still to be completed. The total yield from the 231 liability reviews completed is €4.3m. 17 cases have been deemed ineligible and 8 of these have paid additional amounts of €0.8m. The remaining ineligible cases are at various stages of investigation.

Revenue obtained information on taxpayers who held bogus non-resident accounts but who did not avail of the Voluntary Disclose and Pay Scheme from financial institutions on foot of High Court orders under Section 908 of the Taxes Consolidation Act, 1997. At July 2005, payments of €362m had been received from such taxpayers.

Offshore Investments via National Irish Bank

In 2005, investigations began into an additional 13 cases that invested in an offshore investment scheme operated by National Irish Bank to bring the total number of cases involved to 465. Investigations have concluded in 416 of the cases. 299 cases have settled with total liabilities of €48.2m and 117 cases had no liability. Investigations are continuing in the remaining 49 cases and payments on account of €4.2m have been received from 16 of these. NIB has paid €2.4m in respect of Capital Gains Tax on compensation it paid to certain investors.

[1] 3,675 taxpayers paid €227m by the deadline of 15 November 2001. In total, 3,754 taxpayers availed of the Scheme and paid €232m.

Ansbacher Investigation

Cases directly involving Ansbacher type arrangements as well as other cases involving offshore funds and deposits are being investigated. There are 289 cases comprising 179 cases on the High Court Inspectors' Report and 110 similar cases discovered by Revenue or listed in the Authorised Officer's Report.

High Court orders have been used to gain access to books, records and other documentation relevant to the investigation. The High Court granted access to documents and information obtained by the Inspectors in relation to Ansbacher clients and persons who failed to co-operate with the Inspectors and Revenue has applied for such access in a number of cases.

136 cases have been settled to date, 71 of which had total liabilities of €42.3m, including a settlement of €7.5m with a Cayman Islands based bank. The other 65 cases settled had no liability and include 43 non-resident cases covered by the provisions of Double Taxation Agreements as well as 4 cases covered by the 1993 Amnesty provisions. In addition, payments on account of €8.7m have been received in 29 of the 153 on-going cases.

Pick-Me-Up Schemes

Pick-Me-Up Schemes involved expenses for goods or services incurred by a political party being invoiced by the supplier to another trader who paid the supplier as a means of supporting the party. Such payments were not deductible for tax purposes, the VAT was not reclaimable and the invoices issued were not in accordance with legal requirements. The investigation found a total of 71 cases that apparently avoided tax by engaging in 'picking up' expenses which were proper to political parties. 42 cases have been settled for a total of €470,724 including interest and penalties. Revenue has decided not to settle 15 cases that have been mentioned at the Mahon and Moriarty Tribunals until those bodies have reported. €158,157 has been received on account from 6 of those cases. 14 cases are still under investigation some of which relate to payments in the 1980s or early 1990s and for which records are no longer available. As a result it is proving difficult to confirm liability. Payments on account of €90,340 have been received in 5 of these cases. These figures have not changed in the last two years.

Tribunals

Matters disclosed at the Moriarty and Mahon Tribunals that suggest that tax evasion may have occurred are being investigated as they come to notice. Currently, 18 cases are being investigated as a result of the Moriarty Tribunal and two have been settled for a total of €6.3m. Payments on account of €1.4m have also been received. 27 cases are being investigated as a result of the Mahon Tribunal. None of these cases have been settled but payments on account of €28.5m have been received in 14 cases.

Offshore Assets

In 2001 Revenue established an Offshore Assets Group to examine the tax status of assets held offshore by Irish residents. Following inquiries into taxpayers who invested funds in offshore subsidiaries of two Irish financial institutions, Revenue announced in February 2004 the commencement of an investigation into unpaid tax on funds in offshore accounts and investments. Account holders were encouraged to give Revenue notice of their intention to make a qualifying disclosure by 29 March 2004. They were then required to submit a statement of disclosure and any payment due by 28 May 2004 (subsequently extended to 10 June). The benefits to account holders of meeting these deadlines were mitigation of penalties, settlement details would not be published and there would be no investigation with a view to prosecution. Revenue intend to seek High Court orders to identify those who have not made a voluntary disclosure and

one order has been obtained. A total of €754m has been received to the end of July from some 13,200 cases as a result of the work of the Offshore Assets Group.

Undisclosed Funds – Life Assurance Products

Investigations began in 2004 into the use of single premium life assurance products to hide income or gains not previously disclosed for tax purposes. The first stage of the investigation involved a deadline of 23 May 2005 for taxpayers who invested undeclared funds in life assurance products to give notice to Revenue of their intention to make a voluntary disclosure. The disclosure scheme does not apply to anyone currently under investigation and the benefits to taxpayers of availing of the scheme are that

- the disclosure will be treated as a voluntary disclosure and therefore, settlement details will not be published
- Revenue will not initiate a prosecution
- penalties will be mitigated in accordance with the Code of Practice for Revenue Auditors

Some 10,000 such notifications were received and these had until 22 July 2005 to pay their outstanding liabilities. Payments of €329m had been received by the end of July 2005 from some 4,600 cases. The second stage of the investigation will identify taxpayers who have not availed of this voluntary disclosure scheme and Revenue will use the powers obtained in the Finance Act, 2005 (section 140) to inspect information held by life assurance companies to assist in making an application for a High Court order.

2.7 Special Savings Incentive Account Scheme

Introduction

The Special Savings Incentive Accounts (SSIA) Scheme was introduced by the Finance Act, 2001, to encourage individuals to provide for the future by saving regularly. The essence of the scheme was that the Exchequer would effectively pay a tax-free bonus of 25% on amounts saved monthly by individuals over a five-year period. The estimated annual full year Exchequer cost of £100m (€127m) indicated a tentative estimate for annual subscriptions of £400m (€508m). It was considered that the scheme would also help reduce inflation by taking money out of the economy but the gross amount (€635m p.a. – subscriptions and Exchequer contribution) was considered too small to have any measurable effect.

Administration of the Scheme

The administration of the SSIA Scheme was provided for under the Special Savings Incentive Accounts Regulations, 2001 (S.I. No. 176 of 2001). In essence, the Regulations required the financial institutions to operate and ensure compliance with all of the terms of the Scheme. Revenue were given a policing role that included the power to audit financial institutions' compliance with the Scheme. The main features of the Scheme are

- The Scheme commenced on 1 May 2001 with the first subscription to an account to be made before 30 April 2002. The Exchequer contributes a tax credit equal to 25% of the amounts saved each month for 60 months. The maximum savings permitted in a month are €254 per account and a minimum of €12.50 was required to be saved in each of the first 12 months.
- Only individuals over 18 years of age and resident for tax purposes could open an account. An account holder must remain resident or ordinarily resident throughout the period the account is held. Each individual is allowed only one account and is required to produce evidence of their PPS number to the account manager and complete a declaration when opening the account.
- Each account must be funded from the account holder's own resources (except in the case of married couples) and sums cannot be borrowed or repayments of borrowings deferred in order to fund savings to the account.
- SSIA accounts are managed by Qualifying Savings Managers (financial institutions) which are required to register with Revenue. There are 330 financial institutions registered consisting of banks (9), building societies (3), credit unions (302), insurance companies (15) and the Post Office Savings Bank. Funds in SSIA accounts can be invested by financial institutions in deposits, shares, government securities or life assurance products. Individuals can transfer accounts from one financial institution to another. On maturity[2], tax at the rate of 23% is deducted from the income or gain arising from the investment of the funds in the account i.e. tax is applied to the difference between the total value of the account on maturity less the total subscriptions and tax credits that were lodged to the account. However, if there is a withdrawal at any time before the account matures, tax at 23% is deducted from the full amount of the withdrawal i.e. the subscriptions and tax credits as well as any income or gain.
- Revenue makes monthly payments to financial institutions based on claims from them for the net amount due i.e. the tax credit due less tax on gains. Financial institutions must make annual returns by 28 February giving details of all SSIAs.

[2] An account matures if it runs its full 5 year term or if the account holder dies

Outturn of the Scheme to date

Total subscriptions to 31 March 2005 amounted to €7.26 billion and the net amount claimed from Revenue to that date was €1.776 billion. Details are shown in Table 10.

Table 10 Accounts, Subscriptions and Tax Credits

	No. of Accounts	Total Subscriptions	Net Amount Claimed from Revenue[a]
2001	398,214	€356,565,983	€88,790,617
2002	1,143,418	€1,859,321,585	€459,664,728
2003	1,113,880	€2,187,421,507	€532,623,415
2004	1,094,294	€2,264,832,004	€550,244,518
2005 (to March)	[b]	€591,814,025	€144,605,547
Total		**€7,259,955,104**	**€1,775,928,825**[c]

[a] The financial institutions receive the tax credit one month in arrears.
[b] Not available until 2005 Annual Return submitted.
[c] Total tax credits claimed were €1,815,533,212 less total tax on gains of €39,604,387.

Statistical data compiled by Revenue (Table 11) shows the distribution of income levels for SSIA holders for the years 2002 to 2004. That distribution closely reflects the overall distribution of taxpayers' incomes as reported by Revenue[3].

Table 11 Distribution of Income Levels for SSIA Holders 2002 to 2004

Income Category	Income Range (2002 levels)	% of account holders 2004	% of account holders 2003	% of account holders 2002
Low	<€20,000	27.7%	28.1%	28.8%
Medium	€20,000-€50,000	49.1%	49.0%	48.8%
High	>€50,000	23.2%	22.9%	22.4%

Scheme Issues

In light of the unexpected extent of the uptake of the Scheme, I sought the views of the Accounting Officer of the Department of Finance on

- the original estimate of the cost to the Exchequer
- the factors supporting the setting of the Exchequer inducement of 25%
- the extent to which existing savings were switched into SSIAs
- the impact of the Scheme on inflation.

Given the benefit conferred on the financial institutions by the scale of the response to the Scheme, I also asked if any consideration had been given to seeking contributions towards the cost of the Scheme from them.

[3] Revenue Statistical Report 2003, Table IDS1

The Accounting Officer of the Department of Finance pointed out that the Government, on the recommendation of the Minister for Finance, decided to introduce the Special Savings Incentive Scheme to encourage individuals to provide for the future by a regular pattern of savings and as a means of taking demand out of the economy. The Minister provided a tentative estimate to the Dáil and Seanad of an Exchequer cost of €127m per annum indicating a level of savings of over €500m per annum. The Accounting Officer stated that these figures were not targets for the amount of savings the Scheme might attract and that the Minister made it clear during the Dáil and Seanad debates that he would be happy to see the Scheme maximised resulting in significantly more savings and therefore a greater cost. He also informed me that there is no target level for retention of savings as such.

The Accounting Officer explained that the Scheme arose out of consideration by the Minister and the Department early in 2001 of various suggestions for tax relief to encourage consumers to save rather than spend. The basis of the 25% Exchequer contribution to amounts saved was simply the 20% standard rate income tax relief expressed in terms of the net cost of the contribution i.e. tax relief at the standard rate on the grossed up amount of the contribution. The contribution was conceived in this way, as a bonus via the financial institutions, largely to keep administration costs down.

In relation to switching of savings, the Accounting Officer said that the Scheme was designed in as much as possible to reduce switching but it was clearly understood when the decision was being made that such switching could not be ruled out. However, the evidence from the annual returns to Revenue from the SSIA providers indicates that the scheme was successful in attracting a significant number of younger savers and people on lower incomes.

As regards the effect of the scheme on inflation, he said that the position is that in general terms, goods price inflation in Ireland is determined by international prices and exchange rate changes while services sector inflation is largely determined by the strength of domestic demand, the amount of slack in the labour market (i.e. wage pressures) and the level of competition across the different services sectors. Therefore, it is reasonable to expect that reducing domestic demand has a favourable impact on services sector inflation and therefore on the overall level of consumer price inflation. It is extremely difficult to isolate the impact of this factor from other factors driving inflation at the time. The gap between Irish and Euro area inflation has by now been effectively eliminated but clearly there were many other factors at work here. It is important to note however that economic theory strongly suggests that relationships in this area are not stable over time.

As for the likely impact of the scheme on inflation when funds are released, this will depend on a series of factors including the level of retention of savings, the amount of the remainder spent or invested, whether spending will be on domestic output (e.g. services) and assets or on imports, (e.g. cars, foreign holidays or foreign assets), the amount of slack in the economy when the money is spent and the extent to which the savings habit fostered by the scheme is persisted with. Estimates vary widely as to the influence of these factors. Information on intentions to spend or save is of necessity based on surveys and the output from these are very difficult to assess. What the money will be spent on is difficult to gauge. There is little or no previous experience in the economic literature to go on and in any event decisions are likely to be strongly influenced by the economic environment at that time. He said that the Department of Finance approach is to develop a range of scenarios and factor these into their current economic forecasts and accompanying variability analysis.

The Accounting Officer stated that the decision to introduce the scheme was a policy decision, taken for the stated reasons and that no contribution was ever envisaged from financial institutions. He noted that interest rate competition between institutions seeking to attract investors to the SSIA scheme provided some very competitive rates of interest (in addition to the 25% bonus) for those who shopped around between institutions.

Control of the Scheme by Revenue

Revenue operate direct control over the Scheme through processing and approval of claims for monthly payments from financial institutions as well as validation and reconciliation of annual returns. Responsibility for ensuring individual savers comply with the terms of the Scheme has to a large extent been entrusted to the financial institutions. Revenue carry out inspection visits to financial institutions to monitor their operation of controls in this regard and to ensure that the financial institutions themselves are in accord with the terms of the Scheme. My staff reviewed Revenue's checks on the Scheme with generally satisfactory results. In response, the Accounting Officer of Revenue informed me that

- there were no instances of invalid monthly claims from financial institutions
- discrepancies mainly relating to PPS numbers and dates of birth arising from the validation of annual returns were followed up and have either been resolved or will be before the end of 2005
- a programme of inspections in the financial institutions shows that they have fulfilled their administrative responsibilities adequately
- some 700 cases were reported for non-compliance and 450 cases have been disqualified since the Scheme commenced.

In response to my query as to whether Revenue has established the number of instances where payments are being made by Revenue under the SSIA Scheme in respect of individuals who owe money to Revenue, have had outstanding taxes written off or have not submitted tax returns due, the Accounting Officer for Revenue stated that while tax compliance as such is not one of the conditions attaching to the SSIA Scheme, Revenue's approach to non compliance is to identify the non compliant at an early stage and casework the case as appropriate. This may include enforcement or indeed attachment. It is Revenue policy that where appropriate, all suitable creditors will be examined for the purposes of attachment, including SSIA accounts. This approach has been successfully used in the recent past. He pointed out that SSIA account holders must be individuals, the majority of whom are PAYE employees and as such would not generally feature on the Revenue non-compliant listings.

2.8 Relevant Contracts Tax

Background

The Relevant Contracts Tax (RCT) tax deduction system was introduced in 1970 to counter tax avoidance in sub contracting in the construction industry and was subsequently extended to forestry and meat processing operations. The number of contractors and sub contractors engaged in these industries is set out in Table 12.

Table 12 Contractors and Sub Contractors in Construction, Forestry and Meat Processing Industries

	2000	2005
Principal Contractors	22,000	33,801
Registered Sub Contractors (C2 Holders)	27,000	40,329
Unregistered Sub Contractors	36,000	56,580

For 2005, 18,640 contractors act as principals and registered sub-contractors and are included in both categories (11,000 in 2000).

RCT only applies where the principal contractor and the sub contractor operate in the same industry. A principal contractor must establish, for each job, whether a worker is a sub contractor or an employee. It is not always obvious whether an individual is employed or self employed and there is no absolute definition covering all cases. The category a person falls into depends on what they actually do, the way they do it and the terms and conditions under which they are engaged.

Under the RCT system, a principal contractor must deduct tax at 35% from payments to sub contractors unless the principal has a relevant payments card issued by Revenue for that sub contractor. Where a principal has a relevant payments card for a sub contractor, payments are made without deduction of RCT and recorded on the payments card. Relevant payments cards are only issued by Revenue in respect of sub contractors who hold certificates of authorisation (C2s). C2s are issued by Revenue to sub contractors on application provided their tax affairs are in order and the applicant is deemed to be a bona fide sub contractor. Where RCT is deducted from a payment, the principal gives the sub contractor a deduction certificate showing the gross amount of the payment and the tax deducted. After the end of the month in which the payment is made, the sub contractor can submit the deduction certificate to Revenue and claim repayment or offset of the RCT deducted.

Principal contractors must maintain a record of payments to all sub contractors and submit monthly returns (RCT30) together with remittance of the tax deducted. An annual return (RCT35) must also be made showing the total payments to each sub contractor (paid with and without deduction of RCT) and the total RCT deducted (if any) from each. The amount of RCT collected and repaid for the years 2001 to 2004 is shown in Table 13.

Table 13 RCT Collected and Repaid or Offset 2001 to 2004

	2001 €m	2002 €m	2003 €m	2004 €m	Total €m
Collected	422	394	477	612	1,905
Repaid/Offset	365	365	403	522	1,655
Not Allocated	57	29	74	90	250

Changes Introduced Since 2000

Since my 2000 Report on the systems and procedures for administration of RCT several operational changes have been introduced.

- RCT has been incorporated into Revenue's Integrated Taxation Services (ITS) system.
- RCT was introduced into Revenue's Active Intervention Management (AIM) caseworking collection system in a limited way in 2002 thus allowing monitoring of the larger principal contractors. RCT has recently been fully integrated into the AIM caseworking system.
- Monetary limits can now be applied to payments cards issued. For payments over that amount, RCT must be deducted or a new payments card applied for.
- The Finance Act 2004 empowers Revenue to maintain a register of principal contractors.
- A risk evaluation of RCT has recently been carried out by Revenue.

I sought the observations of the Accounting Officer on the extent to which the changes introduced have addressed the issues identified in my 2000 Report and in particular

- the progress made in pursuing the €38m - €44m arrears of RCT highlighted in my 2000 Report
- when electronic processing of the annual return data is likely to be implemented and the benefits it will give to the administration of the tax
- when the recommendations of the risk report will be available for consideration and implementation
- whether it is intended to seek a legislative basis for the payment card monetary limit.

The Accounting Officer stated that in recognition of the potential risk associated with RCT, Revenue had committed a large proportion of its information technology resources to incorporating the tax into the ITS system. This necessitated assigning a higher priority to RCT than the development of the PAYE system for employees. He said that this decision was taken on the basis that it was necessary to move RCT into ITS before the administrative problems identified could be properly addressed. Its inclusion in ITS means that a full audit trail of all RCT processing activity is now available. Further benefits are system checking

- of the tax compliance of sub contractors prior to C2 issue
- that contracts limits are not exceeded prior to Payments Card issue
- of deduction certificates and tax compliance status of sub contractors claiming refunds or offsets. ITS automatically offsets refund claims against outstanding taxes.
- for principals who are not up to date with returns and payments when sub contractors claim refunds or offsets
- of cumulative monthly payments by a principal against total deductions from sub contractors per annual return and issue of estimate as necessary.

Revenue's recent restructuring has included the establishment of Special Compliance Districts in each of the Revenue Regions. These Districts have commenced a number of projects and initiatives with a particular focus on the construction industry and major infrastructural projects which have produced information and intelligence that has increased Revenue's understanding of the RCT sector as well as identifying and profiling cases that present risks. The intelligence from such projects provides a base from which Revenue can evaluate the effectiveness of its current programmes and develop new strategies on how to tackle fraud and evasion. These developments coupled with the introduction of a new computerised risk assessment system will facilitate the development of new policies and compliance programmes to actively pursue appropriate cases. He regards these measures as a significant step towards ensuring the efficient administration of RCT, the identification of compliance risks and addressing any weaknesses in RCT administration.

In relation to the cases with arrears of €38m to €44m, the Accounting Officer stated that when RCT was introduced into ITS in November 2002, all balances for the years 2000/2001 and later were included in ITS. Balances for prior years were not automatically transferred to ITS due to the uncertainty of the charges under the old system. Where the older charges were confirmed as valid, they were manually input to ITS for full collection case working. The majority of cases have been examined at this stage and where necessary, the liabilities have been included in ITS. Some of the cases have to be rechecked to confirm the status of the charges. This requires access to files stored "off site" and it is taking some time to retrieve the files and confirm the position. Examination of all cases is expected to be completed by the autumn.

The Accounting Officer also informed me that the facility to capture the data on the annual returns is currently being developed and is scheduled for completion in December 2005. Annual returns for 2004 and subsequent years will be processed. He stated that the capture of this data will allow Revenue to

- Match data already being captured from refund/offset claims with the principal's returns.
- Check the validity of payment card numbers quoted.
- Identify subcontractors who are not reclaiming RCT deducted.
- Identify patterns where principal contractors engage uncertified subcontractors only (increased cash flow), C2 holders only (less administration) and subcontractors who do not provide a tax reference number (possible shadow economy issues).
- Identify principal contractors where compliance with RCT legislation and regulations may be an issue (payments card numbers not quoted and no tax deducted, payments card number quoted not issued to that principal).
- Use the annual return data in the risk assessment system to profile cases where tax might be at risk across all taxheads.

The Accounting Officer also stated that Revenue was in discussions with the Department of Social and Family Affairs as to the extent of information they would require from the annual returns to assist in identifying instances of sub contractors working while claiming social welfare benefits.

The Accounting Officer said that Revenue management have not yet considered the report of the risk evaluation of RCT which has just recently been completed. Some of its proposals and developments could be introduced quickly while others will require information technology developments.

The Accounting Officer informed me that the monetary limit on payments cards was introduced on an administrative basis in 2004 under the care and management provisions of the Taxes Consolidation Act, 1997. It was introduced to reduce some of the risks associated with the tax including cases where sub contractors who held C2s on the basis of a small contract were being used to channel significant payments to large operators in the shadow economy who would not have met the criteria to obtain a C2. The limit also provides a degree of protection to Revenue against the possibility of small, labour only contractors building up significant tax debts. Revenue consider that the monetary limit is a pragmatic response to these risks and is appropriate and desirable in the long term and is therefore best placed on a statutory footing. Revenue are considering this and other changes required to the RCT legislation with a view to putting forward proposals to the Department of Finance for consideration for inclusion in the Finance Bill, 2006.

Current Audit Issues

In the light of the findings of my previous audit and the changes introduced since, I examined the operation of RCT in the Fingal District, the Cavan/Monaghan District and the Construction Business Unit of the Large Cases Division. The system operated in each of these was examined. Sample checks were made of principal contractors and their annual returns, the validity of payments cards and tax reference numbers supplied on annual returns and the compliance record of sub contractors listed on the annual returns. In addition, a sample of Revenue audits in the construction sector was examined and internal audit activity in the RCT area was reviewed. The findings of my audit together with the responses of the Accounting Officer are set out below.

Submission of Annual Returns by Principal Contractors

32 of 65 annual returns examined were submitted from 1 to 10 months after the due date. A penalty for late submission was not imposed in any case.

The Accounting Officer stated that based on the experience of the use of penalty proceedings in relation to other taxheads, Revenue are of the view that the automatic taking of penalty proceedings alone for late submission of returns will not be effective in changing the compliance behaviour in RCT cases. Since Revenue restructuring, a more whole case approach to tackling non-compliers is being followed. This means that instead of dealing with individual instances of non compliance (such as the failure to file a particular tax return) in isolation, account is taken of the total risks across all taxheads. Decisions on the type of action to be taken are made based on what is considered to be the most appropriate intervention to change the behaviour of the taxpayer. The introduction of the computerised risk assessment system will greatly facilitate this new approach. It may be that in some cases, penalty proceedings will be the most appropriate action to take. However, this new approach is at an early stage.

Completion of Annual Returns

- 8 of the 65 annual returns included entries for 38 sub contractors without a payments card number but no RCT was recorded as deducted.
- Entries on annual returns for 3 sub contractors showed negative amounts.
- There were some 6,533 sub contractors on the annual returns examined. Tax reference numbers were not supplied for 457 of these.
- Addresses were not provided in all cases.

The Accounting Officer informed me that it is Revenue policy that annual returns are examined to check for deficiencies but due to pressure of other work programmes some were not fully examined. Where problems are identified, cases are considered for audit as part of a District's annual audit programme and the decision to initiate an audit will take into account factors such as the degree of the deficiency (the tax at risk), the tax history of the case and resources. Where a decision is made not to proceed with a formal audit other options and contacts need to be considered. To ensure that there is consistency in RCT administration across all Regions, Revenue proposes to issue comprehensive instructions on the best practice to be applied in working annual returns. The instructions will also address other issues such as the quality of information provided on RCT return forms.

In relation to cases where no payments card number was quoted but no tax was deducted he said it may be the case that the principal omitted the number from the annual return in error. Where this is not the case, the matter is generally referred for audit. Where the audit shows that tax should have been deducted payment is required unless, in exceptional circumstances, where there is no neglect, all parties are fully compliant and nothing would be gained by processing a payment through the system. Also, payment is not required in group cases, as provided by the Code of Practice for Revenue Audit, where the group is compliant.

Enquiries into the cases where there were negative amounts on the annual return show that the principals' own internal systems led to these amounts being recorded on the RCT 35s. Any tax implications arising are being followed up.

In relation to the absence of tax reference numbers on the annual return, he said that as the return may be submitted a year or more after the subcontractor was engaged, possibly on a short term contract, a difficulty arises in that the principal contractor may not have the means of getting this information. The subcontractor must however provide their date of birth in all cases. The address should also be supplied in all cases, but in practice it is often omitted where the subcontractor has provided a tax reference number or has a C2 certificate. In any event the subcontractor's address is available on Revenue's computer records.

He stated that the electronic capture of annual return data will automate the detection of discrepancies but that until that process is complete, processing of forms would be extremely costly in terms of resources and has to be assessed in terms of the benefit to be gained and the opportunity costs involved. Revenue has other strategies in place to detect non-compliance and tax at risk with new dedicated teams in its restructured organisation. The work of the Special Compliance Districts means that those who are not in the tax system are now being detected on a current basis and not after the fact when an annual return form has been submitted and the subcontractor cannot be traced.

Sub Contractors' Tax Reference/Registration Status

The validity of the reference details and the tax registration status of a sample of sub contractors recorded on the principals' annual returns were checked as part of my audit. In most cases the outcome was satisfactory but there were difficulties with some cases which I raised with the Accounting Officer.

The Accounting Officer stated that in light of the large amount of information relating to subcontractors on annual returns, coupled with the practical difficulty of interrogating this data outside of a management information system, no specific check has been carried out to date on the validity of tax reference numbers. However, this difficulty will be addressed by the electronic data capture of information on annual returns. The approach to using this development to ensure that taxpayers who supply inaccurate data can be detected is being examined.

Comprehensive instructions issued in October 2004 to all staff outlining procedures in the registration process with the main emphasis on the ongoing maintenance and accuracy of taxpayers' data. The instructions address the question of registration for other taxes by directing that where staff processing registration applications consider that the taxpayer should be registered for other taxes, the taxpayer or their agent should be contacted. In relation to unregistered subcontractors, the Accounting Officer said that such taxpayers generally apply to Revenue for a tax refund. When processing the refund, checks are made to ensure the subcontractor is registered for all relevant taxes and compliance checks are made where this is not the case. These compliance checks have resulted in the detection of taxpayers who do not submit tax returns or who underpay their liabilities. Procedures are also in place to ensure that non-resident sub-contractors are registered for all appropriate taxes.

Employee/Sub Contractor Status

My examination reviewed files relating to Revenue audits in the construction industry finalised in 2004 with particular reference to the classification of workers as between employees and sub contractors and found some evidence of principal contractors being advised by Revenue auditors to reclassify sub contractors as employees. In 1998, a programme of site visits to principal contractors had been undertaken to check whether any persons treated as sub contractors should be reclassified as employees. The status of some 63,000 sub contractors was examined and as a result some 20% were reclassified as employees. A similar special programme commenced in 2001.

I sought the observations of the Accounting Officer as to

- whether he was satisfied with the level of checking of the classification of workers as between employees and sub contractors
- whether the special programme of site visits commenced in 2001 was completed or is planned to be completed
- the extent of the contribution of work of the Joint Investigation Units[4] to the control of RCT, including the classification issue.

The Accounting Officer stated that Revenue have responsibility for administering the operation of all taxes in the construction industry and ensuring that all operators within that sector comply with all their taxation obligations, and not just RCT. Revenue carry out a range of checks in relation to the status of those engaged in the construction sector and also monitor activity in the sector through the issue and processing of RCT forms. He said that Revenue auditors examine the employee/sub-contractor status as a routine part of audits. Approximately 1,500 audits (about 10% of all audits) were conducted on building contractors in 2004. The auditors would have examined the forms that a principal contractor and a sub-contractor complete in respect of each contract (RCT1) which contain details of the duration and type of contracts and a statement that the contracts are not contracts of employment. He pointed out that recent computer enhancements make it easier to identify cases where an employment arrangement rather than a contract arrangement may exist e.g. where sub-contractors are receiving regular payments under deduction of tax from one principal contractor.

The Accounting Officer informed me that in 2004, Special Compliance Districts initiated a number of key projects to tackle tax evasion and in the construction sector concentrated on major infrastructure projects. Surveillance of construction sites allowed Revenue to develop a profile of those engaged on sites and to

[4] Revenue and the Department of Social and Family Affairs carry out joint investigations through Joint Investigation Units which are staffed by officials from both departments.

use this information to carry out site visits where risks were identified. These site visits have led to cases being referred for possible prosecution and informed the selection of cases for future audits. Investigations into the construction and property development sectors focusing on all taxes and duties are continuing in 2005.

The special programme of site visits, which commenced in 2001, was suspended in September 2002 to allow Revenue to provide audit staff with Health and Safety training to enable them to move around the sites. The programme was not resumed following an analysis of the degree of misclassification uncovered (of the 984 subcontractors examined only 65, i.e. 7% were misclassified). However, officials who are engaged on construction site visits have now been provided with the recognised training courses to enable them to move around the sites.

The Accounting Officer informed me that the focus of the Joint Investigation Units crosses all taxheads and all areas of business activity. While no specific RCT projects were undertaken, the Joint Investigation Units have regularly examined taxpayers operating in the construction, forestry and meat industries and have dealt with RCT compliance and classification issues as they arose. Their compliance interventions also focus on other tax heads and duties including the operation of PAYE, VAT and Income Tax. No separate statistics are kept of RCT classification issues as the classification issue has not presented itself as a significant risk and the main focus of these Units is on areas where persons are working and claiming social welfare allowances.

Internal Audit

The Revenue Internal Audit Section examined RCT repayments and offsets to sub-contractors and refunds to principals who had overpaid RCT in June 2004 as part of a general audit of repayments. A sample of 55 repayments and offsets to sub contractors were examined with satisfactory results. Since the introduction of RCT into the ITS system, the volume of refunds to principals had increased dramatically from an annual level of about 30 to about 4,000 per annum. Previously, the principal had to apply to have the amount refunded or included in the balancing of the annual return. In the ITS system a refund is automatically triggered for all taxes where the amount received is greater than the charge on record. The Internal Audit found one case where refunds were incorrectly made to a principal as a result of a supplementary payment of RCT, correctly due, being treated by the ITS system as an overpayment, and automatically refunded. In light of the identification of that problem, the Collector General's Office temporarily suspended the automatic refund facility for RCT. A subsequent review found 399 cases where improper refunds totalling €912,000 had been made. All refunds to principals greater than €10 are now blocked by the system and must be manually processed. 388 of the cases found have been resolved and the moneys recovered, and 11 cases, which received refunds totalling €14,000, are still to be resolved.

I asked the Accounting Officer whether he was satisfied that incorrect repayment had not occurred in respect of any other taxhead in ITS.

The Accounting Officer stated that he was satisfied that the issues that resulted in incorrect automatic repayments of RCT were generally related to the migration of RCT to the new ITS environment. Steps have been taken to specifically address the issues identified in relation to RCT and additional validation procedures have been implemented. In relation to taxheads other than RCT, situations where taxpayers do not use the returns provided or do not clearly indicate the circumstances of the payment give rise to some potential for incorrect repayments. The validation systems in place and the maturity of the other taxheads within the ITS environment provide assurance that similar issues to those identified in relation to RCT are not a significant concern.

General Management

In relation to management of RCT generally, I also asked the Accounting Officer

- what action was planned to improve the compliance rates for monthly and annual RCT returns
- the extent of frauds in relation to RCT and the action taken in response
- whether he was satisfied with the operation, control and administration of RCT and that it is achieving its objectives.

The Accounting Officer informed me that it has only proved possible to accurately and reliably compute compliance for the monthly return commencing in January 2005. The compliance rate within one month of the due date is 52%. The Accounting Officer informed me that compliance rates for monthly returns are currently significantly below PAYE/PRSI (P30) compliance rates. This is to be expected, as compliance case working for PAYE/PRSI has been a core element of Revenue's compliance programmes for a number of years. As case working has been extended to include RCT since the beginning of 2005, Revenue anticipates that compliance rates will improve considerably for RCT in the coming years. For 2005, the Collector-General's division has introduced specific compliance targets for RCT in its business plans. The computerised risk analysis system will form a significant part of Revenue's continuing focus on improving compliance behaviour across all taxheads.

Establishing compliance rates for annual returns prior to 2003 has also proven to be unreliable. Since 2003, formal compliance campaigns have been introduced. The compliance rate for the 2003 return at the time of issue of the compliance programme in August 2004 was 60%. This has now risen to 81%. The compliance rate for the 2004 return at the time of issue of the compliance programme in May 2005 was 57%. Matching annual return data processed electronically with sub contractor deduction certificates will help identify principals who have engaged sub contractors but not submitted annual returns.

The Accounting Officer informed me that twelve cases of RCT fraud were investigated by Revenue in recent years. Two cases involved collusion among large numbers of individuals and companies (97 in one case and 24 in the other) including principal contractors and these cases were referred to the Gardaí whose enquiries are ongoing. The remaining ten cases where serious suspected abuse of the RCT system were identified were referred for investigation by Revenue's Investigation and Prosecutions Division (IPD) with a view to prosecution. To date one of these cases has resulted in a Court conviction and the defendant was sentenced to 240 hours of Community Service. In two other cases, the defendants failed to appear in Court and bench warrants were issued for their arrest. The remaining seven cases are under active investigation by IPD.

He said that the main weakness identified in these frauds, was the fraudulent issue by principals of deduction certificates in respect of work never carried out and payments that were never made. The tax shown as deducted on these certificates was bogus and not remitted to Revenue. He said that the functionality of the ITS system allowed Revenue to respond quickly to these fraud cases and identify the deduction certificates that were being used in the fraud. An analysis of the alleged frauds identified six common traits in these cases and a development was introduced to the ITS system to identify potentially bogus claims and principals who were not returning adequate amounts of RCT deducted. A risk evaluation was carried out to make recommendations to counter such frauds.

In relation to the operation of RCT generally, the Accounting Officer stated that the serious compliance problems that RCT was introduced to tackle still exist today and are compounded by the highly

competitive nature of the industry where non-payment of tax debts is seen by some as a way to gain a competitive advantage. He said that Revenue faced new challenges arising from the increased level of activity in the construction sector and the increase in the number of non-resident contractors. The difficulties in tackling non-compliance in the construction sector are recognised internationally and different jurisdictions have come up with their own responses to the problem. The main focus and purpose of the RCT system is to secure payment of tax by subcontractors who might not otherwise pay. Most operators in the construction, forestry and meat processing industries are relatively tax compliant in terms of returns and payments. Revenue's compliance programmes monitor the returns and payments made by principal contractors. Registered subcontractors are subjected to a returns and payments compliance regime that annually reviews their entitlement to hold a C2. Unregistered subcontractors suffer a tax deduction of 35% and their compliance is monitored when they apply for a refund or offset of this tax. While the unregistered subcontractor who does not apply for a refund or offset is not being monitored at this point in time, they have suffered a deduction of tax at 35%, which might not otherwise be achievable. With the capture of the data from the annual return, Revenue will be in a better position to analyse and profile these cases and put in place a comprehensive and efficient response.

The Accounting Officer stated that Revenue's new structure has increased its capability to respond more quickly to this complex and changing environment. Initiatives already started by the regions have increased Revenue's understanding of the RCT sector and its risks and these projects will continue. While the RCT system is still mainly paper based, ITS and AIM have streamlined processes and allowed Revenue to monitor compliance more effectively than heretofore. As a result of the tightening up of procedures and the enhancements that have been made to the underlying computer systems, Revenue is satisfied that the RCT system is still achieving the objectives for which it was put in place. He said that the computerised risk analysis system will increase Revenue's effectiveness at tackling non-compliance in the sector.

2.9 Stamp Duty on Electronic Share Transactions

Background

The introduction of a new electronic system (CREST) operated by a UK company for the settlement of transactions arising from the sale or transfer of shares in UK and Irish registered companies was noted in my 1996 Report. Under Section 105 of the Finance Act, 1996, Revenue entered into an agreement with the operating company for the collection and payment to Revenue of Irish stamp duty. Before the CREST system went live Revenue tested a range of individual transactions to ensure that the amount of stamp duty due would be correctly calculated by the system.

Operation of the CREST System

Under the agreement the stamp duty collected is lodged by the operating company to designated bank accounts in trust for Revenue and is transmitted weekly, three weeks in arrears, to the Central Bank. Prior to the transfer of funds a daily breakdown of stamp duty payments collected is forwarded to Revenue by the operating company. The weekly receipt of funds is confirmed to Revenue by the Central Bank. My 1996 report also noted that a direct link with the new system was under development that would download further transaction details to Revenue. That data would facilitate verification that the correct amount of duty was paid over by the operating company, and also facilitate audit procedures. Under the agreement with the operating company Revenue was given the right to undertake a system audit of the company.

In order to participate in the CREST settlement system, brokers are required to become members of the system and put in place guaranteed payment arrangements. The system matches the details input by both parties to a sale and completes the transaction, the respective bank accounts are debited and credited with the agreed amount and, where applicable, the stamp duty liability of 1% is also collected from the account of the purchasing broker. €220m was collected by Revenue through the CREST system in 2004. Table 14 shows the total stamp duty on share transactions for the years 2000 to 2004 and the CREST payments and refunds for each year.

Table 14 Electronic Share Transactions and Stamp Duty 2000 - 2004

Year	Collected through CREST System	CREST Refunds	Paper Based Transactions	Total Stamp Duty on Share Transactions
2000	€212m	€25m	€44m	€231m
2001	€306m	€25m	€65m	€346m
2002	€272m	€32m	€63m	€303m
2003	€250m	€28m	€34m	€256m
2004	€255m	€35m	€40m	€260m

Exemptions and Section 75 Returns

Legislation provides for exemption or relief from stamp duty on share transactions in certain circumstances. The main instances are outlined in Table 15. Closings relief is provided only on a 'pay and refund' basis, while the other three exemptions are obtained on a self-assessment basis by brokers inputting the relevant exemption code to the CREST system. Stamp duty is not deducted by the system from exempt coded transactions. However, data subsequently provided in electronic form by the system

to Revenue includes the unique identifier number of each transaction, date of transaction, whether shares are Irish, broker identity, number and identity of shares, value of transaction, broker self assessment code in relation to exemptions or relief, and the amount of stamp duty assessed and charged by the system.

Table 15 Exemptions/Reliefs under Stamp Duties Consolidation Act, 1999

Exemption/Relief	Criteria	Stamp Duty
Beneficial Ownership did not change	• Broker is acting in an agency capacity • Legal title only is transferred • By Electronic Transfer only	Stamp Duty not payable
Closings Relief	• Broker is acting in an agency capacity • Both contracts due for completion on the same day • Both purchases are closed within 25 days • By Electronic Transfer only	Stamp Duty payable but refundable
Market Maker	• Broker registered by the Stock Exchange to trade in the relevant securities • Electronic and Paper Transfers	Stamp Duty not payable
Broker/Dealer	• Broker acting in a principal capacity • Securities purchased must be sold on within a calendar month • Electronic and paper transfers	Stamp Duty not initially payable, but due if no resale within a calendar month

Member firms that have claimed broker/dealer exemption through the CREST system must submit a report to Revenue on a six monthly basis (Section 75 Report) containing details of the actual outcome of each purchase that had been initially coded as a Section 75 exemption on the expectation of resale within a calendar month and of the amount of duty which may subsequently have become due. A certified declaration is also required from the broker/dealer to the effect that the shares transferred under the Section 75 exemption, and in respect of which stamp duty has not been paid, were transferred on sale to a bona fide purchaser within the permitted period of one calendar month[5]. Refund claims for closings relief must include details of each transaction and a declaration as to why the refund is warranted.

Internal Audit 2001

An internal audit of the payment of Stamp Duty through the CREST system was carried out by the Revenue Internal Audit Section in November 2001. The audit findings noted that

- A number of brokers had not complied with Section 75 return requirements for the previous six monthly period, and had not been pursued by Revenue
- Desk-based audits of Section 75 returns are mainly carried out where errors have been discovered in the course of processing refund applications
- It was not possible to identify all members trading in CREST as the members' identification numbers were not known to Revenue
- No Revenue audit of a CREST participant had been carried out since the system was introduced in 1996.

[5] 'Traditional' paper share transactions deemed exempt by brokers will be accepted unstamped by a Company Registrar. There is no record of subsequent receipt of Section 75 returns by Revenue in such cases.

Current Audit Concerns

It was noted in the course of an audit by my staff in February 2005 that those weaknesses still existed. It was also noted that an unsolicited payment of €1.1m was received by Revenue from a broker in November 2003 in respect of stamp duty on 516 share transactions through the CREST system in the period April 2001 to March 2003. The transactions had been coded exempt by the broker at time of purchase under broker/dealer relief (Section 75) but had not been sold on within the required period of one month of purchase thereby negating the relief and incurring a liability to stamp duty. In October 2004 Revenue informed the broker that a further €3.3m comprising interest of €0.1m and penalties of €3.2m was due to Revenue in respect of the late payment of the stamp duty.

As the €1.1m underpayment underlined the significant risk of underpayment of stamp duty which may arise in relation to exemptions, and as the failure to obtain Section 75 returns and declarations deprived Revenue of a key tool to police compliance in that area, I sought information from the Accounting Officer as to

- whether the systems and procedures operated by Revenue were adequate to ensure that all of the stamp duty due to the Exchequer from transactions on the CREST system was promptly identified and collected
- the circumstances and outcome of the case in which interest and penalties totalling €3.3m had been demanded by Revenue in October 2004
- whether a Revenue stamp duty audit had been carried out on the books and records of any CREST member since 1996 and, if so, the outcome of such audit
- whether Revenue had exercised its right under the 1996 agreement to undertake a system audit of the CREST operating company.

Revenue Response

Adequacy of Systems and Procedures

The Accounting Officer informed me that the operation of CREST had since its introduction in 1996, been the subject of many meetings and correspondence between the Revenue Crest Unit and both the Irish and London Stock Exchanges, individual Member Firms and other interested parties with the objective of educating them in Revenue's requirements for submitting refund claims and returns in relation to stamp duty exemptions. Reclaims sought on the basis of inputting errors by CREST participants had a draining effect on the Revenue resources available to administer the system.

Revenue's approach has been to tackle the deficiencies in reporting through a two-streamed approach – education and compliance leveraging. The relationship-based business model had sought to address the non-compliance in this area and had been successful in assisting brokers in understanding and meeting their obligations. Revenue has also been working to improve audit case selection using business intelligence. A number of meetings to outline compliance issues had been held with the Irish Stock Exchange. A Technical Group consisting of Revenue and Irish Stock Exchange representatives had been established to review difficulties in complying with CREST obligations and it was hoped that this Group would be shortly able to agree a guidelines (Market Norms) document which would outline details of Revenue requirements. Brokers were given an opportunity to get their affairs up to date and had confirmed that there would be full and timely compliance with their obligations from December 2004.

The UK Stamp Duty Reserve Tax exemptions in CREST differ from those in relation to Irish stamp duty and had resulted in confusion for UK brokers in regard to their Irish stamp duty obligations. Having regard to this, there had been a series of discussions and meetings since September 2000 to educate them and to improve the level of compliance and the accuracy of their returns.

The recommendations of the 2001 Internal Audit report had been implemented where considered feasible. It had also been decided that management of the compliance of the CREST activities of the main brokers would be transferred to the Large Cases Division. The transfer would release resources within the Crest Unit to concentrate on the remaining brokers.

The CREST system to date had grown significantly both in terms of the volume of transactions effected and data flows since its inception. For example, the 1996 net stamp duty collected through CREST was €6m (some 12% of the total collected for shares) and in 2004 had risen to €220m (84.5% of the total for shares). Revenue had responded to the increase in the level of business by moving to upgrade its computer system. When implemented, the upgraded system would increase user capability and solve a number of existing performance problems.

The securities market had also evolved over the past few years and that had resulted in a different trading environment from that which obtained at the commencement of CREST. In light of this, the Irish Stock Exchange had approached the Department of Finance with proposals to replace the existing legislative stamp duty exemptions for CREST transactions by a Single Intermediary Relief (the simplified exemption used for UK securities). If such a relief were introduced, it would reduce the present administrative burden both for CREST participants and for Revenue.

Non-Compliance with Broker Reporting Requirements

The Accounting Officer indicated that the main issue of ongoing concern for Revenue had been the failure of brokers to comply with the Section 75 reporting requirements. Due to resource constraints, there had not been a formal procedure in place in Revenue to identify brokers dealing in Irish shares. Additional resources had been allocated to the Crest Unit in the latter half of 2004 to deal with compliance issues. The Business Plan for 2005 included an activity to identify brokers dealing with Irish shares on the CREST system. However, it is difficult to accurately quantify the number of brokers with returns outstanding as the indicator flag used on the CREST system for Section 75 relief is the same as that used for Market Maker relief (see Table 15) for which no return is required. Table 16 sets out the total number of brokers dealing in Irish shares and the outcome of Revenue's exercise to identify the potential number of brokers with returns outstanding for the six monthly periods ending March 2000 to March 2005.

Table 16 Section 75 Returns Outstanding 2000 - 2005

Period ended	Total Number of Brokers Trading in Irish Shares	Potential number of Brokers availing of S.75 Relief	Number of Brokers who submitted six-monthly returns	Potential number of Brokers with returns outstanding
March 2000	191	44	28	16
September 2000	211	51	27	24
March 2001	242	59	23	36
September 2001	235	61	18	43
March 2002	219	76	23	53
September 2002	242	72	12	60
March 2003	220	82	38	44
September 2003	224	87	45	42
March 2004	227	96	46	50

September 2004	238	101	46	55
March 2005	235	104	34	70

In outlining the steps taken by Revenue since 2000 to obtain the outstanding returns together with all stamp duty due, the Accounting Officer reported that where non-compliant brokers were identified, they were advised of their obligations and given the opportunity to bring their affairs up-to-date. Furthermore, where a broker submitted reclaims on foot of the Section 75 exemption, these were withheld if their appropriate returns[6] were outstanding. Those actions had resulted in more brokers becoming compliant and in the collection of outstanding stamp duty where appropriate. The exercise also indicated that as 45%-50% of brokers with a potential obligation to submit a Section 75 return had less than 100 trades exempted in the period, the extent of potential underpayments from these brokers is small. Having analysed the year 2004, only 10 brokers had in excess of 10,000 trades in the six-monthly periods and there were no issues regarding their understanding of their Section 75 obligations.

Reconciliation of CREST Payments Received

The weekly payments notified to Revenue by the operating company are checked against the weekly amounts of stamp duty charged on the CREST computer, and subsequently with the Central Bank confirmation of payments lodged. However, due to the design of the CREST computer system, checks of weekly payments made by the operating company against relevant underlying transactions can only be carried out on behalf of the Crest Unit by expert Revenue computer personnel. Such checks, which were carried out in 2001 and again in early 2005, consisted of examining the data-feed from the operating company to identify the transactions on a specific date, the stamp duty paid on each transaction and the total yield for that date. Crest Unit then compared that data with the payment advice for that date. In the context of the proposed upgrading of the computer system, a request had been made for that facility to be directly available to the Crest Unit users. Differences arising from the checks are rare, with only two instances in the past six months. The previous discrepancy prior to that was in November 2003.

Underpayment of €1.1m

Following a desk-based audit in May 2003, it appeared to Revenue that the firm in question was availing of Section 75 exemption but had failed to submit six monthly returns. The firm was advised that all reclaims would be suspended and was requested to examine the position. After further contacts, a payment of €1.1m was received in November 2003. Outstanding Section 75 returns for the period May 2001 to April 2003 were subsequently submitted in June 2004. The formal Section 75 declaration by the broker was not received but had recently been sought. Revenue assessed interest at €104,809 and penalties at €3,254,940. Following correspondence, the penalties were mitigated to €281,443 in June 2005 in line with Revenue policy and in recognition of the cooperation received from the firm in question as well as the level of neglect involved. There was no mitigation of the interest. A reminder subsequently issued in July 2005 requesting payment of the interest and the mitigated penalty.

Revenue Audit of Brokers

The Accounting Officer stated that the Crest Unit regularly undertook desk-based audits to confirm the bona fides of exemptions claimed. In any case where desk-based audits detected an underpayment of stamp duty, the underpayment was pursued and collected. Regular field visits were made to brokers to discuss record keeping and compliance issues with them. Although an external Revenue CREST audit had not to date been carried out on any brokers participating in the CREST system, the desirability of such audits was identified during 2004. Accordingly, computer based audits of a number of CREST

[6] i.e. covering the 6 month period in which the related transactions occurred.

brokers were planned for later in 2005. A team had now been put together to carry out these audits with the Crest Unit providing the technical expertise in the development of the audit plan and the audit itself being facilitated by officers outside the Crest Unit with the appropriate level of audit and computer skills.

Revenue Audit of CREST System

Arrangements had been made with the operating company to conduct a system audit in London before the end of 2005. The audit will be carried out by the same team including assistance from the Revenue Computer Audit Services Unit. It was anticipated that the results would also be of benefit during audits of individual brokers.

General

In conclusion, the Accounting Officer noted that while the existing systems and procedures in place were not designed to accommodate the level of business presently generated through the CREST system, he was confident that, as with all self-assessed taxes, where underpayments of stamp duty were identified they were pursued and collected. The existing CREST computer system was being upgraded to offer the necessary response to present day demands. It was expected that the features of the upgraded system would in turn require management to adopt new practices and procedures in the manner of identifying and collecting stamp duty. In all, the additional measures currently being taken (including the audit of the operating company and some of the broker members) would increase Revenue's effectiveness in improving compliance.

Chapter 3

Office of Public Works and An Garda Síochána

3.1 Agreement on the Use of Garda Radio Masts

Background

The Government decided, in February 1997, to approve a proposal to permit a mobile telephone company (the company) to install, erect and maintain mobile telephone antennae and ancillary equipment on and adjacent to the radio masts maintained by the Garda Síochána in specified locations subject to certain terms and conditions. A non-exclusive agreement was entered into between the Commissioners of Public Works, the Minister for Justice, the Minister for Finance, the Garda Commissioner and the company in June 1997 to this effect. The agreement was for a period of five years and contained a provision for the company to renew it for a further five years, subject to certain terms and conditions. The company exercised this right in August 2001.

While 459 sites were originally identified, the number of masts utilised since the commencement of the agreement to May 2005 is 185.

Licence Fees

In the agreement sites were categorised as: premises located in the County of Dublin, premises located in other urban areas, and other premises. Different tariffs applied to each category. Provisional rents were specified in the agreement and were payable from February 1997, where applicable. The agreement made provision for the definitive determination of licence fees by an independent arbitrator reporting within 3 months of referral to him. The company was required, within 14 days of the date of execution of the agreement to select an independent arbitrator from a panel nominated by the Office of Public Works (OPW). An arbitrator was appointed in March 1999. The arbitrator, in a report dated July 2002, determined revised rates payable from the agreed valuation date in June 1997.

Arrears of licence fees of €3.6 million, due to the arbitration findings, were received by OPW in February 2003.

I asked the Accounting Officer of OPW what caused the five year delay in finalising the licence fees and if the question of claiming interest on the arrears due to the delay had arisen. In reply he informed me that, in order to prepare the State's case for arbitration, it was necessary to gather comparable evidence and one of the main sources of such evidence was licence agreements that the company had entered into with other landlords. Discovery was agreed in principle in April 1999 but this process was a very long drawn out affair. Due to prolonged negotiations on confidentiality considerations, the need to issue formal Orders of Discovery and the necessity to instruct Counsel, an Oral Hearing did not take place until December 2001. The Arbitrator issued his findings in July 2002. He pointed out that the time scale required by the Arbitrator to consider the evidence and issue his award was a matter entirely for the Arbitrator. He also informed me that the award was effective from the commencement of the Agreement and that there was no provision for the payment of interest on the arrears of licence fees.

Equipment

The agreement required that the company provide the Garda authorities with 300 mobile phone handsets free of charge together with free connection to the company's GSM[7] network. It also provided for connection for a further 150 other GSM handsets already in use by the Gardaí as well as connection of a further 100 handsets for use by the Gardaí.

I asked the Accounting Officer for the Garda Vote how was the need for the quantity of mobile phones acquired, initially and subsequently, assessed - particularly *vis-à-vis* the availability of the Garda radio network. He informed me that there are recognised security issues with the existing Garda analogue radio systems. While the GSM network is not considered to be a replacement for an Emergency Services Network, it does provide an important element of security. This is considered very beneficial to the Garda organisation and is, to some degree, a stop gap measure until the new digital radio system is introduced. Plans for a new radio system were progressing as quickly as possible. The new system would have the requisite level of security and is expected to lead to a considerable reduction in the number of mobile phones required by the Gardaí.

He stated that the telephone services included in the original deal were negotiated as part of the overall agreement. It would appear that, although the Gardaí had a requirement for mobile telephony prior to the agreement, the Gardaí did not pursue it because they had concerns about the means to control the costs of calls. The company's proposal, with the use of a closed user-group and free air time, reduced this risk to a degree.

Call charges

The agreement specifies a detailed scheme of charges that provides a mix of:

- calls totally free of charge
- calls free of charge at certain times
- free SMS[8] communications and
- calls and SMS communications at cost and without profit to the company.

The number of mobile phones in use by the Gardaí has risen substantially due to operational reasons since the agreement was signed. The number of connections has increased from 550 to approximately 1,000. This has allowed the Gardaí to migrate phones on a separate agreement to a more favourable tariff regime.

An internal circular was issued by the Garda authorities in September 1998 on the distribution, care and use of official issue Garda cellular phones. This states, *inter alia,* that phones must be used for official purposes only, that daily usage in excess of €40 is flagged for examination and that Chief Superintendents will be responsible for monitoring and certifying usage. I asked the Accounting Officer if he was satisfied that the level of checking employed by the Garda authorities was commensurate with the risk of use other than for official purposes. He replied that he was satisfied that the control procedures employed by the Garda authorities were in line with the potential risk of usage that fell outside the scope of the official circular. To minimise the risk of unofficial usage, the Garda authorities reviewed the monthly electronic

[7] Global System for Mobile communications
[8] Short Message Service, more commonly known as a text message.

and paper bills. The Gardaí had reviewed the operation of this monitoring system and an official had been assigned the task of reviewing the bills for usage. A monthly report was now sent to each Assistant Commissioner requesting that he satisfy himself that the usage was reasonable. Separately, all calls to premium numbers were blocked.

Net Income

Mobile charges incurred by the Gardaí under the agreement are deducted from the licence fees payable by the company. The licence fees received and the amounts offset in respect of mobile phone charges incurred by An Garda Síochána are set out in Table 17.

Table 17

Year	Licence Fees Received	Offset in respect of Charges[9]	Net Receipts[10]
1997	282,625	-	282,625
1998	579,299	195,683	383,616
1999	1,342,371	422,567	919,804
2000	639,085	567,040	72,045
2001	1,152,350	524,042	628,308
2002	860,746	766,921	93,825
2003	5,855,706[11]	1,374,516	4,481,190
2004	2,040,955	1,119,924	921,031

Certification of costs and inspection of books of account

The company is obliged to supply to OPW, within three months of the end of the calendar year, a statement signed by its auditors certifying that the amounts invoiced for call and other charges have been calculated in accordance with the provisions of the agreement. However, the company failed to submit audit certificates in respect of 2000, 2001 and 2002 until April 2003 following requests from OPW.

The OPW also has the right, upon written notice being supplied to the company, to appoint a representative to examine the books and records of the company for the purposes of verifying that the amounts invoiced to the Garda Síochána have been properly calculated in accordance with the provisions of the agreement. This right was exercised for the first time by OPW in January 2005. I enquired what the results were of the examination of the books and records of the company. I was informed that the results of the inspection were generally satisfactory but that clarification on some discrepancies had been requested and was still awaited.

[9] As certified by the Company's Auditors.
[10] As recorded in the Appropriation Accounts.
[11] Includes arrears of €3.6 million received on foot of the arbitrator's findings.

Chapter 4

Valuation Office

4.1 Shortcomings in Financial Controls

An Accounting Officer is required by law to sign and present for audit an Appropriation Account for each Vote for which he/she is responsible before 1 April of the year following that to which the account relates. It is my responsibility to audit the Accounts and to report on them by 30 September of the same year. The Appropriation Account for the Valuation Office - Vote 15 - for the year ended 31 December 2004 was signed on 31 March 2005 and submitted to me on that date.

Following the commencement of the audit the following deficiencies in the Account were noted:

- Monthly statements from the Paymaster General (PMG), who acts as the Valuation Office's banker, were not reconciled to the Office's accounting records on a regular basis throughout the year. A year end reconciliation had been completed in February 2005 and was presented for audit. However this contained an error of approximately €1.3 million.
- The statement of outstanding payable orders, supplied by the PMG, did not reconcile with the figure for outstanding payable orders in the Appropriation Account.
- The PMG was requested by the Valuation Office to cancel two payable orders, for amounts of €108,210 and €37,284, in July and August 2004 respectively. These instructions were not acted upon by the PMG in 2004 but this was not noticed by the Valuation Office and resulted in a duplicate charge to subhead C of the Vote. The charge to the Vote was therefore overstated by an amount of approximately €145,000 and the surplus to be surrendered understated by an equivalent amount.
- Suspense and deduction accounts are operated by the Office as part of normal financial recordkeeping. However these accounts were not reconciled on a monthly basis and it was noted that some contained unexplained balances going back a number of years.

A corrected Appropriation Account was submitted on 20 July 2005.

In addition to these shortcomings noted in the course of audit, my Office was informed by the Valuation Office in December 2004 that it had been brought to its attention in September 2004 that income from the public office for a week in November 2003 and, subsequently, for a week in January 2004 had not been lodged. While all the cash involved has been recovered, an amount of €2,041 in respect of cheques was still outstanding. The failure in control relating to the prompt lodgment of receipts to the PMG had been identified by the Valuation Office itself and was addressed by the introduction of new procedures and controls. However my audit found that new procedures recommended to, and operated by, the Valuation Office did not reconcile receipts to bank lodgments on a regular basis.

It is important that there are effective and sound financial control systems and procedures in operation in the Valuation Office, as in any organisation, to ensure that the risk of financial loss, because of errors or irregularities, is minimised and that accurate and up to date information is available to management. In this regard the carrying out of reconciliations on a regular and prompt basis and the correct recording of transactions in the financial records is essential. As it was a matter of concern to me that there was a failure by the Valuation Office to ensure that these functions were properly carried out in 2004 I sought the views of the Accounting Officer.

Accounting Officer's Response

The Accounting Officer informed me that the new Management Information Framework financial system went live in the Valuation Office at the start of 2004 thereby introducing many different procedures for staff to follow. While the system had been tested extensively prior to implementation, there was a lot of pressure on staff in the accounts area throughout the year.

He explained that the lapses and failings were due, in the main, to a lack of knowledge by staff as to the correct procedures to be followed. While staff were aware of the error of the amount of €1.3 million in the PMG account they were unaware of the correct procedures to be followed to correct the balance. Neither were staff aware of the necessity to undertake monthly reconciliations. He informed me that the outstanding payable orders difference was due to a financial system interface giving inaccurate information that resulted in the value of payable orders being understated for some months. The software supplier was now taking steps to rectify the problem. The problem relating to the two non-cancelled payable orders was also due to unfamiliarity with correct procedures and resulted in the failure to make the necessary journal entries until 2005. Staff had been unaware of the need to reconcile all accounts, including suspense and deduction accounts, monthly. This was now being done and some old irreconcilable balances identified would be considered for write off in 2005.

He assured me that new procedures and controls had been introduced and were in place to address and correct all the deficiencies and weaknesses noted.

He stated that public office receipts had been the responsibility of one officer only. When it was noticed that lodgments had not been made, the money could not be found and the officer concerned was on maternity leave and could not be contacted. Correct procedures were not in place to ensure that the failure to make a lodgment in a timely manner would be brought to attention. Lodgments were not made on a regular basis, only one person was responsible for money at all stages of the process and checking procedures were inadequate. Accounts staff had attempted to solve the problem themselves rather than bringing the matter to the attention of management. A full investigation had since been carried out which had resulted in disciplinary action being taken. New interim procedures had been introduced but all procedures would be examined by a project group that was being set up to examine the issue and recommend improved procedures. All outstanding cash had now been lodged but a small amount of income represented by cheques was still outstanding pending the submission of re-dated cheques.

Chapter 5

Department of Justice, Equality and Law Reform

5.1 Enforcement of Deportation Orders

Introduction

The Department of Justice, Equality and Law Reform is responsible for implementing Government policy on refugees and asylums seekers. The costs borne on the Vote in 2004 for implementation amounted to €129m.

Within the Department, the Office of the Refugee Applications Commissioner (the Commissioner) considers and decides on applications for refugee status from asylum seekers who wish to remain in Ireland. The Refugee Appeals Tribunal (the Tribunal) decides appeals against Commissioner decisions. Both agencies forward their recommendations to the Ministerial Decisions Unit of the Department of Justice, Equality and Law Reform.

The Ministerial Decisions Unit makes decisions on behalf of the Minister in relation to recommendations made by the Commissioner and the Tribunal on asylum applications. The Minister is, in general, bound by recommendations to grant asylum made by those bodies. In the case of negative recommendations, the asylum seeker is given the options of leaving the country voluntarily, consenting to deportation or making representations to the Minster on a number of grounds as to why he/she should not be deported. Following consideration of the case, including any representations made, leave to remain, on humanitarian or other grounds, may be granted at the discretion of the Minister or (as happens in most cases) the Minster is asked to sign a Deportation Order. The Arrangement Section (within the Repatriation Unit) is responsible for arranging deportation in cooperation with the Garda National Immigration Bureau (the Bureau).

My examination sought to establish the effectiveness of arrangements for enforcing deportation orders. Records of all cases where the Minister had signed an order in 1999 were reviewed to track performance in bringing cases to finality. I also examined a small number of cases from 2003 and 2004 to confirm whether the issues noted from the 1999 cases continued to apply.

Audit Findings

A departmental computer system was first introduced in the Repatriation Unit for the management of deportations in November 1999 and was replaced in October 2004 by a more comprehensive case management system. Migration of data to this system and quality assurance checks will shortly be completed. Table 18 summarises the status of the deportation orders signed by the Minister as recorded on the computer system for the period November 1999 to June 2005. Some 6,300 cases are described as "evaded". The Department informed me that these are cases where the deportation has not been effected and the case is not being actively pursued. An analysis of the 1,236 cases where orders remain to be enforced indicates that about 20% have been stalled due to Irish Born Child Applications and 10% await the outcome of Judicial Review proceedings. Over half of the cases, however, are awaiting enforcement.

Table 18 Status of Deportation Orders 1999-2004 at 30 June 2005

	1999	2000	2001	2002	2003	2004	2005	Total
Deportation Orders Signed	80	797	1,801	2,195	2,250	2,723	967	10,813
Deported, left State before enforcement or transferred to another	27	262	470	542	498	384	92	2,275

jurisdiction								
Evaded	30	326	1,089	1,454	1,467	1,449	522	6,337
Through revocation or otherwise, applicant permitted to remain	14	148	189	104	93	384	33	965
Orders remain to be enforced	9	61	53	95	192	506	320	1,236

The audit review noted that the knock on effects of the following factors are likely to have contributed to the rate of enforcement

- Significant delays between the date of application for asylum and the interview with the Commissioner to determine eligibility to remain in the country. These delays ranged from 2 days to over 22 months, averaging over 9 months.
- Significant time taken to translate questionnaires, which applicants were required to complete for the Commissioner. These ranged from 6 days to almost 2 years and averaged around 8 months.
- Widespread failure by applicants to attend the scheduled interview with the Commissioner. This resulted in repeated written reminders to applicants at addresses from which previous correspondence had been returned undelivered.
- Delays of 1 to 3 years from the date a negative recommendation was made by the Commissioner/Tribunal to the time the Department sent the Deportation Order to the Bureau for enforcement.

In order to help assess the effectiveness of the enforcement of deportation orders, I reviewed papers made available to me by the Bureau in relation to a specific deportation operation in April 2005. My review of this operation showed that the Department targeted 456 failed asylum seekers for deportation to an African country. The Department was aware that that country would accept no more than 50 persons on any one flight. An analysis of the outcome of the 456 cases written to is given in Table 19.

Table 19 Analysis of the Deportation Operation

Failed to show	228
Made new Applications	90
No Deportation Order Received in the Bureau	32
Injunctions taken out	16
Undertakings Made by Asylum Seeker	14
Unable to Travel for Medical Reasons	10
Deportation Orders Revoked	8
Held	6
Irish Born Child Applications	5
Other	22
Number finally Deported	**25**
Total	**456**

Accounting Officer's Response

In response to my enquiries, the Accounting Officer pointed out by way of background, that the number of persons applying for asylum in 1996 was only 1,179. By 2000, this had increased to almost 11,000 and further increased to a high of 11,600 in 2002. The Government approved additional resources to deal with the backlog of applications that had arisen. The formal establishment of the Office of the Commissioner and the Tribunal absorbed the majority of these resources. A high level of resources was allocated to these units in 2000 – 2001 resulting in increased outputs. As a consequence, the backlogs in the asylum system moved from application processing to the repatriation function. The intended movement of staff from application processing to repatriation did not happen as quickly as expected resulting in an inflow of files to the Repatriation Unit between 2001 – 2004 without the necessary staff resources to consider them.

He noted that the Refugee Act, 1996 was technically inadequate to address the large-scale increase in applications which arose since its enactment. In addition an elaborate legislative basis for the deportation process (introduced by the Immigration Act 1999) has been shown to be cumbersome and insufficiently streamlined to deal with speedy processing and enforcement of the large increase in deportation orders arising. New legislative proposals are in preparation to address this issue. Furthermore, he stated there was a need to put in place additional legislation (Immigration Act, 2003) to further streamline the Refugee Act, 1996 to deal with the large number of unfounded applications for asylum being received.

He stated that an increasing number of judicial reviews and the slowness of the judicial process in dealing with them had limited the Department's and the Bureau's ability to swiftly process and enforce deportation orders. Other factors outside the control of the Bureau *viz.* applications for Irish Born Child status and the non-availability of travel documents from diplomatic missions also impact on the enforcement of orders.

However, he was of the view that the overall average of orders enforced since November 1999 (23%) compared favourably with international experience. Over 60% of Deportation Orders issued are deemed 'evaded', in that the persons fail to report to the Bureau as requested in the notification letter sent to them. The legal effect of this is that the persons concerned can be arrested and detained pending their removal for failing to comply with the instruction to report but, in practice, the Bureau told the Accounting Officer that most of those 'evading' are believed to already have left the State of their own accord and have been removed from the social welfare system on the basis of exchanges of information between the Bureau, the Repatriation Unit and the Department of Social and Family Affairs.

Other delay factors

The Accounting Officer also dealt with the other factors which it was noted had contributed to delays and outlined progress being made.

Interview delays

He informed me that the present position with regard to waiting times for applications to be processed in the Office of the Commissioner and the Tribunal had improved to some 2,739 cases (31 May 2005). This compared with 5,414 at the same time in 2004 and some 10,000 cases in 2000. The number of cases over six months in the asylum system (Commissioner and Tribunal) as at 31 May 2005 stood at 734 as compared to some 6,500 in September 2001. Under new prioritisation arrangements introduced in January 2005, applicants are receiving interviews and decision at first instance within 3 weeks and subsequent appeals are processed within 10 working days.

Translation delays

He informed me that the Commissioner holds questionnaires submitted in support of asylum applications for translation until an interview has been scheduled for the application in question. This is done for reasons of efficiency and economy because of the numbers who do not attend for interview or withdraw from the process. From an average time of 8 months in 2003/4, questionnaires are now translated in less than 4 months.

Failure to Show for Interview

Applicants who fail to show are deemed to have withdrawn and the Commissioner makes a negative recommendation in these cases. As regards failed delivery of correspondence he said desk based and other related procedures are used to check the validity of addresses. It would not be practical from a resource point of view to go beyond these. In any event the Department believes that a significant number of such applicants have left the jurisdiction. Further attempts to trace these people would require additional resources and it is therefore considered that the priority, for efficiency and economy reasons, should be to process those applicants who were interested in having their applications investigated.

Analysis of the Deportation Operation

In the case of the deportation operation involving the 456 failed asylum seekers to the African country, the Accounting Officer said that the numbers targeted could be high multiples of the number actually deported, reflecting the very uncertain and unpredictable environment in which deportation operations are carried out. The high numbers arose from the knowledge that the likely rate of attrition would be high.

He pointed out that in relation to the 228 who failed to show, some were subsequently located in the United Kingdom and the African country. Others have been subsequently deported or will be deported in the future. In each case of 'failure to show' extensive investigations were made in an attempt to locate the individuals concerned. In many cases there was no trace of the individuals after the initial claim for asylum at a port of entry. These people are believed to have claimed asylum for the sole purpose of gaining entry to the State. Others had left their accommodation after receipt of the arrangements letter. The absence of exit checks at departure points from the State and the ease of movement over the land border with Northern Ireland allows for substantial abuse of the common travel area by persons subject to deportation orders.

He also stated that the cases described in Table 19 as 'No Deportation Order Received in the Bureau' refers to persons who had moved from their addresses without permission (in order to avoid deportation) and who were at Ministerial Decisions Unit stage in the process and had been located by the Bureau. The Bureau informed the Department of this and requested that the order be expedited. The Department was unable, for very valid reasons, to provide the orders on time to include the persons concerned in the flight.

Chapter 6

Prison Service

6.1 Human Resource Management System

Background

Delivering Better Government, published in May 1996, stated that the modernisation agenda in the Civil Service needed to be supported by changes in Human Resource (HR) Management policy and practices.

The actions required to give effect to Delivering Better Government called for the roll-out of modern, IT based Human Resource Management Systems (HRMS) in individual Departments/Offices across the Civil Service to provide a platform for improved service and strategic re-orientation of the HR function.

The benefits of the new systems were expected to include

- enhanced management information and reporting, with a greater emphasis on strategic HR issues
- greater efficiency in administration and improved service to staff
- an integrated system for both personnel administration and training/development
- interfaces to other systems such as payroll.

It was also expected that improved HRMS would open up the possibility of devolving certain aspects of HR to line managers.

The Department of Finance's Centre for Management and Organisation Development (CMOD) took the lead in centrally acquiring a well known Human Resource software package as the basis for strategic human resource management in the Civil Service and as a replacement for the existing Personnel Administration System (PAS) which had been in use for many years in most Departments/Offices. The chosen package was customised for use in Government Departments and Offices and piloted in the Department of Social and Family Affairs and Office of the Revenue Commissioners.

CMOD's main responsibilities were to maintain a standard template for the new system, coordinate maintenance of the common interfaces, respond to functional and technical support queries and issues as second level support, manage and control HRMS customisations and coordinate upgrades of the software.

Departments and Offices would be responsible for implementing, integrating, training, funding, maintaining and operating the new HR systems.

Coordinated Approach to Implementation

CMOD provided a standard Request for Tender (RFT) document to assist Departments and Offices in procuring an implementation partner to bring the new system into operation. The RFT, which included a standard Specification of Requirements, allowed each Department/Office the flexibility to define its own particular needs and to deal with issues arising from systems already in operation in Departments/Offices.

Justice Group Implementation

The Department of Justice, Equality and Law Reform decided, with the objective of achieving significant economies of scale, to seek a single supplier to implement the system for its five main entities, the Department itself, the Prison Service, the Courts Service, the Land Registry and Registry of Deeds and the Legal Aid Board.

Following a tender competition in late 2002, the Department engaged a leading consultancy firm as its implementing partner for the project.

HRMS in the Irish Prison Service

An audit review by my staff of implementation of the system in the Justice Group noted that notwithstanding significant payments to the consultants and the expenditure of considerable time and effort by staff, use of the new system was discontinued in the Prison Service in December 2004.

The Prison Service was the only one of the five organisations in the Justice Group not to be a user of the existing PAS system widely in use across the Civil Service before commencement of this project. The Prison Service used a personnel system based on a particular database package. Implementation of the new HRMS system commenced on a phased basis in the Prison Service in September 2003. By February 2004 Governors in prisons where the system had not been implemented decided to continue to use the old system rather than migrate to HRMS because of concerns raised that the new system did not meet the Prison Service business needs, required significant additional administration time to operate, and did not provide accurate management information. An internal Prison Service committee was set up to review the position and in September 2004 the Prison Service notified CMOD of its intention to withdraw from the HRMS. Formal notice of non-renewal of licences was sent to CMOD in December 2004.

The Prison Service ceased to use the new system on 1 December 2004, subsequently re-instating the old system, which required re-input of personnel records that had been migrated to HRMS.

Audit Concern

As the decision of the Prison Service to pull out of the HRMS project gave rise to significant nugatory expenditure and may have been indicative of either a failure by the project management to properly evaluate the needs of the Prison Service, or alternatively a lack of commitment in making the chosen system work, I sought the Accounting Officer's views.

Accounting Officer's Response

General

The Accounting Officer in his response stated that the Prison Service is a branch of the Department of Justice, Equality and Law Reform and operates from sixteen prisons and five other locations, including its headquarters in Clondalkin. At the time of the introduction of the HRMS in September 2003 there were eighteen prisons, and the system was implemented in all of them at that time.

The great majority (approximately 3,200 out of 3,350) of staff in the Prison Service belong to grades unique to the Prisons, resulting in a set of business needs that are particular to the Prison Service, which include dealing with staff that work irregular hours, injuries on duty, compensation for injuries, the

generation of sick leave reports which take into account the different work patterns of Prison Officers, letters for staff and the withdrawal of paid sick leave. This specialised set of requirements has made the Prison Service's experience with HRMS different from that in other agencies where the system has been implemented. In effect, the Prison Service is a seven day-24 hour a day organisation and its HR activities are geared on a "round-the clock" basis. The failure of the system customised to meet these particular requirements led to the Prison Service's decision to discontinue its use.

Given the unique needs of the Prison Service, work is underway to consider how best to meet current and future needs, with external facilitation. A decision will then be taken as to whether any off-the-shelf package would be suitable or whether the Prison Service requirements demand a custom built programme.

Response to Specific Queries

- *How much did implementation in the Justice Group cost?*

The Accounting Officer informed me that the total cost of implementing HRMS in the Department's Head Office, the Land Registry, the Legal Aid Board, the Courts Service and the Prison Service was €1.06 million. Table 20 gives an apportionment of these costs. The amount attributable to the aborted HRMS in the Prison Service was €450,545.

Table 20

	Justice Headquarters €	Prison Service €	Courts Service €	Land Registry and Registry of Deeds €	Legal Aid Board €	Total €
Pre Implementation	197,091	248,420	78,075	49,684	29,101	
Implementation/Consultancy	118,034	174,308	56,775	38,855	21,419	
Implementation Costs	12,311	27,817	5,943	3,821	2,123	
Total	**327,436**	**450,545**	**140,793**	**92,360**	**52,643**	**1,063,777**

He also indicated that the cost of re-keying information in the prisons was unlikely to exceed €5,000. The internal staff costs associated with implementing the system in the Group are approximately €26,000.

- *Why were the specific needs of the Prison Service not recognized and factored into the implementation prior to the issue of the RFT?*

In reply the Accounting Officer pointed out that while there was an awareness of the special business needs that might apply in the prisons it was decided to go for one singular implementation. It was likely that the Group would get economies of scale from going this route in terms of a cheaper overall implementation contract, and this proved to be the case. Secondly it gave the Group more clout in the market as a bigger and more lucrative implementation client and therefore more likely to attract 'serious' players. Thirdly there were considerable additional synergies on the technical level, in particular the idea of using a common server as opposed to setting up a separate one in each organisation.

The RFT sought an implementation partner for the basic HRMS available to the Civil Service. It was felt that individual agencies could then build their own modifications to fill any gaps. As it turned out, this approach did not work out for the Prison Service. The extra functionality required was extensive, there was little scope for upgrading/modifying the system itself, and any option taken would have required a lot of time.

Some of the difficulties with the RFT, from a Prisons perspective, were due to changeover of staff as the Prison Service moved to Clondalkin and the loss of corporate knowledge that accompanied it. New work practices were adopted to deal with these difficulties, but these did not adequately meet the needs of prison users. HRMS managed to provide much of the functionality of the existing software system, but was noticeably weaker than the old system in some of the key areas used by prisons. A HR system in a more 'finished' form would have been more well received by prison users, as from their perspective HRMS was a significant step backwards. This resulted in a low level of user acceptance across prisons.

He indicated that a standard set of reports when configured for Prison Service use proved cumbersome and untrustworthy. As a result, Clerks in prisons were often unable to fulfil their reporting requirements to their Governors.

Since the Justice implementation, a further set of 30 Civil Service reports were developed by CMOD, but only a small proportion of them provided any information. Furthermore, they did not work at all unless exported into a report writing package that could not be used in the Prison Service for security reasons. The Accounting Officer added that he understood that Prison Service was not unique in having difficulties with the system's capacity to provide satisfactory reports.

A further difficulty arose in relation to the Prison Service's requirement to provide sick leave advice letters to staff (as a result of a High Court ruling) and extra cost was incurred to build in letter production functionality. The Prison Service was presented with two options at the time, one was for five days' effort by the consultant, and the other for twenty days' effort, both at the daily rate of €990. The Prison Service opted for the cheaper of the two options.

- *Was adequate training provided?*

He informed me that Key Functional Users (KFUs) in the Prison Service were used to train the clerks of the prisons. Each clerk was given a half days training to learn how to input sick leave, print letters and see sick leave reports, using training manuals designed by the KFUs and the consultants. The clerks made numerous complaints about the system itself at this stage, but the KFUs covered all of the training areas with each of the clerks, as well as providing a considerable amount of "hand-holding" after the system went live.

The consultants did not include report writing training during the main implementation in any agency to the knowledge of the Accounting Officer. The rationale offered by the consultants at the time was that they felt it was better for agencies to go live with the system and get a feel for use of the system first before coming back for training in report writing. The consultants also felt that report writing training was not relevant to all end users but only to the KFUs.

- *What acceptance tests were performed to ensure delivery of a fully operational system?*

The five agencies of the Justice Group fully loaded current personal and sick leave information onto a test version of the HRMS database in order to test it. In the Prison Service tests, post go-live, the differences between HRMS and the old system were limited and for the most part due to different features of the new system. However there were difficulties with some documentation provided by the supplier.

The Accounting Officer pointed out that problems emerged with system response times depending on local infrastructural conditions in the 18 different Prison Service sites. As the HRMS is based on a web browser, there is no way around this except ensuring fast connection speeds at all stages. The Prison Service has since spent in the region of €150,000 upgrading infrastructure in the larger prisons. This requirement would continue to exist in the context of a new shared services solution provided by CMOD.

Was the assistance and guidance given by CMOD appropriate for the implementation of HRMS in the Justice Group as a whole?

The Accounting Officer stated that at the time of the Justice Group project, it was CMOD's position that each Department look after their own individual implementation. However, CMOD had a representative on the Justice Group Project Board and gave input as appropriate during the course of implementing HRMS.

As many of the Prison Service's difficulties arose post-implementation there is no particular evidence to suggest that CMOD was aware of the problem until after the go-live date.

When contacted about Prison Service's problems with HRMS, CMOD was of the view that the Prison Service was just one organisation in 17, and was not given any particular priority, despite the difficulties being experienced, though it could be argued that the Prison Service represented 10% of the staff in the Civil Service on HRMS.

In June 2004, after the prisons had discontinued use of HRMS, CMOD offered to assist in testing reports, but did not in fact do so, due to other work demands.

It could also be said that CMOD did not undertake any specific body of work to aid the Prison Service in this matter.

In summary, CMOD may have been constrained by the lack of resources available to them in providing support to all of the 13 Civil Service implementation projects, many taking place simultaneously. Learning from this process has since resulted in a change of approach to HRMS implementations for new users with a move to a common implementation.

Finally, Justice and the Prison Service were severely constrained in adapting the chosen system. The common HRMS system was customised for the Civil Service based on the Social Welfare and Revenue experience. The CMOD rationale of a common system across the service implied that modifications by users would interfere with future upgrades etc. so were not encouraged. The Prison Service environment, and consequently its IT needs, varies considerably from the broader Civil Service.

Summary Observations by the Accounting Officer

The Accounting Officer said that while there clearly were issues with HRMS in the Prison Service that ultimately led to its withdrawal, it would not be accurate to say that the other four entities in the Justice Group experienced anything like the same level of difficulties. That said, there were teething problems with HRMS across the Justice Group as end users acclimatised and got used to the new system. He said there is nothing unusual about this as many end users to most new IT systems generally experience similar difficulties in adapting to new processes and technical configurations. While the other users in the Justice Group had less technical requirements and quickly came to terms with the new system, the unique requirements pertaining to the Prison Service were such that a long term commitment was not a viable option. He added that with the benefit of hindsight, it might have been preferable had the Prison Service decided not to go along as part of the Justice Group on the basis that its requirements were so fundamentally different to the generality of needs across the Civil Service, that any enhancements of a substantive nature post implementation would have been difficult, and prohibitively costly, to implement.

In summary, his Department had little option but to go along with HRMS as CMOD had decided to discontinue supporting enhancements on the existing PAS system. While the HRMS system has worked well in most of the Department's agencies, the experience in the Prison Service is that system does not meet the particular requirements there. The fact that the Prisons operate from 18 different locations, on a 24 hour/7 day per week basis with a range of atypical attendance patterns and unusual arrangements in relation to sick leave requirements etc, meant that a fully integrated HRMS system was always going to be difficult to achieve. Moreover, the overall situation in the Prison Service has also been exacerbated by the industrial relations scene in recent years including the need to reduce the substantial overtime bill.

He assured me that his Department had learned a very considerable lesson from its experiences with HRMS. Any further IT projects on a cross-agency basis, will need to be critically examined - irrespective of the demands or where they are coming from - to ensure that they can meet the requirements of the different entities involved.

Views of the Department of Finance

In light of the comments of the Accounting Officer, I asked the Department of Finance for its observations on the role of CMOD in the matter.

The Accounting Officer of the Department of Finance informed me that he believed that CMOD had met its obligations as regards the maintenance of a standard template for the new HR Management System, co-ordination of the maintenance of the common interfaces, responding to functional and technical support queries and managing and controlling HRMS customisations and co-ordinated upgrades of the product.

Ownership remained with Departments and Offices and ultimately it was their responsibility to allocate the appropriate resources to maintain and manage their instance of the HRMS software and also to provide day-to-day support of the system.

With reference to the comments of the Department of Justice, Equality and Law Reform, he made the following points

- While the Prison Service implementation took place in late 2003, his Department was unaware of the Prison Service problems until June 2004. CMOD were not notified of the decision to discontinue use of HRMS until the end of November 2004.
- Although some organisations experienced problems with the standard reports issued with the template, they could alter these to meet their specific requirements and many did so. CMOD also prepared 30 additional general-purpose reports for civil service application in the first quarter of 2004 and made them made available to the Justice Group at that time. They could be further refined or extended to meet particular requirements. This set of reports continues to be widely used, including use by non-HR staff in devolved locations.
- It was never envisaged that the original reports, or the additional set of 30, would be sufficient to meet all the needs of Departments or Offices. CMOD expected that Departments and Offices would develop further reports using the querying/reporting facilities provided by the HRMS.
- The CMOD set of reports does not require an export to an additional report-writing package as they can be run successfully within the HRMS application. However, the additional report-writing package referred to is in widespread use both within the civil service and worldwide. CMOD are

aware of HRMS implementations that have over 100 reports, many of which are specific to their own needs, and would have been written in-house.

- In regard to the responsiveness of the system, CMOD do not agree with the Prison Service view as they consider that it would have been open to the Justice IT Unit to have provided more processing capacity if there had been a significant and persistent problem with running queries/reports. CMOD would also like to state that badly written queries/reports can have an adverse impact on system performance.
- CMOD could not accept any responsibility for network infrastructure deficiencies in the Prison Service and note that the HRMS desktop uses a web browser that requires far less network capacity than, for example, e-mail, word-processing, and older shared file databases.
- The production and content of letters from the system was always a matter for each individual Department/Office.
- CMOD have on many occasions provided HRMS assistance to the other Justice sites by phone, by e- mail and through on-site assistance. The Prison Service was provided specific assistance by phone and e-mail. Offers of support on report writing were made at a meeting with the Prison Service in June 2004 and at a meeting with the Department of Justice, Equality and Law Reform in September 2004, but these were not taken up.
- Offers by CMOD to make site visits to the Prison Service offices were also not taken up.
- CMOD were unaware of any instance where a lack of resources caused it not to respond to the Prison Service calls for assistance and support.

As a result of the experience of the 13 implementations of the HRMS, and following on from a CMOD study of shared services, the Civil Service HR community have used a private sector partner to implement the latest upgraded version of the HRMS. This will be a single implementation for the whole of the Civil Service and will eliminate the repetitive work and the multiplicity of computing resources associated with an individual approach to the implementations.

Chapter 7

Department of Education and Science

7.1 Superannuation Schemes

Introduction

Superannuation schemes may be statutory or non-statutory.

A statutory scheme is one which is provided for in an Act of the Oireachtas. The provision usually takes the form of an enabling section in the Act giving authority for the making of Regulations (i.e. Statutory Instruments) setting out the details of the relevant superannuation scheme. Changes to the statutory schemes are intended to be carried out through the making of amending Regulations. The main superannuation schemes for teachers are statutory.

A non-statutory scheme is one which has no legislative foundation but is made, with the consent of the Department of Finance, to implement agreements entered into between the Department of Education and Science (or one of its agencies, with the Department's approval) and the appropriate staff representatives. Non-statutory schemes established over the last 20 years or so will comply with the model superannuation scheme devised by the Department of Finance for state-sponsored bodies. Changes to the non-statutory schemes are implemented with the sanction of the Department of Finance. Most such changes arise out of claims by the public service unions for improvements in superannuation provision.

Non-statutory schemes are regularly operated throughout the public service. Apart from those for which the Department is responsible, the superannuation benefits for non-established civil servants are, for example, provided for by means of a non-statutory scheme.

Audit Issue

I have previously reported to Dáil Éireann on the failure of the Department to ensure that there was up to date legislative authority for amendments to the statutory superannuation schemes of teachers. These reports were subsequently discussed at the Public Accounts Committee where the then Accounting Officers confirmed that steps were being taken to comply with the legislative requirements.

During recent audits by my staff, it became apparent that despite these assurances, amendments made to statutory schemes operated by or under the authority of the Department have not been given the necessary legislative authority.

Accounting Officer's Response

Changing and Consolidating Schemes

The Accounting Officer provided details of the improvements and changes made to the schemes over the years. She pointed out that many have common application but some apply only to particular schemes.

She agreed that formal updating of the statutory schemes, by means of statutory instruments, is necessary in order to meet legal requirements. Apart from this, she accepted that it was most desirable, from the point of view of facilitating administration, to formally update all schemes, statutory and non-statutory, as changes and new provisions come on stream.

She stated that in recent decades, taking into account the pace of change in the area of superannuation, and the fact that industrial relations agreements are regularly implemented with retrospective effect, it has become common practice throughout the public service to implement changes to statutory superannuation schemes administratively, usually through the issue of circular letters, and to make the appropriate statutory instruments at a later date.

She also informed me that a number of initiatives to bring the schemes up to date have been undertaken over the years but have faltered along the way. The most recent of these was in the case of the Secondary Teachers' Superannuation Scheme where, in 2000, a barrister was assigned to the task of drafting a consolidated scheme, including all amendments. The barrister provided the Department with a draft consolidated scheme in Spring 2001 but it has not been possible to address the necessary task of verifying the work of the barrister because relevant staff of Pensions Unit have been occupied by other work, including work which has arisen in connection with the consideration and implementation of the Part-time Work and Fixed-term Work Acts and the consideration and implementation of the recommendations of the Commission on Public Service Pensions. The immediate priority, when work recommences, will be to carry out the required verification in connection with the Secondary Teachers' Scheme.

She added that she expected that the Universities, as required by the Universities Act 1997, would have their new public service model schemes ready for approval by autumn 2005. It would be desirable that other schemes should also be formally updated when the model scheme is available but this will be dependent on resources being made available. In this regard, her Department is not aware that the absence of statutory amendments to schemes has caused any particular difficulties for the Universities, Institutes of Technology, Vocational Education Committees and other external education institutions and bodies. She accepted that a consolidated scheme in each case, including all amendments, would be the optimum in terms of ease of administration and in terms of transparency.

Difficulties to be Overcome

The Accounting Officer said that the main difficulties to be overcome to bring the work of formally updating the Schemes to a successful conclusion include

- The availability of skilled staff to deal with the complex and technical nature of drafting the schemes
- The competing demands for staff resources within the Department
- The rapidly changing superannuation environment.

Given the substantial work involved, addressing this issue is a multi-annual project.

In relation to the allocation of staff for specific projects the Department must prioritise the many demands it faces. The Department must also operate within its approved staffing numbers and is bound by the Government policy on staffing numbers in the public service. Therefore the scope to apply additional resources to the task of bringing the superannuation schemes legislatively up to date is limited. That said, the Department intends exploring other options including contracting the work to appropriately qualified outside experts if such can be found.

Consequences of Schemes not being updated

The Accounting Officer informed me that in the absence of a statutory instrument underpinning a change in a statutory superannuation scheme, the change would be open to the challenge that it is *ultra vires* the Minister for Education and Science.

On the other hand, the changes which have been implemented on an administrative basis are in effect part of the terms of employment of teachers and other staff, negotiated generally through industrial relations machinery. As such they are legally binding agreements related to superannuation. Furthermore, the changes have at all times been subject to the approval of the Minister for Finance.

Chapter 8

An Roinn Gnóthaí Pobail, Tuaithe agus Gaeltachta

8.1 Financing of Rural Social Scheme

€10 million was paid from the Dormant Accounts Fund into a suspense account operated by An Roinn Gnóthaí Pobail, Tuaithe agus Gaeltachta to meet the expenses of a Rural Social Scheme announced by the Minister for Finance in his Budget Speech 2004. During 2004, almost €3.4 million was paid to scheme beneficiaries from the suspense account with the balance paid in 2005. A further €12 million was provided in the Vote for 2005 for on-going funding of this scheme.

Strictly speaking, the legally correct way of channelling the money to the beneficiaries would have been to pay the €10 million into the Central Fund as Exchequer Extra Receipts, take a Supplementary Estimate for Vote 27 in an appropriate amount for Subhead Q.3. and account for the moneys paid out under the scheme in the normal way as subhead expenditure in the Appropriation Account.

The Department of Finance had directed An Roinn to use the suspense account mechanism. However, following my enquiries, the Accounting Officer for the Department of Finance conceded that on reflection it would have been better to have channelled the funding through the Vote. The recently enacted Dormant Accounts (Amendment) Act 2005 provides that future disbursements from the Dormant Accounts Fund will be through moneys provided by the Oireachtas, *i.e.* through a Vote.

I have qualified my audit certificate on the Appropriation Account for Vote 27 accordingly.

Chapter 9

Department of Arts, Sport and Tourism

9.1 The Irish Genealogical Project

Background

The Irish Genealogical Project (the Project) was established in 1988. Its objective was to facilitate

- The compilation of a comprehensive and accurate computerised database for all the major genealogical records available in Ireland
- The implementation of a system for marketing and delivery of reliable family history research.

In 1996 I carried out a value-for-money examination of the project and reported my findings to Dáil Éireann.[12]

In 1997 the responsibility for steering the Project was assigned to a limited company, Irish Genealogy Limited (IGL), a company-limited by guarantee whose mission is to deliver on the objectives of the project. Up to that point a Committee, serviced by the Department of the Taoiseach, had responsibility for its co-ordination. IGL is currently supervised by the Department of Arts, Sports and Tourism (the Department). From establishment in 1997 to 31 December 2004, IGL received grants totalling €2.5 million from its funding Department.

The Project also benefits from State aid in the form of

- Assistance by way of FÁS trainees and staff in the inputting of records to databases in the genealogy centres around the country. FÁS has estimated that the value of its assistance since 1988 up to 31 December 2004 has been in the order of €32.2 million
- Some assistance from Local Authorities, which varies in form from area to area.

At the commencement of the Project there were 35 genealogy centres throughout the island of Ireland recording and collating records of various types.

IGL has assisted centres from 2001 onwards by providing resources to replace obsolete IT systems with modern server based systems on a common software platform. The upgrade of the IT systems is to be completed in 2005.

Genealogical Records and Research

The original concept of a computerised database called for the recording of an estimated 28 million records drawn from Church and Civil records, the 1901 and 1911 Censuses, Griffith's Valuation and Tithe Applotment Books.

It was planned that a Central Signposting Index (the Index) would be created utilising data fields drawn from the database records. The Index would be the first point of contact for an individual seeking family

[12] Report No. 14 The Irish Genealogical Project — December 1996

records through using the Internet. The Index would signal the existence of the records and guide the individual, through a hyperlink, to the genealogy centre with the required detailed records.

While the business plan of IGL for 2005 – 2007 aims to have 90% of Church records completed by the end of 2007 it is accepted by the main project stakeholders that at the current rate of progress on the inputting of Church records onto the databases in the centres it could take over 20 years to complete the recording.

In some respects the project has been overtaken by events. Non-Church records are now available directly from a variety of sources. IGL considers that the centres should focus on church records only and has opened discussions with FÁS on this matter. Table 21 sets out the position in regard to non-Church records data.

Table 21 Non-Church Records

Record Type	Agent/Owner	Availability
Tithe Applotment Books	Ulster Historical Foundation	The entire record is available to members of the public on compact disks
Griffith Valuation	National Library and an English Private Company	Access is from National Library without charge and from the company via the Internet for a fee
1901 & 1911 Census	National Archives and the National Archives of Canada	Access to the records in the National Archives is without charge. A project to digitise the records is being undertaken and access will be provided on the Internet
Civil Records of births, marriages and deaths	General Register Office	Access to the records in General Register Office. The records have been digitised but are not accessible through the Internet

Project Stakeholders

Irish Genealogy Limited

IGL co-ordinates the project and it has a staff of three — Chief Executive Officer, an IT Manager and a Project Administrator.

The Board consists of 15 Directors as follows

- 3 appointees of the Minister for Arts, Sport and Tourism
- 3 appointees of the Department of Culture, Arts and Leisure (Northern Ireland)
- 2 appointees of the Association of Professional Genealogists in Ireland
- 1 appointee of the Association of Ulster Genealogists and Record Agents
- 5 appointees of the Irish Family History Foundation.
- The Chief Executive Officer is an *ex-officio* member.

The following bodies nominate observers to the Board who attend and contribute to Board meetings

- FÁS, The National Archives Office, Fáilte Ireland, Northern Ireland Tourist Board, National Library, General Register Office (GRO), Department of Arts, Sport and Tourism.

The Department requires IGL to submit periodic business plans.

Irish Family History Foundation (IFHF)

The IFHF represents 28 of the 35 genealogy centres throughout the island of Ireland.

The stated objectives of the IFHF are

- The completion of the computerisation of the Church records by the centres throughout the island.
- The provision of genealogical research services through the centres on a commercial basis.

Association of Professional Genealogists in Ireland

The APGI represents individual genealogists who provide family history research services on a commission basis. The APGI functions as a regulatory body to set standards for the conduct of genealogical research by its members and to protect the interest of its clients.

Association of Ulster Genealogists and Record Agents

AUGRA is a representative association of professional genealogists operating in Northern Ireland.

General Register Office

The GRO has custody of all civil records of births, marriages and deaths, which were registered since registration began in 1845. The GRO facilitates genealogical research, consistent with carrying out its main function of maintaining the public records.

National Archives

The primary function of the National Archives is to preserve public records and make them available to the general public.

Foras Áiseanna Saothair

In the Republic of Ireland FÁS supports the centres through the provision of staff to supervise trainees inputting records and contributes to overhead costs. The centres operating in the Republic of Ireland are dependent on FÁS training programmes for their staff. FÁS have stated that continued support cannot be guaranteed in the long term.

Ownership of Data and Access to Records

The position in regard to the ownership and custody of the records and databases derived from them is understood to be as follows

- The ownership of the Church records vests in their original custodians, the relevant Church authorities. The use of the information drawn from the original records for genealogical research purposes is provided for in a set of agreements between the owners and the centres affiliated to the

IFHF and a set of agreements between the owners and those centres in the Republic that are not members of the IFHF

- There is also a set of agreements in place between the owners of the centres and the IFHF whereby the records will be placed in the custody of the IFHF (subject to such legal agreements as may apply to the sources in question) in the event of a centre closing its business.
- IGL maintains the Index. A legal agreement with IFHF covers the arrangements for transfer of data from the centres for inclusion on the Index. The agreement provides that the IFHF, from June 2002, will forward Church records for a period of ten years for inclusion on the Index. It is agreed that while IGL will have exclusive access to the Index the custodian of the records on the Index will be IFHF on behalf of its members.

Current Issues

In the course of my audits of IGL I noted a number of issues of management and co-ordination which impact on the successful completion of the Project and on the capacity of the stakeholders to maximise genealogy tourism.

- There is disagreement between the stakeholders on whether to prioritise the finalisation of the databases of Church records before the creation of the Index and a question of how data input might best be carried out in order to complete the database within a reasonable time.
- Centres closed *i.e.* Limerick, Carlow, Tipperary North (now reopened) and Kerry (now reopened) when FÁS or local authority support is withdrawn. The critical business continuity risk is the current business model which relies on this type of support to sustain the centres.

Completion of the Databases

Up to the 31 December 2004 no funding was provided by IGL to assist in the completion of the databases or for administration of the centres. Moneys were made available to them, however, for IT systems upgrade, including equipment, staff training and changeover support and marketing supports including product development and sales.

Although 19 of the centres have fully completed the inputting of information from religious records the IFHF has expressed dissatisfaction with the rate of progress on the inputting of Church records, which they put at around 1% per annum. They are also unhappy with the IGL focus on completion of the Index before all data is input on the databases. The IFHF believes that the completion of the databases in the genealogy centres should be the primary focus of IGL.

The IFHF has pointed out in a letter of May 2005 which it sent to IGL that

- The recording of new data had virtually stagnated in the past six years
- The Index appears to be a big database due to the inclusion of records other than those on births, marriages and deaths and remains in a partially completed state and was unlikely ever to be completed.

Currently, IGL is considering assisting in the recording of the religious records through a funded programme and, for the first time in 2005, €75,000 will be made available for commercial inputting of records.

In 2000 it was estimated for IGL that the commercial completion of the inputting of Church records on the databases at that time would have cost approximately €3.43 million.

However, since February 2005 the situation has become further complicated because the IFHF has withdrawn its support of the Project and has advised its members not to forward any further records for inclusion on the Index; as a result the provision of information for the Index ceased from that time.

The IFHF directors resigned from the IGL Board in February 2005.

Business Continuity

Currently, two of the 35 genealogical centres are closed — Carlow and Limerick. The feasibility of reopening these centres is being examined.

In February 2005 consultants reporting to IGL on the operating structure and viability of the centres, noted that the challenge for the Project is to move from the production of the databases to product development and marketing. The long-term sustainability of the Project depends on managing this change.

The report also emphasised that on the resource side one of the main sources of funding was from FÁS and that this funding was being used to support the operational viability of the centres. FÁS have indicated that its long-term support cannot be guaranteed and as a result of this there is a threat to the viability of some of the centres.

The review outlined a number of strategic options to make the centres sustainable. These included

- The negotiation of a long term relationship with FÁS
- Failing this, the sourcing of sponsorship from another body
- Delivery of a streamlined genealogy service through different business models.

The advent of the Internet and changes in tourism trends appear to have also impacted on the original objective of promoting roots tourism. A report prepared for IGL indicates a downward trend in overseas participation in genealogy tourism between 1999 and 2003. Table 22 sets out this trend.

Table 22 Trend in Overseas Genealogy Tourism 1999-2003

	1999	2000	2001	2002	2003[13]
Visitors	107,000	118,000	88,000	36,000	53,000
Holidaymakers	102,000	102,000	81,000	29,000	47,000

Views of the Department

In view of the slow progress in completing the project, which commenced some 17 years ago I sought the Accounting Officer's views.

[13] 2003 figures are provisional

What targets had been established for the completion of the databases and the Index?

He informed me that as regards Church Records, the present policy of IGL is to focus exclusively on the completion of indexing and inputting of Church records of baptisms (births) and marriages prior to 1900. IGL is now of the view that the construction of databases for non-church records is more appropriate to other bodies including the National Archives, National Library of Ireland and General Register Office. The network of 33 genealogy centres some 27 of which are affiliated to the IFHF, is considered by IGL to be an appropriate mechanism for processing and indexing of local church records. The project is by its nature labour-intensive and painstaking. Of the total current estimate of 13.7 million church records, some 10.5 million (76%) have been indexed and inputted to the computerised database. The bulk of the remaining 3.2 million records require to be indexed and inputted. He noted that 19 of the 33 county-based genealogy centres have inputted 100% of their church records. Work in the centres, carried out in the main by FÁS trainees, is well supervised and has been executed to an acceptable standard with an error rate of just 1.8% (against a norm of 3%).

He pointed out that in recent times, inputting of records has slowed, the prime reason for which is a reduction (from 337 to 213) in the number and profile of FÁS trainees available to carry out the inputting task. This has resulted in records being indexed/input at a rate of just 1% per annum. This would require 20-25 years to complete the inputting of the 3.2 million church records outstanding. IGL is now contemplating completing the task mainly on a commercial basis together with some inputting by volunteers. In 2004, IGL estimated that if funding of the order €150,000 per annum were available and augmented by local area funding, some 90% of records could be indexed/input by end 2007. To enable commencement of commercial inputting, IGL has allocated €75,000 for this purpose in 2005.

As regards the Index, the Accounting Officer informed me that currently some 2.8 million church records in 11 counties can be accessed through the Index. The IGL target is to have some 10 million records on the Index by the end of 2007. He stressed that unlike other genealogy websites, the IGL website encourages customers to take the next step and visit the area of their ancestors, thereby generating tourism revenue especially in rural areas.

Since its inception, there have been some 250,000 individual searches of the Index database by customers, resulting in IGL referring 1700 firm marketing leads to the genealogy centres. In addition, it can be surmised that interest in visiting Ireland will have been stimulated.

Whether the project approach continues to be a viable mechanism for achieving those targets and delivering on the original objectives and if so how business continuity risks will be managed?

He informed me that it is the view of the Board of IGL that the county-based genealogy centre delivery system continues to be a workable concept but that a business model for future sustainability needs to be put in place. IGL has commissioned consultants who have proposed a range of business models which are currently under consideration by the Board. These include the negotiation of a long-term linkage with FÁS or with Local Authorities.

He added that long-standing differences of opinion on the delivery of the project between IGL and the IFHF, as major stakeholders, have been a difficulty in pushing for completion. However, he felt that the business risk is minimised to the extent that, of the 3.2 million church records outstanding, some 2 million can be inputted by centres which are not affiliated to IFHF.

The Minister for Arts, Sport and Tourism met with the IGL Board in June 2005 and requested them to revert to him as soon as possible with a sustainable business plan for the project and to take steps to have all matters in dispute between IGL and IFHF resolved without delay.

Whether the project structure continues to be suitable to the management of the network of relationships both public and private involved in the delivery of the service?

The Accounting Officer stated that IGL is a conglomerate of public and private stakeholders. While this structure brings a broad range of relevant genealogical experience to the deliberations of IGL, there is an onus on Board Members, as conveyed to them recently by the Minister for Arts, Sport and Tourism, to maintain a coherent focus on the objectives of the project.

At the invitation of the Chair of IGL, a meeting between IFHF and IGL was held on 14 July 2005 at Limerick to discuss existing difficulties with a view to reaching an amicable settlement on all issues currently in dispute. Both accepted the need for working in co-operation and a further meeting to establish a bilateral arrangement is scheduled for September. Following this, IGL will provide a supplementary business plan focused on completion of the project within a specified timeframe.

How the completion of the recording of the Church records and compilation of the Central Signposting Index will be effected from this point onwards and in particular how data input will be organised, controlled and resourced?

IGL has advised that there are three elements to the completion of indexing of the church records. The existing FÁS scheme, though depleted, together with a volunteer input will make some inroads. However, indexing and inputting on a commercial basis will be essential to clear the bulk of the outstanding records. The allocation by IGL of new computer equipment to replace the obsolete equipment at the centres affiliated to IFHF was conditional on those centres facilitating the transfer of computerised records to the Central Signposting Index. In itself, linking the computerised records to the Index is largely a technical operation which can be progressed rapidly on the basis of provision of complete data from the centres, in particular the IFHF-affiliated centres. It is expected that these issues will be addressed in more detail at the forthcoming meeting.

What progress had been achieved in gaining access to non-church records on behalf of the network of Genealogy centres?

The Accounting Officer informed me that IGL has advised that some 7.2 million non-church records have been indexed by the genealogy centres on an ad-hoc basis mainly from local health boards. It is current IGL policy that only church records should be indexed and IGL maintains that indexing/inputting of non-church records is a matter inter alia for the General Register Office, the National Archives and the National Library. Since publication of the Value for Money Report of the Comptroller and Auditor General in 1996, an examination of the project in 1999 was undertaken by the then Department of Arts, Heritage, Gaeltacht and the Islands. That report was positive on the future viability of the project. In the main, IGL has endeavoured to implement the recommendations of the Comptroller and Auditor General's Report.

In addition, IGL itself has commissioned consultancy advice on genealogy tourism and on the business models which might be appropriate to promote a sustainable future for the county-based genealogy centres.

Notwithstanding that IGL is a private company, senior management in the Cultural Institutions Unit of the Department will continue to attend IGL Board meetings.

The Minister for Arts, Sport and Tourism has asked the Board of IGL to revert to him with a sustainable business plan for completion of the project. On receipt of this plan, the Minister will then decide on whether or not to commission a separate independent consultancy evaluation of the project.

IGL views on Progression of the Project

The key challenges identified by IGL are the completion of the index/input of church records; the sustainability of the local genealogy centres; the marketing of the genealogy project and the development of genealogy tourism; and to ensure that the cultural and peace and reconciliation dimensions are delivered.

The project of indexing and inputting some 10.5 million church records on a modern database and providing a Central Signposting Index access facility for some 2.8 million church and non-church records has been executed for a relatively modest financial outlay. In the period 1998 to 2004, Departmental grants amounted to €2,104,880 (Excluding FÁS funding of its trainees). In addition, some €400,000 has been provided under the PEACE I and PEACE II programmes. The evaluator on behalf of the EU in relation to the earlier expenditure commented *inter alia* that *"The IGL project has proven to be an ideal project to seize opportunities arising from the peace process as well as integrating steps that can help pave the way for reconciliation…….. there are no concerns in relation to the financial management of the project."*

Having regard to the change in relation to the availability of FÁS trainees, IGL believes that indexing/inputting of data on a commercial basis is necessary to complete the project.

IGL foresees that the completed project with a fully implemented Central Signposting Index will be an excellent tool for assisting development of the fledgling genealogy tourism product.

Other Accounting Officer comments

The Accounting Officer stated that while it is clearly a matter of concern that delivery of the Project is taking far longer than anticipated in 1988, it is reasonable to note that the project has been overtaken by events in some respects. It is also clearly the case that the resource implications of the project were significantly underestimated.

The Accounting Officer concluded by stating that the Board of IGL has now been left in no doubt that if the project is to be funded further, there must be a clear business strategy for completion in accordance with value for money principles.

FÁS comments

I also asked FÁS to comment on the sustainability of the present arrangements taking account of any changes in the structure of the trainee population in recent years and the policy priorities of FÁS.

The Director General informed me that FÁS funds heritage centres on the basis of the quality of the training that they provide for the unemployed person. He pointed out that while much change has taken place in the economy and the jobs market, some communities and individuals have not progressed at the rate of their contemporaries. Therefore, FÁS continues to provide a range of supports to enable unemployed job seekers access and progress within the labour market. The partnership between FÁS, its sponsors and the community results in FÁS — with a modest outlay in training allowances that goes directly to the trainees, a supervisory grant and a small contribution to administration costs — being able to provide good quality training for unemployed persons for whom it would otherwise be very difficult to cater for.

Chapter 10

Department of Foreign Affairs

10.1 EU Presidency

Introduction

An Interdepartmental Administrative Planning Group met regularly from 2001 to co-ordinate work associated with the EU Presidency and extensive preparatory work was necessary to ensure the successful planning and organisation of the very large number of meetings to be hosted and chaired.

The 2004 Presidency posed new and demanding challenges in comparison with that held in 1996 on account of:

- The progression of ten States from observer to full membership of the European Union during the Presidency which required provision of logistical support for twenty-five Member States and three observer States, Bulgaria, Romania and Turkey.
- The negotiation of private sector sponsorship and
- Significant advances in information and communications technology since 1996.

Financing the Presidency

The largest proportion of the cost to the State of hosting the Presidency was borne by the Department of Foreign Affairs (the Department). Funding for the costs relating to Presidency events was provided in the Vote for 2003 and 2004. The main expenditure headings were payroll costs of extra staff, travel and subsistence, accommodation and hospitality, information technology, telecommunications and office premises and supplies. The total amount charged to the Vote was €10.7 million in 2003 and €21.4 million in 2004. During the course of audit an analysis was carried out of Departmental Presidency expenditure in 2003 and 2004 and the results are summarised in Table 23.

Table 23

	2003 €	2004 €	Total €
Salaries and Allowances	3,871,284	5,312,668	9,183,952
Travel and Subsistence Expenses	414,475	3,220,213	3,634,688
Helicopter Hire	-	159,723	159,723
Accommodation and Hospitality	9,005	2,396,640	2,405,645
Premises Costs	1,429,289	1,611,921	3,041,210
Telecommunications and Postal Expenses	63,329	1,642,534	1,705,863
Publications and Stationery	587,277	2,163,475	2,750,752
Information Technology Costs	3,486,309	559,272	4,045,581
Presidency Training	83,409	64,298	147,707
Press and Information	552,593	1,074,851	1,627,444
European Council Expenses	-	2,255,964	2,255,964
Incidental Expenses	210,841	910,897	1,121,738
Total	**10,707,811**	**21,372,456**	**32,080,267**

The analysis was hampered by an inadequate account code structure. The Department accepts that there were inadequacies and has since simplified and rationalised the structure.

In the course of my audit of the expenditure a number of minor issues arose and were brought to the attention of the Accounting Officer. He has informed me that lessons have been learned from these

instances and such problems will not recur. However in the case of road transport services two specific issues arose and these are addressed in the following paragraphs.

Road Transport Services

Expenditure on Travel and Subsistence Expenses includes an amount of €920,220 paid in respect of road transport services provided by a single contractor. A further amount of €45,166 paid to the same contractor, is charged to Press and Information bringing the total paid to €965,386.

Procurement procedure

The procurement process, which resulted in the placing of this contract was as follows:

- A notice seeking expressions of interest was issued on 31 October 2003 to six transport providers seeking expressions of interest by 5 November and detailed proposals by 10 November 2003.
- Three proposals were received and two applicants were interviewed on 24 November 2003.
- Following consideration of factors including cost, management skills, personnel, capacity, capability, experience and quality of service, the Interdepartmental Administrative Planning Group for the Presidency agreed on the supplier to be offered the contract.
- The Department on 26 November 2003 issued a letter of offer to that supplier. The letter stated that the Department would be in contact later to discuss the terms and operation of the contract.
- On 1 December 2003 the supplier confirmed acceptance of the offer in writing.

Under national and EU procurement guidelines the appropriate procurement procedure for services on this scale is an open tendering competition. However in this instance the Department utilised negotiated tendering. The use of negotiated tendering is permitted only in exceptional circumstances or in the case of extreme urgency or unforeseen events. According to the *Guide to Community Rules on Public Procurement of Services*, published by the European Commission for Directive 92/50/EEC, unforeseen events are events which fall outside the field of normal economic and social activity, such as floods or earthquakes which necessitate urgent services to assist victims. Recourse to the urgency procedure is permitted by the Directive only to the extent necessary to procure services necessary to deal with the immediate urgent situation over a period of about one month. For services required after this period it is considered that the contracting authority has sufficient time to publish a contract notice and award a service contract in accordance with normal procedures. I asked the Accounting Officer why the Department did not employ open tendering and place a formal notice in the Official Journal of the EU as required by national and EU procurement guidelines. I also asked how the Department concluded that the negotiated tendering procedure was appropriate in the circumstances as it was not clear to me that the Department could rely on the extreme urgency provision of the EU Directive in the circumstances in which it found itself in October 2003.

The Accounting Officer informed me that the Department acknowledges that it should have placed a formal notice in the Official Journal and regrets that it did not do so. He stated that it was the complex and protracted nature of the ultimately successful negotiation of private sector transport sponsorship that compelled the Department not to employ the open tendering procedure.

For the first time during an Irish Presidency the Department negotiated a range of private sector sponsorship agreements. This sponsorship resulted in an overall estimated saving of approximately €3.5 million. Of that amount the value of transport sponsorship was an estimated €1.8 million.

As the Danish Presidency provided the model for the Department on how to handle private sector sponsorship, an evaluation of the Danish experience was possible only in February 2003 after their Presidency. Cabinet Committee approval to seek private sector sponsorship was received in early April 2003 and the process of seeking sponsors for the Presidency was initiated at that stage. In the transport area a number of companies offered sponsorship. Until an offer of sponsorship was agreed in October 2003, the Department's precise transport needs for the Presidency could not be fully known.

In view of the time constraints, and the absolute need to have transport arrangements in place at the start of the Presidency, the Department was not in a position, in October 2003, to use the open tendering procedure. It came to the conclusion, therefore, that it had no option but to use the negotiated and urgency procedure. This procedure can be used in cases of extreme and genuine urgency where the delay was caused by factors unforeseeable and not attributable to, or within the control of, the contracting authority. Article 20 of Council Directive 92/50/EEC and the Department of Finance 1994 Guidelines provided the framework in operation at the time.

At that time the 1994 Department of Finance Guidelines set out the framework of how to proceed to tender. However, the Accounting Officer stated from Presidency preparatory work, it was known that a new draft Directive was close to completion. The Department contacted the relevant unit in the Department of Finance and received a copy of the new draft guidelines. These had been prepared in anticipation of the conclusion of the negotiations and the imminent adoption of the draft Directive (which became Directive 2004/18/EC published in the *Official Journal of the European Communities,* 30 April 2004). Both sets of guidelines informed the Department's decision to use the urgency procedure. The text of the draft guidelines on the negotiated and urgency tendering procedure supplied by the Department of Finance is identical to Guidelines adopted in 2004. The Department sought to follow best practice in awarding the Presidency contract in that it both anticipated and applied the new regime.

In his reply to me the Accounting Officer also stated that one of the lessons to be learned from the Presidency in 2004 is that, if significant sponsorship arrangements are to be entered into for services such as transport, the negotiations with potential sponsors should start and conclude some very considerable time before the Presidency. The Department now knew that nine months is an insufficient amount of time to negotiate a transport sponsorship arrangement and to conduct a full tendering procedure.

Form of agreement

I noted that the contractual arrangement or agreement between the Department and the service provider took the form of an exchange of letters, comprising a letter of offer from the Department and a letter from the contractor confirming acceptance of the Department's offer. The correspondence did not refer to any terms or conditions relating to the contract. However, the Department did indicate in its letter that it would be in contact thereafter to discuss the terms and operation of the contract. While these matters may have subsequently been discussed no formal written record exists nor did they result in a formal written agreement.

Given the value, scale and nature of the services involved I was concerned that the State's financial and legal interests might not have been adequately protected by a simple exchange of letters. I asked the Accounting Officer why the Department did not follow up the exchange of letters with a formal written contract setting out the terms, obligations and standards required. Such a contract should include conditions regarding the contractor's responsibility for meeting all statutory obligations.

I was informed that the successful tender proposal contained a breakdown of the services to be provided and the terms and conditions of the proposal were acceptable to the Department. At the time, the Department considered that the tender document, together with the performance of those arrangements, gave rise to a contractual relationship that protected the Department. This has been confirmed by legal advisers, including the Chief State Solicitor. The Department accepted and recognised that a formal written contract should have been concluded. However, due to the extraordinary demands of the Presidency, this was not acted on.

He also stated that, determined to learn from this failure, the Department has had a series of meetings with the Chief State Solicitor's Office and its own legal advisers with a view to ensuring that a Departmental wide system is in place to ensure that such a situation could not happen again.

10.2 Automated Passport System

A new automated passport application and production system has recently been installed in the Passport Office of the Department of Foreign Affairs (the Department). I carried out an examination of this project to establish that proper public procurement procedures were applied, to review the planning, implementation, and management of the project and to compare progress against plans in terms of costs and implementation timetable.

Background

By the late 1990s, the systems in the Passport Office for processing applications were in urgent need of replacement. The technology was obsolete and in some cases no longer supported by the manufacturers. The volume of passport applications had grown to the point where the system was overloaded, frequently breaking down and in danger of collapse. The Department was concerned that it was not in a position to provide the high level of service that citizens had a right to expect and that, in a worst-case scenario, it might even be unable to issue travel documents in a timely manner to applicants.

Late in 1998 the Department commissioned consultants to review the passport system. The terms of reference were to

- evaluate the current passport system and identify those aspects that should be retained and, where necessary, improved
- research what was available or being developed in the field of automated passport systems (APS) on the basis of technical factors
- report to the Department with a set of recommendations covering design, specifications and projected costs for the optimum automated system capable of interfacing with those parts of the existing system already identified for retention and/or improvement.

The main benefits of an APS foreseen at that time by the Department were

- a reduction in staffing levels
- more secure passports produced more quickly
- discontinuance of the issue of less secure handwritten passports at diplomatic missions.

Recommended Replacement System

The consultants recommended the adoption of an automated system which would provide for

- electronic data capture
- verification of entitlement to passport
- production of passports
- a workflow system to link the component parts
- administrative functions such as management reports, stock control and payments.

The report stated that no off the shelf system was available to meet all the Department's needs. Seven different options were costed and specified, based on combinations of different data capture and production technologies, in both centralised and decentralised configurations. The report recommended that the Department take advantage of new technology to produce a higher quality passport with improved security features. The cost of these solutions was estimated at between €2.84 million and €6.47 million. The report was drawn up on the assumption that passport applications would be of the order of 350,000 per annum.

The same consultants were re-engaged in 2000 to make a firm and final recommendation regarding the most appropriate technologies to choose. They were also required to develop a high-level technical architecture and implementation plan that would enable the Passport Office to rapidly move to design, build and deploy the new systems, processes and staff structure.

The consultants' report recommended a system with an estimated overall cost of €13,559,000. This cost included the purchase of hardware and software and consulting costs for design, development and deployment of the system. The report assumed that passport issues would reach 1,000,000 within 5 years and that the maximum daily issue figure would be 7,000.

Procurement of New System

In 2001 a project team was established to manage the procurement and implementation of the new APS. The tender process used was the open procedure as defined in EU Public Procurement Directives. The Department engaged a firm of business advisers to assist in drafting the request for tender (RFT) and subsequent tender evaluation. The RFT was issued in August 2001 with a closing date in October 2001. Six tenders were received. One of these was subsequently eliminated, as it did not adequately demonstrate an ability to meet the requirements set out in the RFT.

A tender evaluation committee drew up evaluation criteria and a marking system. The heaviest weighting (56%) was given to the ability to meet the functional requirements. A weighting of 2% was given to cost.

The committee short-listed three bidders for further consideration. Each was invited to make a presentation and to attend a question and answer session and subsequently to resubmit detailed costings in response to a clarification notice issued by the evaluation committee. This notice requested the three bidders to supply a fixed price quotation for all aspects of the project. The RFT had previously stated that a fixed price tender was desired. Costing clarifications were submitted, in November 2001 and in January 2002, by one of the three bidders only.

The Department met this bidder in January 2002 and in the course of the meeting sought further clarification of costs. The bidder indicated a willingness to give a fixed price for phases 1 and 2 of the project and to identify areas of phases 3 and 4 for which it would be prepared to fix a price. It was also guaranteed that the price for the remainder of the project would not vary by more than 10%.

In price terms the preferred bidder was ranked second of the three short listed and was over €7 million higher than the lowest tender but significantly cheaper than the third short listed bidder. The lowest price tender was virtually eliminated from consideration after the question and answer session held by the Department. When all evaluation criteria were taken into consideration, the preferred bidder attained a percentage of 68.1%. This was considerably higher than either of the other two short listed tenders. The preferred bidder was a consortium headed, as prime contractor, by the firm of consultants who had prepared the initial strategy plan and conceptual design.

Although there was some uncertainty about the propriety of the manner in which the clarification of costings was pursued, the Secretary General, in May 2002, approved a proposal that, notwithstanding the risks, the Department should continue with the procedure and award the contract to the chosen bidder. In December 2002 a contract was signed with the successful bidder in the sum of €21,819,000. This did not include support and maintenance costs, blank booklet costs, datapage costs or royalties. It did however include datapage redesign costs of €786,500 that were not included in the original estimated cost per the consultants' report.

In response to my enquiries regarding the weightings ascribed in the evaluation the Accounting Officer stated that the RFT was drafted in such a way as to achieve a level playing field that would give all potential bidders the same information about the Department's requirements. The scoring system used to evaluate the tenders against the award criteria was developed in consultation with the business advisers who assisted with the procurement procedure. The Evaluation Committee, with the guidance of the advisers, did not consider that the scoring system conferred any advantage on any bidder.

As regards the uncertainty surrounding the clarification of costings the Accounting Officer accepted that it would have been better to have sought legal advice before the RFT issued.

Costs

Changes in the expected costs of the project occurred in two distinct phases. The first relates to the period between the consultants' report of October 2000 and December 2002 when the contract was signed. In response to my enquiries as to how a system estimated to cost €13,559,000 in October 2000 came to cost €21,819,000 in December 2002 the Accounting Officer explained that the purpose of the October 2000 report was to update the technology evaluation undertaken in the earlier study and to develop a high level plan for a new passport system. The costs in this report were accordingly described as outline costs which would provide a general overview of the cost of developing the new system. The specification in the RFT of the functional requirements for the new system was much more detailed and it was on this basis that the different tenders were submitted. In addition, the October 2000 report did not propose the use of machines for laser perforating passport booklets as this technology was not available at the time. These machines, which considerably enhance the security of the passport booklet, cost €3.87 million.

The evolution of costs in the period October 2000 to December 2004 is set out in Table 24.

Table 24

Non-Recurring Costs			
	Outline Estimate Oct 2000	**Estimate on Signing of Main Contract Dec 2002**	**Outturn Dec 2004**
	€	**€**	**€**
Systems costs — hardware and software and consulting costs	13,559,000	21,820,000	21,820,000
Contract Price Variation Clause	-	-	754,000
Contract Change Notes	-	-	3,576,000
Other	-	-	907,000
Legal Fees	-	47,000	294,000
External Project Management	-	58,000	423,000
Total	**13,559,000**	**21,925,000**	**27,774,000**

Recurring Costs			
	Estimated at Date of Contract	Year One Expenditure	Estimated Future Annual Expenditure
Support and Maintenance	1,840,000	3,820,000	3,000,000
Blank Booklets, Datapages and Royalties	-	3,700,000	4,760,000
Total	**1,840,000**	**7,520,000**	**7,760,000**

In response to my enquiries the Accounting Officer gave the following explanations for the increased costs in the two years ended 31 December 2004.

Non-Recurring Costs

The contract signed provided for a variation of up to 10% on the cost of phase 2 and certain costs of phases 3 and 4 if it turned out that the contractor's understanding of the project differed from what was originally envisaged. In the course of the design of the new system in phase 1, a number of areas were identified where it was considered that the functionality of the new system could be enhanced. This required additional design and development work and testing on the part of the contractors. The Department accepted these extra costs on the basis of an assessment by the project management consultants that they were reasonable.

The contract also provided for change variation procedures that were formalised by the signing by both parties of contract change notes (CCNs). It was accepted from the beginning of the project that it was likely that additional requirements would emerge from the design phase that would give rise to extra costs. All of the CCNs were considered to be essential enhancements of the original project that were worth acquiring. In the course of the project twenty six CCNs were agreed and signed with a total cost in excess of €3.57 million. The largest of these was for approximately €1.45 million in respect of hardware and software to allow implementation of the APS in diplomatic missions abroad. Another CCN signed was to allow implementation of the APS in the London embassy and the Cork passport office.

While the original concept underlying the RFT was that passport production would be centralised in Dublin it was decided in the course of the project that, because of the volumes of applications handled by Cork and London, it would be more efficient and more reliable to install the full APS system – up to the point of passport production - in those offices. Furthermore, it was concluded that a contingency system would be required in the public offices in Dublin and Cork to provide a fallback in case of a system failure that interrupted passport production. To cover all of these situations, it was decided that the emergency passport module would be an essential requirement.

Recurring Costs

The original tender costed support and maintenance at €1.84 million per annum. However the Department is currently in the process of signing a separate contract for the provision of support and maintenance at a cost of €3.82 million in year one with an option for years two and three at a cost of €3 million. I was informed that the original proposal envisaged an arrangement whereby the Department would make the initial diagnosis of a fault, the resolution of which would then be coordinated or addressed by the contractor. The Department would have had to provide a cadre of expert staff for this purpose and this would have been difficult. The support and maintenance contract now agreed provides for a much broader set of activities and assumes no expert input by the Department in relation to the APS.

The contract also provided for the exclusive purchase of blank passport booklets and datapages from the contractor and the payment to the contractor of a royalty for each passport issued. These costs increase in line with the consumer price index as provided for in the contract. Expenditure to 31 December 2004 amounted to €3.7 million. The estimated annual total of these costs, based on a production level of 650,000 passports, is approximately €4.76 million.

Legal Fees

The Department requested tenders in January 2002 from a limited number of firms for legal services. These services were for assistance in drawing up the terms of engagement and a contract for the provision of the APS. The firm that provided the lowest quotation was engaged in February 2002 by way of an exchange of letters. This did not specify a number of days for which the advice was required. However, in correspondence the firm estimated that its total professional fees might amount to €41,000 - €47,000.

In response to my enquiries as to why legal costs had risen to €294,238 the Accounting Officer stated that the quotation of €47,000 was based on a very preliminary estimate of the work involved in drawing up a draft contract. In the event it had been necessary to devote a substantial amount of additional time to an examination of the procurement procedure and the negotiation of the contract proved much more difficult and lengthy than originally envisaged. This was partly because of the size and complexity of the project and partly because the Department was dealing with a consortium consisting of a group of companies and not a single supplier. He stated that the advantage from the Department's point of view of devoting considerable resources to the drafting and negotiation of the contract was that it was able to secure more onerous warranties and obligations from the contractor in relation to the performance of the contract than were provided for in the RFT.

External Project Management

It was estimated in the RFT that a minimum of forty days assistance would be required for project management. The contract was intended to take the form of a draw down of services on a daily basis. Depending on the particular phase of the project, it was anticipated that assistance would be required one day per fortnight or three weeks over the duration of the contract. A fixed price per service day was required. The assignment was awarded following an open competition. The per diem rate varied between €480 and €1,450 depending on the particular consultant used. At the time of audit some €423,000 had been paid for these services that, at the maximum rate (€1,450), would represent some two hundred and ninety days compared to the minimum forty days envisaged in the RFT. As I was concerned by the extent of the increase in these costs I asked the Accounting Officer for an explanation.

The Accounting Officer stated that it was impossible to estimate in advance what the project management costs would be. Initially, it was assumed that one day's consultancy a fortnight would suffice. However, it became clear early on that the size and complexity of the project were such that much more extensive support was required. In addition, it became necessary to obtain specialist support for User Acceptance Testing to ensure that the system would fully meet requirements. This involved significant additional expertise being brought in as provided for in the contract and this accounted for almost three-quarters of the total costs. This was a critical stage in the project and expert input was essential to enable the Department to satisfy itself that the system, as delivered by the contractor, performed in accordance with the specifications. The Department was satisfied that there was no alternative to incurring these costs. Without this support, it would not have had the expertise to manage the contract prudently and effectively. The advice received in this context also enabled it to limit the number and cost of CCNs.

Implementation Timetable

In response to my enquiries concerning delays in meeting the anticipated delivery dates the Accounting Officer informed me that when the project began in January 2003 it was expected that it would be ready for implementation in May/June 2004. However the Department was concerned that the implementation of the new system should not impact negatively on the EU Presidency or on the operation of the Passport Office during the busy season and, accordingly, it was decided that, if the system was delivered on schedule, implementation would be deferred until after the peak season in the Passport Office i.e. until September 2004. It was also decided, in order to minimise risk, to phase the implementation by commencing the passport production facility in Balbriggan and then moving on to the passport office in Molesworth Street after an interval of a number of weeks. In the event, problems with the development and testing of the system delayed its initial implementation until the end of November 2004 in Balbriggan. Molesworth Street went live in January 2005.

Subsequent teething problems with the system led to a decision to defer the further implementation in Cork, London and the missions until the autumn of 2005, i.e. after the peak season. It is now expected that this will be implemented by the end of this year.

Cost Benefit

The realisation of staff savings was one of the Department's objectives in undertaking this project. The Evaluation Committee had also recommended that a cost/benefit analysis of the financial impact of the successful tender be carried out. I noted that this recommendation had not been implemented and asked how, in the absence of such an analysis, the Department could establish that the anticipated benefits in terms of cost savings and administrative efficiencies would be realised.

I was informed that the Department had sought a proposal for a cost/benefit analysis from the business advisers who were advising on the procurement procedure. They advised that there were many unknown quantities and that significant assumptions would be required on which to base future costings. They also noted that it would be extremely difficult to quantify, in monetary terms, the benefits of having a more secure passport booklet or to estimate the potential staff savings until the design of the new system had been defined. Taking these constraints into account, it was concluded that it would not be a useful exercise to carry out a cost/benefit analysis at that stage.

Notwithstanding this explanation as to why it was considered inopportune to undertake a cost/benefit analysis at the time of the procurement I made enquiries as to the savings made or envisaged in the level of staffing that might be attributed to the implementation of the APS and as regards the arrangements in place to monitor its performance in terms of output volumes, turnaround times and cost savings.

On the issue of staffing the Accounting Officer replied that one of the benefits foreseen in 1998 of an APS was the reduction of staffing levels by the removal of the labour intensive aspects of the old system. This has been achieved in the data entry and production stages that have been largely automated and require fewer staff to operate than the old system for the same number of passport applications. On the other hand, the constantly growing demand for passports has led to an overall increase in the number of staff, particularly in the area of entitlement checking i.e. verifying that applicants are entitled to receive a passport, an area that requires human evaluation and judgment and cannot be fully automated. In 2005 38% more passports would be issued than in 2001 when the RFT for the new system was issued and 83% more than in 1998 when the new system was first mooted. Furthermore, for risk management purposes, it was necessary to have two production centres, Balbriggan and Molesworth Street, where previously

there was only one. This inevitably introduced a certain duplication of staff that reduced the potential for staff savings.

He also informed me that the new system incorporates an extensive reporting system designed to provide comprehensive management information. This will provide detailed information on output volumes, turnaround times, productivity levels, efficiencies and breakdowns of applications by age, gender and location.

Chapter 11

Department of Communications, Marine and Natural Resources

11.1 MediaLab Europe

Background

MediaLabEurope (MLE) was established in May 2000 as a University level research and education centre to specialise in telecommunications and information and multimedia technologies, including the Internet and digital commerce. Contractual arrangements were outlined in a series of collaborative agreements between the Government, Massachusetts Institute of Technology (MIT), and MLE. It was envisaged that MLE would become self-sustaining within the ten-year timeframe of the agreements. This was to be achieved with the initial provision of Exchequer funding and subsequently by raising sponsorship and other income. Payments totalling €24.9 million and €10.6 million were made from the Exchequer to MLE and MIT respectively between 2000 and 2003. In addition the State leased property that had cost €22.5 million to MLE at a nominal rent and undertook to pay €1.27 million per annum for seven years to the Higher Education Authority (HEA) in respect of collaborative research projects between MLE and Irish universities. Table 25 shows the flow of funds over the years 2000 to 2003.

Table 25

Year	MLE €m	MIT €m
2000	8.4	9.4
2001	10.2	1.2
2002	5.7	-
2003	0.6	-
Total	€24.9m	€10.6m

Project Evaluation

The Department of the Taoiseach assumed initial responsibility for the management of the project. Responsibility transferred to the Department of Public Enterprise in May 2001 and to the Department of Communications, Marine and Natural Resources in June 2002. A Task Force chaired by the Department of the Taoiseach and comprising representatives of the Departments of Finance, Enterprise, Trade and Employment, Education and Science, Public Enterprise, the Office of Public Works and the agencies IDA Ireland, Enterprise Ireland, Forfás and the HEA oversaw the process which led to the signing of a Memorandum of Understanding in December 1999.

Concerns expressed by Task Force members in their consideration of the MIT proposal included

- The high cost to be borne by the Exchequer
- The disproportionate risk being carried by the Exchequer
- The minimal exposure of MIT which would not provide any guarantee in the event of project under-performance or failure
- The uncertainty regarding the replication in Europe of the US model, particularly in the area of sponsorship income
- The perceived over-optimistic financial targets with MLE projected to be self-financing within a timescale not experienced elsewhere
- The lack of clarity regarding the exact work and output of MLE, leading to doubts over whether the project would meet Ireland's strategic needs or those of MIT

- The absence of any in-depth evaluation which would establish the credibility of, and justification for, the project
- The degree to which the success of the project relied on the personal commitment of key personnel and the corporate commitment of MIT.

In the course of the project evaluation the financial statements of MITML (MIT's research laboratory based in Boston) for a period of three years were sought. There was no evidence available in Departmental papers that these were ever received.

In 2000 the Department of the Taoiseach stated that, as regards the financial issues and balance of risk, the terms of the arrangements had been the subject of detailed negotiations and that MIT believed that its reputation would be enormously damaged if MLE failed. Key MIT personnel had indicated that between 30% and 50% of their time and energy would be given to MLE. The Department of the Taoiseach also stated that the objectives of MLE made clear what the overall areas of activity would be. There would be co-operation between MIT and MLE in selecting areas of work and a proposed Liaison Committee would provide a means for Government to have influence, if necessary. The multimedia village environment would further shape the overall character of MLE and its activities.

Following an approach from the Department of the Taoiseach**,** a respected international consultant reviewed the MIT proposal. While no written report appears to have been received, his views are recorded in Departmental papers by way of reports of meetings and telephone conversations in July and August 1999. These indicate that he considered that MIT, with its unrivalled international reputation, was uniquely placed to establish a facility on the lines proposed. He felt that the project would be an important anchor for a strategy to position Ireland as a location for this expanding industry. He did not consider the detail of the proposed financial arrangements to be very important. While representing a premium of about 80% on providing an equivalent number of places in a third level setting, resources sought from the State would, in his opinion, be money well spent, given the direct and indirect benefits that would arise. This was conditional upon

- MIT and MLE being equal partners
- MLE securing a clear brand identification with MIT
- The guaranteed ongoing substantial commitment of key MIT personnel
- Access to MIT for MLE staff and students
- Clear agreements covering fundraising from the private sector – fundamentally a shared MIT/MLE approach to raising funds from a common pool of sponsors
- Partnership arrangements between Irish universities and MLE.

Following negotiations, a series of collaborative agreements involving the Government, MIT and MLE was signed in May 2000. The core undertakings by the parties were:

Government

- provide funding of €24.9 million to MLE and €10.6 million to MIT
- provide suitable premises to MLE at a nominal rent

- pay €1.27 million per annum for seven years to the HEA in respect of collaborative research projects between MLE and Irish universities

MIT

- provide management expertise and technical support
- provide access to intellectual property rights
- grant right of use of the MIT brand
- guarantee exclusivity regarding the location of any similar venture in Europe
- secure corporate sponsorship and private contributions for MLE

MLE

- make further payments totalling €11.3 million to MIT in respect of MIT's involvement in joint research programmes
- pay MIT a percentage of sponsorship moneys which it received from year three onwards.

A Liaison Committee, consisting mainly of Task Force members, was set up under the agreements to deal with policy issues arising during their implementation.

Addressing the Risks

In light of the MLE going into voluntary liquidation in February 2005, I asked the Accounting Officer if he was satisfied that an ex-ante evaluation commensurate with the scale and nature of the MLE project was carried out and, in particular, how the specific concerns expressed by members of the Task Force, were addressed in the agreements concluded

He informed me that the MLE model represented a unique and innovative approach in the area of digital content R&D that played a key role in positioning Ireland in the global digital media industry, in line with the goal of Ireland's long-term economic development as a knowledge-based economy. He pointed out that, at the time the project was being considered, the ICT sector was expanding rapidly and digital media was seen as a key high-growth segment. The digital media market is still a strategically important market for Ireland in which to establish an enterprise presence.

Taking account of the significant potential benefits to Ireland, he stressed that the decision-making process, itself, which addressed the issue of whether to invest in MLE, should not have been excessively risk-averse and, at the same time, should have continued to emphasise the attractiveness of Ireland as a location for high-value, knowledge intensive economic activities. Public policy that is unduly conservative and reluctant to try innovative approaches to support economic progress nonetheless incurs an enormous, albeit unseen, opportunity cost in terms of economic development forgone.

With this in mind, he felt it was clear that the decision to invest in the MLE concept was made in the light of identified risks, which were set out by the Task Force. The innovative nature of the MLE approach meant that existing benchmarks were of limited value when considering the proposal. The advice received was positively supportive of the initiative subject to particular approaches being taken.

However, the unprecedented global downturn in the ICT industry since 2000 undermined the MediaLab concept at an early stage of development. This dramatic reduction in research by industry had a severe impact on MLE's ability to reach a critical mass of sponsorship. It subsequently came to light that the MIT MediaLab, the role model for MLE, is not self-financing in this new industry climate. Despite the downturn in the ICT sector worldwide, he considered that Ireland fared better than most and the sector has improved since. He stated that the Digital Hub itself has been hugely successful in attracting companies and MLE has been a contributor to that.

In acknowledging that the Task Force chaired by the Department of the Taoiseach did raise some concerns, he informed me that it was considered that, conditional on MIT's full commitment, the project had significant potential. A number of these concerns, such as costs, financial projections and project risks, impacted on the making of a decision by the Government on whether to proceed or not. The agreements, themselves, did not set out to address the management of the project *per se*. The concerns of the State relating to the management and implementation of the project were therefore addressed through the Liaison Committee on an on-going basis.

Project Monitoring

The Liaison Committee met for the first time in September 2000 and regularly thereafter.

The Department of the Taoiseach, in November and December 2000, outlined a reporting framework for MLE. This comprised annual budget and accounts, together with a quarterly report of outturns, both financial and non-financial, as measured against projected figures.

In general, MLE submitted the required information up to the end of 2003, though it was often late and regularly led to Liaison Committee demands for further information. However audited accounts for 2003 and quarterly reports for quarters two, three and four of 2004 do not appear to have been received.

MLE itself commissioned two external reviews in late 2001 and early 2002. These were forwarded to the Department and reviewed prior to being returned to the company. As copies were not retained these were not available for audit inspection. MLE also informed the Department in April 2003 that it was conducting a review of its relationship with MIT. This was not available either.

Liaison Committee Sub-Group Activity

As a result of concerns over MLE projections for years 2001 to 2005, a financial sub-group of the Liaison Committee was formed in November 2001 to review MLE performance and to establish an early warning system for the Liaison Committee regarding potential financial problems. The sub-group immediately questioned the basis of MLE projections, including those relating to sponsorship and other income, on which the success of the project greatly depended. Subsequent reviews highlighted MLE's failure to raise the required level of sponsorship and other income and the effects of the consequent cutbacks in expenditure. As early as December 2001, the sub-group posted warnings regarding the potential fallout in the event of shortfalls in sponsorship and other income, who would underwrite such deficits, and indeed, the viability of the project if downsized. In January 2002 the sub-group reported difficulty in accepting that MLE revenue targets of €49.3 million for 2002 to 2005 were attainable, and predicted a shortfall of between €10.1 million and €15.2 million for the period. These misgivings were repeatedly expressed throughout 2002 and were borne out by MLE results for that year - €2.7 million sponsorship and other income received as against an amount of €6.9 million projected in December 2001. The sub-group concluded that the level of shortfall in such a narrow forecasting period, fifteen months, undermined confidence in MLE submissions. In October 2003 and April 2004 it repeated concerns about the

accuracy of financial information emanating from MLE, all the while highlighting the seriousness of MLE's situation.

The Department wrote to MLE in October 2003 requesting its views on whether MIT was discharging its obligations and questioning the financial sustainability of MLE. No reply appears to have been received.

On foot of December 2003 returns showing sponsorship and other income received of €1.9 million against a projected €3.8 million, the sub-group carried out a Status of Business review in April 2004. The review

- noted MLE's failure to achieve any of the income projections contained in its budgets from its establishment to 2004
- predicted that MLE cash reserves would run out in early 2005
- concluded that the time lag between initial start-up and the successful generation of sponsorship and other income to a level necessary to create a viable entity was far greater than originally imagined
- stated that, while the Exchequer was the main funding source for MLE, the Board was under effective MIT control and decisions were taken without reference to the Exchequer
- noted that substantial severance payments had been made to executives at a time of serious cash constraints
- concluded that the existing MLE model was patently not viable.

Review of MLE's Strategic Plan 2004

In response to a request in February 2004 from the Liaison Committee, MLE prepared a Strategic Plan.

The plan, which was received in May 2004, acknowledged the shortfall in corporate revenue and sought additional Exchequer funding of €9 million. The Department's initial assessment of the plan was that it appeared to be predicated on a level of performance not yet seen from MLE. An action timetable was drawn up pending a review of the plan and MLE performance to date by consultants engaged by the Department.

The review carried out in June 2004, concluded that

- MLE would run out of cash in 2005 without further funding
- MLE had failed to meet any of the income forecasts contained in the original ten year indicative projections and in the budgets set out at the start of 2002 and 2003.
- The plan envisaged a further funding requirement of €9m for MLE to reach long-term sustainability. Failure to achieve any of the assumptions underlying the plan could result in a funding requirement significantly greater than this.
- No operating surplus was forecast until 2009
- The forecast growth in operating cash inflows appeared unrealistically high

- The plan provided limited information on cost assumptions and how they incorporated many of the future activities identified
- Before providing any new funding to MLE the Department should give very careful consideration to the likely benefits, and the value for money, of such new funding and the sustainability of MLE in its current form..

Performance Review — September 2004

The Department commissioned an assessment of MLE's performance towards achieving its founding mission and objectives. This exercise was carried out in September 2004 by a consultant and was based on performance indicators supplied by MLE and high-level interviews.

MLE was considered to be a unique establishment, being different to the mainstream research and innovation infrastructure existing in Ireland. To best address the performance of MLE in relation to the creation of new knowledge, and the economic and social impact of the investment, indicators derived from its founding objectives were used. The study found that the evidence available suggested that the MIT approach to fundraising and sponsorship could not be replicated in the Irish environment. It concluded that MLE was not sustainable in its current form without significant and continued Exchequer funding.

The study assessed MLE performance against the following founding objectives

- Establishing Scientific and Technological Leadership
- Stimulating Increased Research and Development Investment
- Attracting High Quality Inward Investment and Human Capital
- Supporting Enterprise Development
- Supporting High Quality Human Capital Formation
- Collaborating with Institutions and Development Agencies
- Providing a Forum for International Exchange and Discussion.

Consultant's Findings

Working closely with its MIT connections, it was expected that MLE would fast track the build up of internet and digital media research and innovation capabilities and quickly establish an international scientific reputation for Ireland in this sector. However the consultant found that the scientific output of the laboratory could only be described as dismal with just 24 publications in international scientific literature since establishment. Productivity appeared to be very low – 15 refereed papers from 172 person years of research. Assuming MLE was not motivated towards publication of its work, it was difficult to see what alternative path towards international recognition in the world of science and technology was available or was being pursued by MLE.

It was intended that MLE would act as a stimulus for investment in R&D, attracting high levels of commercial sponsorship and winning research grants and contracts, nationally and internationally. Only 12 sponsorship agreements valued at €7 million were signed. For a laboratory of its size, and with its prestigious brand backing, this appeared to be a relatively poor outcome. There was virtually no research

grant or contract income and it appeared none was being sought. Given the weakness of the sponsorship model in Ireland, it was difficult to understand why alternative sources of funding were not being more vigorously pursued.

It was expected that the MLE presence would help win additional high quality foreign investment and high skill enterprise for Ireland as well as attracting mobile, high quality human capital. However the impact of MLE under this objective appeared to be quite marginal. The company appeared to be of only peripheral value in the drive for foreign investment.

It was expected that MLE would strengthen the prospects for emerging indigenous companies in digital media as well as providing a source for spin-offs and new start-ups emanating from the laboratory and its faculty. It was also hoped that MLE would engage Irish small and medium sized enterprise in its work. The study found that MLE's activities appeared to be having little or no impact on the development of existing indigenous enterprise or on the stimulation of new technology based start-ups or spin-offs from its research. There appeared to have been no collaborative projects of any kind or technology transfer agreements with either indigenous or multinational companies. There was little evidence of engagement with small firms in the Digital Hub with no migration of any MLE project into the Digital Hub and no immediate prospect of that happening.

MLE was expected to help in the training of Irish and European graduates and post graduates by providing research experience and formal academic qualifications with the MIT imprimatur. The laboratory was also expected to contribute to the teaching capabilities of Irish higher education institutions. However MLE appeared to be making little more than a token contribution to this objective with no appreciable engagement in education and training programmes of Irish third level institutions. Of serious concern was the lack of a formal degree-granting arrangement with MIT. An MIT based Masters programme was due to be introduced for the first time in 2004. It had been anticipated that the attraction of the MIT connection would bring in top students, nationally and internationally, to the laboratory.

It was expected that MLE would work co-operatively with development agencies and universities and other educational institutions in Ireland. Apart from collaboration under the HEA-funded research scheme with individual researchers in the universities, there was little evidence that MLE engaged in any significant way with either educational institutions or development agencies.

The ambition was that MLE would provide an attractive conference site that would help to bring together creative thinkers and innovators from around the world. Only eleven MLE international conferences (non-research) were held in the period under review.

Consultant's Conclusions

The consultant found that, after significant investment and more than four years of operation, the potential of this project seemed to be very far from realisation. The aggregate picture suggested that MLE was making very poor progress. The contribution of MLE in relation to its founding objectives appeared to be zero or very close to it, with little hope that it would meet its commitments in respect of these, even in the long term. The quantitative indicators pointed, in the consultant's opinion, to a flawed and largely failed entity in urgent need of remedial attention. Possible reasons underlying the laboratory's difficulties were the inappropriateness of the business model, management and governance failures and staff morale and motivation It was possible that the founding objectives were too ambitious and unrealistic in scope. It was expecting too much to have a self-funding operation at MLE in three years. As far as the Digital Hub was concerned, MLE's presence was felt to have a crucial role to play in driving ambitions for development of the Liberties area and the creation of Dublin's media zone. As indicated, MLE's

contribution to these objectives had been marginal. The study also noted a negative perception regarding the quality of Board governance at MLE, including the frequency of, and attendance at, Board meetings.

Having regard to the findings of these reviews I asked the Accounting Officer if he was satisfied that the structures and arrangements put in place to oversee and monitor MLE were effective.

He replied that, in the first instance, the Chairman and the Board have responsibility for the effective and proper management of a company. The corporate governance model of MLE was unique in that the Board comprised three MIT nominations, three Government nominations and three joint nominations with the Chair being held by MIT. He pointed out that MLE was a unique arrangement based on a not-for-profit company with no shareholders and, as such, the more common governance arrangements of a semi-state commercial body would not have been appropriate and, therefore, did not apply. Oversight of MLE by the Government was the function of the Liaison Committee. The oversight role of the Liaison Committee was circumscribed by the agreements in place between the Government and MLE. In this context, there were limited actions that could be taken under the agreement but the Liaison Committee did monitor the financial performance of MLE effectively and, on foot of this, it communicated its views and sought further information and clarification from MLE. As a result of this oversight role, the Liaison Committee requested a Strategic Plan from MLE in February 2004 when it became clear that it was not performing adequately. This on-going monitoring by the Liaison Committee led in turn to a review of the business status of MLE and ultimately to the decision not to provide further funding.

Given that a key contribution from MIT related to securing corporate sponsorship and private contributions for MLE I also asked the Accounting Officer if any consideration was given to linking payments to MIT to the achievement of sponsorship targets as set out in the Memorandum of Understanding and specific deliverables.

He informed me that there is no evidence that consideration was given to linking payments to MIT to achievement of sponsorship targets. He stated that linkage to performance must be carefully considered in the early stage set-up of an entity in order to facilitate it reaching sustainability. Furthermore, the selection of performance criteria, which are based on the performance of an on-going, established entity, could be damaging in this start-up context. However, in the review that the Department undertook, and subsequent negotiations with MIT in the latter half of 2004, the linking of payments to specific deliverables was a key condition of a revised agreement.

MLE Closure

At meetings with MLE and MIT during June and July 2004 the Department conveyed its views that the business plan was low on substance and high on expectation and that MLE had produced no evidence as to how expected growth would translate into greatly increased sponsorship. MLE confirmed that cash would be exhausted by February 2005, that it had introduced pay freezes and had corrected ineffective expenditure, and cited, *inter alia*, recent changes in MLE management and overall improvements in the economy as the basis for strategic plan figures.

The Department

- expressed the view that Ireland had not received what it had originally expected from the contracts entered into
- asserted that MIT had not delivered on all its obligations under the contracts

- stated that there was a consistent feedback regarding a lack of engagement by MLE with the university sector
- argued that the lack of educational qualifications such as Masters and PhDs meant that MLE had become a paid work experience for students
- pointed out that MIT had continued to draw down payments from MLE despite the latter's serious financial situation
- stated that questions had been raised about the management and organisational ability at MLE.

Departmental papers indicate that MIT

- accepted that the original model for MLE was deeply flawed
- accepted that the initial business plan had failed
- accepted that MLE in its current form was unsustainable
- stated that as a freestanding activity, pure non-directed research was not viable
- would not defend the structures, the management or the way of doing business at MLE
- explained that MIT paid its faculty staff working at MITML.

However MIT re-emphasised its commitment to MLE.

The Department expressed concern at the revelation that MIT had paid its faculty staff working at MITML as the model that was sold to the Government was one that purported to be self-financing and it was the uniqueness of the model that helped get the third level institutions in Ireland reluctantly on board. The Department also asserted that it was now clear that, at the time of the agreements, MIT did not have the agreement of staff to offer their services to MLE and that, consequently, MLE had to pay for many of these fellowships on a consultancy basis.

With agreement on both sides that MLE could not continue in its current format, negotiations commenced regarding a restructured entity as a university-based research and innovation laboratory. MIT would not consider the repayment of any portion of the moneys advanced to it under the original agreements. The Department suggested a structure that altered unsatisfactory elements of the existing MLE. These centred on the areas of governance and the need for more specific commitment to academic awards and finance. The proposal did envisage further Exchequer funding.

Ultimately, negotiations failed with MIT unwilling to accept the Government terms. The Department informed MLE that it was unwilling to advance further funding and, in January 2005, it was announced that MLE would go into voluntary liquidation. I have been informed that the liquidation will be ongoing until January or February 2006. It is considered likely that, in addition to equipment, there will be a cash surplus of approximately €300,000 after liquidation. Under the terms of the agreements, this will be used for charitable, scientific or educational purposes and could be made available to the proposed National Digital Research Centre.

Compliance with Collaborative Agreements

In March 2004, a review of compliance with the agreements was carried out at the request of the Secretary General. It found that the Government had complied in the areas of finance, property and the Liaison

Committee. It concluded in regard to degree-granting programmes that, aside from collaborative projects, progress on formal academic linkages with Irish universities had been slow. In respect of project review mechanisms, which allowed for changes in MLE funding arrangements in certain circumstances, it concluded that, while MLE had experienced a significant shortfall in revenue, it appeared to have adjusted its operating and capital budgets to take account of this, thus complying with the agreement.

The review found that, aside from the slow progress regarding degree-granting programmes, MLE had complied with the agreements with the exception of the late submission to the Department of required reports and documentation.

In respect of MIT's agreements obligations, MLE had confirmed that gifts of €4.4 million, secured by MIT, had been received by it. No share of variable sponsorship, as set out in the agreements, had been received from MIT. MLE also confirmed that MIT had complied with personnel commitments, including the attendance of key personnel for the requisite number of days set down in the agreement.

A legal report, commissioned by the Department in November 2004, concluded that, in the event of a liquidation

- The Government had met its obligations under the agreements and no further obligations to MLE, MIT or any other body could be identified
- State exposure could arise if the Government had issued any letters of comfort or guarantees to banks, employees or third parties who had contracted with MLE. However the Department has confirmed that no such arrangements exist
- The Government was not a member of the company and was not, therefore, exposed to any potential liquidation liabilities.

I asked the Accounting Officer if he was satisfied that MIT had complied with all its obligations under the agreements concluded.

He replied that, in a legal sense, MIT had complied. A key role for MIT was to assist in getting sponsorship and this was not successful. It was disappointing that it was not possible to say that MIT took a more holistic perspective of the project. MIT's unwillingness to help fund the continuation of the project (although not required in the agreements) and its failure to participate financially with the Department in efforts to review and restructure MLE were disappointing since MIT itself supported the Strategic Plan submitted in May 2004.

Other Issues

Governance

A Departmental review of the MLE 2001 accounts highlighted an average salary cost, before PRSI, of €76,000. This was considered quite significant as, while high cost executive directors were included, so too were lower cost research scholars. During its short existence MLE employed four different Chief Executive Officers/ Managing Directors. It is understood that severance packages were agreed for those who left MLE before contract completion.

I asked for details of

- staff numbers employed by MLE by year
- average salary cost per staff member by year
- annual remuneration of each Chief Executive Officer/ Managing Director and
- severance packages agreed in respect of each departing Chief Executive Officer/Managing Director.

The Accounting Officer informed me that the Department has requested this information on a number of occasions but, to date, the Company Secretary has refused to release this information.

Exclusivity

The Spanish Government contacted the Department in 2001 stating that MIT had approached it with a view to setting up a MediaLab in Spain. Following protests from the Department, the proposal appears to have been dropped. MIT denied that they had made any approach and stated that any discussions it had related to a Latin American based laboratory.

A joint MIT/Cambridge University project, partly funded by the UK Government, was not considered to be in breach of MIT/Government agreement in terms of exclusivity of operation.

Positive Outcomes

The Accounting Officer stated that there were some positive aspects to the MLE project. The interdisciplinary and demonstration ethos of MLE attracted significant international interest and the presence of MLE facilitated the growth of the Digital Hub in attracting enterprises to the area. There are approximately 50 companies located in the Digital Hub, employing over 400 people. He stated that at this stage of the Digital Hub's development, it is believed that the termination of MLE will have a negligible impact on the immediate performance of the project. However, the Government remains convinced that a high quality research and development centre, with a clearer commercial focus and educational remit, is necessary for the long-term development of a digital media industry in Ireland and particularly for the cluster based in the Digital Hub.

The collaborative research projects with students from Irish third-level institutions were also very successful. These had been independently reviewed by the HEA on behalf of the Department. The reviews had been positive and the scheme was seen as one of the successful aspects of the MLE project.

There was a very positive social benefit to the local community. There was also an on-going initiative providing children from disadvantaged areas with the opportunity to experience and to learn from digital technology.

He stated that presently it is not possible to ascribe a monetary value to the research work that was being undertaken in MLE at the date of closure. However, this was not to say that the relevant intellectual properties arising from MLE do not have value. At present, Enterprise Ireland is assessing approximately twelve items of intellectual property.

Lessons Learned

The Accounting Officer stated that it is important that the termination of the MLE project should not suggest a public policy that is adverse to innovation and measured risk-taking. Instead, Ireland must continue to work towards a public policy framework that is conducive to innovation and risk-taking in order to ensure that Ireland continues to be an attractive location of new enterprise development, foreign investment, and value-creating industries.

In the context of a project such as MLE, which is fundamentally a concept to promote multi-disciplinary research, development and innovation in this case in the digital media sector, it is clear that appropriate project evaluation is critical. The evaluation process needs to be rigorous. However, an evaluation process must be flexible and relevant where unique and ground-breaking proposals are being considered. In this light, a clear business strategy for the project is necessary in order to test its robustness. All parties should be expected to have some financial commitments in a project and the rewards should be linked to the risks taken.

At a broader level, governance, in terms of accountability, reporting, and strategic decision-taking, is critical. These governance structures should be appropriate to the type of project and while not necessarily a semi-state company governance structure, they should ensure that there is clear accountability and good governance. Finally, performance is central to the delivery of these publicly funded projects and, as such, payments should be linked to particular performance milestones or metrics.

11.2 Fishery Harbour Centres

Failure to prepare Annual Accounts

There are five designated Fishery Harbour Centres in the State – Killybegs, Castletownbere, Rossaveal, Howth and Dunmore East.

Section 4(1) of the Fishery Harbour Centres Act 1968 (the Act) states that the Minister for Communications, Marine and Natural Resources (the Minister) shall manage, control, operate and develop each Fishery Harbour Centre.

Section 8(1) of the Act states that the Minister shall, as respects a Fishery Harbour Centre, cause to be kept, in an approved form, all proper and usual accounts of all moneys received or expended in relation to the Centre. The accounts of the Fishery Harbour Centres are audited by me in accordance with Section 8 of the Act.

The 1999 Income and Expenditure Accounts and Balance Sheets for the five centres were certified by me in January 2003.

My Office raised the question of the lack of accounts for the years 2000 to 2003 with the Department in November 2004 and a schedule was agreed for the production of the outstanding accounts for audit. The Accounting Officer informed me that the principal reason for the delay in the provision of accounts was exceptional pressure on the Department's accounts branch due to changes in the Department's functions during the period. External accountants had been engaged in January 2005 to bring the accounts up to date and draft accounts for the period 2000-2004 were eventually submitted for audit at the end of May 2005.

He was of the view that the installation and roll out of the new financial management package to the Fishery Harbour Centres was providing timely and accurate financial information on the payments side and when fully applied would underpin regular reporting as well as completion of the annual accounts to deadline in the future.

Previous Audit Concerns

Paragraph 28 of my 1999 Annual Report expressed concerns regarding the increase in the level of debtors in the Fishery Harbour Centres over the period 1996 – 1999 and the poor and varying performance of the different Centres in relation to debt collection.

In response to my concerns at the time the Accounting Officer stated that the then current standard procedures for collection were being reviewed with a view to effecting improvements in efficiency. He also stated that steps to improve collection would ensure that available income was maximised and would be accompanied by continued rigorous control of expenditure to ensure the viability of Centres going forward. The position in relation to debt collection was under review and any further action, identified to effect the necessary improvements in the position, would be taken.

Current Audit Concerns

Bearing in mind financial control and governance requirements I sought the views of the Accounting Officer regarding the Department's oversight of the Fishery Harbour Centres in the period 2000 – 2004 and the effectiveness of the collection of Harbour Centre debts.

Accounting Officer's Response

General

The Accounting Officer informed me that the fishing industry had, over the period in question, been going through a very difficult time economically due to declining stocks and, as a consequence, ever more stringent conservation measures. In recent times sharply increasing fuel prices are having a major impact on costs for fishermen. The effect of these factors has been to reduce the volume of landings, the number of active vessels, the volume of in-harbour processing activity and a reduced ability to pay with a consequent increase in bad debts.

He observed that harbours are funded through rents and charges and that charges had not been increased since 1990 and revenues in the early part of the period in question had not kept pace with costs. A significantly increased rate of charge, coupled with the introduction of new charges for services that were previously free, was introduced in 2003. There was strong resistance from the fishing industry to the new and increased charges and the real benefits of the new and increased charges were only really being felt towards the end of the period.

He stated that there was a substantial programme of change and modernisation taking place in relation to structures, roles and responsibilities and work practices and procedures in relation to the management of the harbours generally. It was intended to move at harbour level to a situation where the local Departmental engineer has a much greater and closely defined role in the local management of each individual Harbour Centre as part of his/her responsibility for a geographical area. It was also envisaged that further changes would be implemented as a new integrated fisheries information system and a new financial management package became fully operational.

Response to Specific Queries

- *How did the Department perform its oversight duties for the period 2000 to 2004?*

The Accounting Officer stated that during the period in question there had been considerable difficulties in relation to the filling of Harbour Master vacancies. This had resulted in a more direct hands on approach by the Fishery Harbours Division of the Department. There was day to day interaction relating to routine administration and a programme of regular visits was supplemented by additional specific issue visits. During 2004 the Fishery Harbours Division was restructured to enhance management and oversight of the Fishery Harbour Centres not least because of the continuing vacancies among Harbour Masters. As regards financial oversight the Department's accounts branch exercised some direct functions in relation to the financial processing of payments. On the receipts side the installation of a new accounting system in 2002 enabled receipts/debtors to be better monitored.

- *Was the level of control during the period satisfactory and what specific controls were in place in each Fishery Harbour Centre to ensure*
    - *the correctness of all payments and*

- *the prompt and efficient recovery of all due receipts?*

Based on the information available to him the Accounting Officer said he was satisfied that payments were subject to satisfactory authorisation, control and oversight. He went on to say that Expenditure at the five harbours is broken down into three main categories: Labour, Current Operational Expenditure and Engineering Expenditure both Current and Capital. As regards Labour Expenditure timesheets for industrial workers are certified for payment by supervisors and processed weekly by the Department's Accounts Branch. All Current Expenditure payments arising from the operation of the Fishery Harbour Centres are handled and authorised centrally in Fishery Harbours Division. No major payments are authorised locally. Invoices received are certified at the Fishery Harbour Centre and forwarded to the division for scrutiny, authorisation and processing. Additional staff are being deployed to check invoices and streamline processes. Engineering expenditure, current and capital, is handled by Engineering Division which oversees the execution of necessary works both by the Department's own staff and by contractors. Invoices are approved within the Engineering Division. The Accounting Officer further stated that he was satisfied that controls were adequate to ensure the correctness of all payments but a process of continuous improvement needs to be sustained.

As regards receipts the Accounting Officer stated that Harbour Dues are now calculated locally at 3 Fishery Harbour Centres (Killybegs, Rossaveel and Castletownbere). Harbour dues are calculated in Fishery Harbours Division for 2 Fishery Harbour Centres (Howth and Dunmore East) pending the filling of Harbour Master vacancies. There had been a review of financial procedures and invoices were now being generated on a more timely basis and collection of dues was being more vigorously pursued. However the fully effective operation of these procedures was critically dependent on two factors. Firstly the appointment of Harbour Masters to existing vacancies –- offers of appointment have recently been made by the Public Appointments Service. Secondly the timely provision of fish landing statistics is critical to ensuring the calculation and invoicing of harbour dues. The recently installed Integrated Fisheries Information System is designed to underpin the generation of such data.

- *What progress had been made as regards debt collection?*

The Accounting Officer informed me that external services were engaged in 2001 to assist with collection of accumulated arrears and to design and operate effective debt management procedures. He also said that various campaigns of non-payment had impacted on collection rates over the years.

The Accounting Officer further stated that since 2001 there had been a number of initiatives to enhance recovery. In particular the automation of the systems for issuing invoices and statements in 2002 had been accompanied by telephone follow-up of all outstanding debts. In tandem with this the following debt control procedures had been put in place

- Charges to be paid within 30 days of the date of invoice
- Queries regarding charges to be directed in the first instance to the relevant Harbour Master with direct payment to the Department's Accounts Branch in Castlebar
- Pursuit of outstanding charges and referrals to the Chief State Solicitor for early recovery through the Courts
- The Department reserved the right to withhold services to Fishery Harbour users where there were dues outstanding.

Revised procedures were introduced to report outstanding harbour dues on a six monthly basis and to pursue collection of arrears. In September 2004 all arrears in excess of €10,000 were targeted. The incidence of such arrears had arisen due to a campaign of non-payment by users dissatisfied with the

increased level of charges introduced in 2003. In excess of 90% of targeted arrears was collected in a two month period. The Accounting Officer added that a second exercise is currently underway in relation to arrears in excess of €1,000.

- *What were the actual and relative levels of debt in each harbour centre over the period?*

The Accounting Officer informed me that collection rates show progress on reducing debt levels. For the five centres the collection rate improved from 47% in 1998 to 65% in 2002. There was a dip in the collection rate in 2003 due to the reaction among harbour users to an increase in charges in 2003. However he was confident that the collection rate would improve as the once-off problem that occurred in 2003 passed through the system.

He also provided the detailed information set out in Table 26.

Table 26 Debt Outstanding at Year End in € and Collection as % of Amount Collectable

Year[14]	Killybegs		C'bere		Rossaveal		Howth		Dunmore East		Total	
	€	%	€	%	€	%	€	%	€	%	€	%
1998	457,442	29	164,242	50	28,672	80	118,717	70	111,429	32	880,502	47
1999	227,131	73	175,978	54	32,675	68	106,119	82	117,137	36	659,040	68
2000[15]	182,234	52	89,466	43	38,105	68	151,658	56	106,028	19	567,491	49
2001	207,716	68	89,288	62	68,533	52	276,450	54	95,427	48	737,414	59
2002	191,574	68	102,785	70	86,396	51	184,813	70	116,082	41	681,650	65
2003	435,708	53	152,312	58	111,132	46	324,469	51	134,070	42	1,157,691	51
2004	586,415	62	217,315	62	368,768	21	405,037	55	225,715	32	1,803,250	53

In relation to the foregoing, the Accounting Officer pointed out that

- In the case of 2003, the increased charges took effect in October. However, the amount of increased charges actually collected would be very small resulting in an apparent dip in collection efficiency. Current year collections always lag billings due to delays in assembling landings data.
- Rossaveal income is very dependent on ferry traffic. Increased charges are being resisted and legal action may be necessary to effect collection.
- The poor collection rate in Dunmore East reflects the absence of a Harbour Master.

[14] Figures for 2000-2004 are unaudited

[15] The figures for 2000 are stated after the write off of bad debts of about €250,000.

11.3 Foreshore Leases/Licences

Background

Foreshore is currently regarded as the land and seabed between the line of high water of ordinary or medium tides and the twelve-mile territorial sea limit. It also includes tidal rivers and estuaries. The main governing legislation in this area is the Foreshore Act, 1933. The bulk of the foreshore is State property within the meaning of the State Property Act and ownership lies with the Minister for Finance although there are some parts of the foreshore in private ownership. The Minister for Communications, Marine and Natural Resources (the Minister) administers the State-owned foreshore and the legislative provisions through the foreshore section of the Coastal Zone Management Division.

The Minister may, if it is in the public interest, grant a lease or licence for the use of a section of foreshore. A lease, which is typically for 35 years, generally refers to the erection of a structure on, or the right to the virtually exclusive use of, a section of foreshore. While licences are granted for short term uses of the foreshore, such as horseracing, they are also granted for significant developments such as, for example, pipelines, interconnectors and waste water treatment plant outfalls. Restrictions are placed on the use of foreshore by way of conditions attaching to each lease/licence which address matters such as term, rent payable, reviews and environmental issues.

An internal audit report dated June 2004 prepared for the Department of Communications, Marine and Natural Resources (the Department) indicated that a total of 1,334 leases/licences had been issued as at the end of August 2003. This number had increased marginally by the end of 2004 to 1,384 although the Department states that this would also include a comparatively small number of matters other than leases and licences, such as agreements for the sale of foreshore, and exclude a number of licences that were not assigned reference numbers in earlier years.

Annual receipts in respect of foreshore leases/licences can be substantial. While they amounted to €1.3 million in 2004, amounts in some previous years were higher — in 2002 almost €6 million was collected, primarily due to new major infrastructure projects.

Processing of Applications

Applications received by the Department are initially considered by the engineering, marine survey and sea fisheries control divisions of the Department prior to consultation with a broad range of external bodies including the Department of the Environment, Heritage and Local Government, the Marine Institute and the Central/Regional Fisheries Boards. Public consultation also takes place in virtually all cases. Most cases, including all complex applications are submitted for vetting to the Marine Licence Vetting Committee. A recommendation is made to the Minister in all cases. Under Department of Finance guidelines, issued in 1987, in fixing the rent payable the advice of the Valuation Office should be obtained. For certain developments, standard charges apply. Once the applicant notifies acceptance of the proposed terms, a lease/licence is issued. It is recorded in a database under a unique reference number. However full details of conditions attaching to the lease/licence are not entered. A sealed copy of the lease/licence is held by the Department. Lease/licence holders are obliged to comply with the conditions imposed by the Department. Upon the expiry or surrender of a lease/licence, restoration of the foreshore by the lessee/licensee is mandatory.

Department Records

Electronic foreshore lease/licence records maintained by the Department are not fully comprehensive, resulting in weaknesses that hamper effective management. Leases/licences are recorded on a database but this lacks data such as exact location, specific conditions, review dates etc. that would be contained in a Geographical Inventory System (GIS). However such a system is not currently maintained. The June 2004 internal audit report described the database as inadequate, noted that it did not lend itself to electronic interrogation and recommended that it be replaced. In the absence of a proper database, local office staff, who are best placed to assess compliance, have to request copies of the leases/licences from the Department's headquarters in Dublin where the originals are kept. This works against the systematic review of compliance.

This lack of a comprehensive electronic database, or related systems, is currently being addressed by the Department through a major project being undertaken by its Information Systems Division. Phase 1 of the project will be completed by October 2005 and it is envisaged that the entire system will be fully functional by early 2006. The intention is that the system resulting from this project will give a fully comprehensive database, replacing the existing electronic databases, such as the listing of leases and licences and rent records, that have been developed on an ad-hoc basis over the years. The new system will encompass functions including application processing and financial management and a GIS component.

Review of Cases

Leases issued since 1987 should, in accordance with Department of Finance guidelines, be for a maximum term of 35 years with provision for five yearly or seven yearly reviews unless the prior sanction of the Department of Finance has been obtained. Previously leases were generally issued for a 99 year term[16], some being subject to periodic review. Department records do not automatically trigger cases due for review. Instead, review dates have to be identified and collated manually.

A Departmental report of October 2004 concluded that

- Where cases had been reviewed by the Valuation Office for the period 2001 to 2003 the total value of rent collectable increased from €150,000 to €593,000 — an increase of almost 300%
- Current reviews were substantially in arrears
- The Valuation Office refused to handle review cases between May 2003 and November 2003 and ceased handling review cases between August 2004 and December 2004
- The legal implications of backdating rent reviews were unclear
- Review cases for 2001 were recalled unprocessed from the Valuation Office in March 2004 by the Department due to the passage of time.

Because of delays in the Valuation Office, the Department, in May 2004, sent only the 20 highest rent cases to that office for review. By April 2005 not all of these cases had been processed but of those returned the average increase was of the order of 400%. No cases were referred to the Valuation Office in the first half of 2005.

[16] The Foreshore Acts provide for the issue of leases and licences for periods of up to 99 years.

The Department furnished me with the following information on the extent of rent reviews in recent years.

Table 27

Year	Reviews Due	Reviews Finalised
1998	47	12
1999	66	2
2000	51	-
2001	53	5
2002	65	7
2003	68	6
2004	69	4
2005[17]	38	-

As the failure to review rents in a timely way can lead to a loss of income to the Exchequer I asked the Accounting Officer what remedial action was being taken.

The Accounting Officer acknowledged that there have been delays in the carrying out of rent reviews provided for in foreshore leases. He cited a number of factors that have contributed to this situation, including, in particular, the pressures of other work in the Section and difficulties in obtaining advice on proposed revised rents from the Valuation Office. He stated that the Department recognised the need to address the position as a matter of priority and accordingly is making arrangements for a detailed examination of the situation to be undertaken. The aim will be to address any cases in which a due rent review has not been initiated, or finalised, to date, and to ensure that all reviews are carried out in a timely manner. He further stated that the Department is taking immediate steps to go to tender for an independent body to carry out valuations for all foreshore matters. All outstanding cases will be withdrawn from the Valuation Office and referred to the successful company for immediate appraisal.

Post-Review

If a client does not accept a revised valuation there is a provision for referral to arbitration. I have been informed that, in practice, no cases have been referred to arbitration in the period since 1998. Three requests for arbitration are on hands from lessees at present. Many clients simply continue to pay at the old rate or refuse to pay at all. It appears that the Department does not pursue an enforcement policy in the case of clients who do not accept revised valuations. According to the Department, no leases have ever been suspended or withdrawn as a result.

Valuation Office — Level of Service

The Department has been dissatisfied with the level of service provided by the Valuation Office for some time. Long delays in the provision of valuation advice are common. At a meeting in September 2004, the Valuation Office conceded to the Department that the service provided was not satisfactory, citing the need to concentrate resources on its core statutory function of rateable valuations. It also stated that it could not see any way in which the service could be improved in the foreseeable future.

In view of the comments made on the unsatisfactory nature of the service provided by the Valuation Office I sought the views of that Office's Accounting Officer. In reply he stated that the core business of his Office was the provision of accurate, up-to-date valuations of commercial and industrial properties to

[17] To end June 2005.

ratepayers and rating authorities as laid down by statute. Consequently resources had to be focussed as a priority on the rating valuation service and his Office could not guarantee a satisfactory consultancy service to Government Departments on market value work. For this reason it was agreed with the Department of Finance in September 2001 that the procurement guidelines should be revised to allow freedom of choice to Departments in sourcing market valuation services. All customers were advised by the Valuation Office of its priorities and resource constraints and of the proposed revision of the guidelines.

His Office met with the Department of the Communications, Marine and Natural Resources in September 2004 and again advised of the ongoing problems with service delivery. He concluded by stating that the situation had not changed and his Office will not be in a position to provide a satisfactory consultancy service in the short term.

Monitoring of Compliance with Lease/Licence Conditions

The audit found that the Department does not adopt a proactive role in the monitoring and enforcement of lease/licence conditions. Monitoring, where it does exist, seems to depend on the local knowledge of the Department's officials. In the Offices visited, the existence of copies of leases/licences issued by foreshore section was the exception rather than the rule. Together with the absence of a comprehensive database this makes effective monitoring virtually impossible. When I asked the Accounting Officer if he was satisfied that local offices of the Department were in possession of sufficient information to allow adequate monitoring of conditions attaching to leases/licences he informed me that the foreshore section can make any documentation in relation to a particular lease or licence not held by a local office available immediately to that office on request. The new information systems currently under development will allow local offices electronic access to all relevant records.

The Accounting Officer has informed me that the Department is not in a position at present to undertake comprehensive post-authorisation monitoring of compliance with the terms and conditions of foreshore leases and licences as it is constrained by the limited resources available for work of this nature. Specifically, the Department's Engineering Division, to which it would fall to carry out the inspections essential for monitoring compliance, is multi-tasked and is not, therefore, in a position to undertake systematic post-authorisation compliance inspections on foreshore developments. Consequently, inspections would normally be carried out where specific issues have come to attention, or if a complaint is received. If a report of an inspection by the Engineering Division were to indicate a failure by a lessee or licensee to comply with the terms or conditions of the authorisation, the matter would be referred to the foreshore section for appropriate follow-up action. This might involve correspondence with the lessee/licensee in the first instance, or legal action if there was a failure by the lessee/licensee to address the position. In this connection, the Department is currently engaged with the legal services with a view to instituting legal action for breach of the terms and conditions of a particular lease.

The Department will consider how it might be possible to move towards more structured monitoring of compliance with the terms and conditions of leases and licences, and will consider the role that the new information systems under development at present can play in that regard. However, the nature and extent of any developments in this regard will of necessity be determined by the resources available for the inspectorial work that provides the essential basis for compliance monitoring.

Pursuit for Non-Payment

While the payment of the first year's rent is made in advance, rent due in respect of later years is identified by staff, who then issue the relevant invoice. Reminders are issued approximately every 2 months. Up to four reminders may be issued. My audit indicated that the Department does not initiate legal proceedings

or impose any sanctions in the event of non-payment. The Accounting Officer has informed me that a policy has now been adopted of referring cases to the legal services for appropriate action where rent is not paid. A number of cases have already been sent to the Chief State Solicitor's Office, and a similar approach will be adopted in any other case in which, despite reminders, amounts owed are not paid.

Unauthorised Developments

With very few exceptions, the creation/erection of any structure or the use of or reclamation of any part of the foreshore requires the consent of the Minister by way of a lease or licence issued by him. Audit evidence suggests, however, that unauthorised developments are quite common and an audit of certain local office files noted that 6 such cases had been identified and reported to foreshore section. An audit review, using the results of a coastline helicopter survey undertaken in September 2003, revealed a further 11 unauthorised developments in the same area for which no lease/licence exists. A further audit review of a section of the coastline surveyed indicated many more examples including a significant number of swing moorings.[18]

Unauthorised developments represent a loss of revenue to the State. While the rate to be paid in each case is site specific, the large numbers involved, particularly of swing moorings, means that this loss is potentially significant. It is not clear to what extent the scale of unauthorised development, as identified in the course of the audit, is reflected nationally — it is however, suspected that the number of unauthorised swing moorings alone is in the thousands. The Department has no accurate information on the specific numbers involved. As the Department already has the September 2003 helicopter survey results available to it as well as certain satellite and aerial photographic records of the coastline that clearly show all foreshore developments, a geographical inventory system would enable it to easily identify those for which a lease/licence has and has not been issued.

The Accounting Officer, while accepting that there are many unauthorised swing moorings, pointed to the difficulty of distinguishing between permanent moorings which need a licence and temporary ones which don't. Close physical inspection would normally be required. However, he stated that the Department is currently considering the possibility of having electronic tagging and/or colour coding of authorised moorings to help identify those which are licenced, particularly from aerial surveys. He added that the harbour masters, who charge fees to those using moorings within harbours, were made aware that there was also a requirement to hold a foreshore licence. The feasibility of having both fees collected by harbour masters and the foreshore fees remitted to the Department by them is being examined.

I was informed that the Department is not, as matters stand, in a position to carry out systematic on the ground policing of the foreshore for unauthorised developments in pursuit of its clear policy that only properly authorised developments should take place. In these circumstances, inspections in respect of alleged unauthorised developments are normally carried out when matters come to attention in the context of other work, or in response to complaints and appropriate administrative action taken. If, however, what had been done were considered to be unacceptable, Court proceedings would be instituted seeking to have the development removed. I have been informed that 2 cases are before the Courts at present.

The Accounting Officer also stated that the Department recognises the need for a more structured approach to addressing unauthorised development on the foreshore and believes that the GIS component of the new information systems under development has the potential to offer considerable assistance in this regard if associated with aerial survey and on the ground inspections. It will in the meantime consider

[18] A swing mooring is a single point mooring which is anchored to the seabed and allows a boat to swing around with the tide.

how it might be possible to advance an exercise to correlate the results of the aerial survey referred to with the details of leases and licences that have been granted, and to follow up in respect of any developments undertaken on State foreshore without appropriate authorisation.

Chapter 12

Department of Agriculture and Food

12.1 Damages for Storage of BSE Tallow

Background

I reported in 2001 on a review I had carried out of the Bovine Spongiform Encephalopathy (BSE) eradication programme. Among the main control measures adopted by the Department as part of this programme were procedures for dealing with Specific Risk Material (SRM). SRM is defined in EU legislation as certain parts of the bovine carcase, mainly the brain and spinal column. The measures adopted involved the isolation, staining and direct removal of this material to approved plants for rendering and eventual destruction by incineration.

The control of the collection and rendering of SRM and the storage and destruction of the resultant meat and bone meal (MBM) and tallow was, from an early stage, recognised by the Department as a key anti-BSE measure. The preferred approach was to designate a specific rendering plant to exclusively process all of the SRM generated throughout the State. Having considered a number of applications, the Department approved a rendering plant (the renderer) for this purpose in February 1997. The intention was that this designation would enable the renderer to process the SRM on a commercial basis for the slaughtering sector, without financial assistance from the Exchequer. The receipt of SRM raw material, its processing, and the storage of the resulting MBM and tallow was overseen by the Veterinary Inspectorate of the Department. Its main role was to verify the quantities of SRM received and MBM and tallow dispatched. Ownership of the MBM and tallow remained with the renderer.

In May 1997

- The local Department inspector responsible for the renderer's premises notified the Department that the renderer had filled all its tallow storage tanks and was looking for additional storage. In the absence of storage facilities being found for this tallow, the renderer would have had to cease rendering all SRM.
- The renderer had identified two possible storage premises.
- One of these premises was recommended by the Veterinary Inspectorate.
- The Department issued an approval notice to the renderer in respect of the selected premises (the store).

However, due to the absence at the time of key staff, a licence was not issued to the store owners. At this time, the Department's policy was to inspect and license storage premises in regard to suitability for receipt and holding of MBM and tallow.

An agent on behalf of the renderer negotiated the contract for storage of the SRM tallow. The Department was not a contract party to the storage of tallow at the store in 1997.

The store was used from May 1997 onwards by the renderer under the supervision of the Veterinary Inspectorate. In the following three years over 5,000 tonnes of SRM tallow was sent there. In July 1998 it became necessary for the Department to make a financial contribution for the disposal of the MBM and tallow because of difficulties experienced by the renderer in securing adequate payment from the meat sector for the rendering of the SRM and subsequent disposal of MBM and tallow. As part of an overall agreement reached with the renderer for the disposal of SRM derived MBM and tallow, the Department

took over responsibility for 2,511 tonnes of SRM tallow held in the store. Prior to this the tallow was owned by the renderer.

Legal Case

In February 1999 a dispute arose between the renderer and the store owners that resulted in the initiation of High Court proceedings. The action was taken against the Department and two co-defendants, (the renderer and its agent) by the owners of the store. The plaintiff claimed, at that time, that it had only then been made aware that the material stored was, in fact, derived from SRM.

A High Court case commenced in June 2004. The plaintiff's claim at that time was for €6.5 million in damages — €4 million for destruction of business based on damage to its storage tanks and €2.5m claimed as arrears of storage fees. The rent initially charged for use of the store was €1.27 per week per tonne of tallow stored. However, the store owners sought to increase this rent to €3.17 per week per tonne with effect from 1 March 2000. The Department, on legal advice, paid the increased rate. However, when the plaintiff created legal difficulties with regard to the removal and disposal of the tallow the Department ceased payment of all storage fees in February 2002. These circumstances led to arrears of rent forming part of the Department's ultimate settlement of the case.

The key issue in the case was whether or not the plaintiff had been informed from the outset that the tallow was derived from SRM. The position of the Department was that:

- While it had approved the renderer as the designated SRM processor, it was not a party to the original storage contract concluded by the renderer's agent with the store.
- It was not directly involved in what the store was told by the renderer or its agent.
- It had no control over the description of the material on the delivery dockets which accompanied the tallow being sent for storage.

I have been informed by the Accounting Officer that the Department and its legal team based and built its defence on one critical understanding. This was the understanding given to the Department by the co-defendants, prior to and throughout the duration of the case, that both could clearly and unequivocally establish, to the satisfaction of the court, that the plaintiff was on full notice and absolutely aware, from the first load going into storage, that the tallow was SRM tallow. The co-defendants had no written evidence to establish this fact, so this was a case where ultimately oral evidence was primary and the court would have to weigh up the bona fides and veracity of what was said and by whom.

The fact that the Department had issued formal documented approval of the premises for the storage of SRM was only discovered after the commencement of Court hearings.

Settlement

On day 46 of the case on the conclusion of cross-examination of co-defendants' witnesses, but prior to the commencement of cross-examination of Department witnesses, legal advice from the Department's Senior Counsel recommended that the Department urgently explore the possibility of a settlement of the case. Counsel and the Department were of the clear opinion that their co-defendants had not established sufficient primary knowledge on the part of the plaintiff, to the required degree, that the secondary evidence of the Department's witnesses would copperfasten a successful outcome to the case.

The Department immediately sought and received Department of Finance sanction for a settlement. In December 2004 a settlement in the sum of €3.75 million was signed between the parties and recorded in the High Court. In addition the agreement provided that the Minister would pay the plaintiff's costs. The agreement also provided that the Minister would make an additional payment (€22,000) for the removal of tallow. A separate agreement was recorded in the High Court whereby one of the co-defendants contributed a sum of €1 million to the Minister as its contribution towards the settlement.

In December 2004 this payment was received and the Department paid the agreed settlement sum of €3.75 million.

I have been informed by the Accounting Officer that the plaintiff's costs, to be paid by the Department, have not as yet, been assessed for payment as they had only recently been furnished to the Chief State Solicitors Office. The Department has not yet seen them. The assessment of the plaintiff's costs should be completed shortly. He felt that it would be inappropriate to indicate what the likely fees might be, due to the fact that the matter is currently *sub-judice*. However the Attorney General's Office had paid out a sum of approximately €925,000 to the State's legal team in fees.

Outcome

The outcome of these events, from the Exchequer viewpoint, is that allowing for the contribution of the renderer, net expenditure of approximately €2.75 million was incurred in settling the overall claim, including storage. In addition expenditure of approximately €1 million in respect of State legal costs has been paid and an as yet undetermined amount, remains to be paid in respect of the Plaintiff's legal costs.

12.2 National Beef Assurance Scheme

Background

Following the BSE crisis of 1996, measures were adopted to improve the production and processing conditions of cattle and beef in Ireland and to provide assurances to consumers as to the safety of Irish beef. In order to allay consumer concerns and to safeguard beef markets at home and abroad, the National Beef Assurance Act, 2000, providing for the implementation of a National Beef Assurance Scheme was enacted. The purpose of the scheme is to provide guarantees about the safety of Irish cattle and beef by:

- The development of common high standards of production and processing
- The enforcement of these high standards through a process of registration, inspection and approval
- The enhancement of the animal identification and tracing system.

During 1997, work began on the development of the computerised Cattle Movement Monitoring System (CMMS). The system records all movements of cattle on a central database, i.e. movements through livestock marts, from farmer to farmer, through cattle dealers, to slaughter plants and for live exports. The system is supplemented by the information supplied through calf birth registrations and the issuance of bovine passports. The CMMS was phased in from September 1998 and captures all data on births, movements, deaths and disposals since 1 January 2000.

As well as providing details of the origin, identity and life history of cattle before they enter the human food chain, the database is also being used to provide data to validate payments under livestock premia schemes. In 2004 payments totalling €789 million were made on foot of applications which were subject to verification and validation checks using CMMS data.

Scope of Audit

My examination of expenditure under the National Beef Assurance Scheme included a review of the contractual arrangements between the Department and a private operator for the processing of calf birth registrations and the issue of bovine passports, animal movement permits and on-farm death notifications. It also included a review of procurement procedures for the new Animal Health Computer System.

Calf Birth Registrations and Bovine Passport Issue

The contract for the registration of calf births and the issue of bovine passports has been held by the same service provider since the inception of the CMMS. The service provider successfully re-tendered for the current contract in December 2003.

Invoice Verification

The Department is invoiced monthly by the contractor for the number of calf births registered in the previous month. These registrations are input by the contractor onto its computerised system on foot of notifications received from farmers and herd owners. The data is then downloaded nightly onto the Department's system.

When the contractor's invoice is received staff cross-check the number of registrations claimed with those registered on the CMMS. These should automatically agree as the CMMS reflects what was downloaded from the contractor's system. An amount of €4.4 million was paid to the contractor in 2004 for the registration of calf births and bovine passport issues.

My audit noted that the absence of an independent verification of calf registrations was raised as a serious finding by the Department's Internal Audit Unit in a report in March 2004. The management response at the time was that, until such time as calf birth registration is fully on line as part of the new Animal Identification Movement System, which is intended to succeed the CMMS, there is probably no truly independent mechanism available to verify all invoices in full.

I enquired how the Department satisfies itself that the invoices being submitted by the contractor for payment are accurate. In reply the Accounting Officer stated that the Department is satisfied that there are sufficient validation and control mechanisms in place in regard to the CMMS database.

He stated that calf birth registrations are not accepted onto the CMMS unless the herd number of the applicant is valid, has an active status and has been supplied with a herd identifier. Nor are registrations accepted unless the tag number applied on is valid, the dam is alive in the herd of birth at the time of birth, is over 18 months of age, has not had a calf in the previous 300 days and has matching breed details. Moreover, the CMMS database is an integrated database. All exits, disposals and other movements are validated by reference to the initial calf registration data and act as further verification of the existence of animals. With the exception of brass tagged animals that are not covered by the calf birth registration contract, registered animals may not be removed from the CMMS database unless recorded as slaughtered, exported or dead on farm. Analysis of the database provides no evidence of any anomaly or any imbalance between entries and exits.

In addition, over the past number of years, the Department has supplied herd profiles on a regular basis to all farmers both for Extensification Scheme entitlements and herd reconciliation purposes. The production of these profiles acts as a barometer of the accuracy of the database. In feedback and other notifications from farmers, the question of incorrect registrations has never arisen as an issue.

The Department is therefore satisfied as to the accuracy of payments made to the contractor despite the fact that invoices are raised and calf registration numbers are generated from the same source.

Monitoring of Administrative Controls

The contract for calf registrations and animal passport issue specifies the level of supervisory checks to be carried out by the contractor. It states that supervisory checks should be carried out regularly on the work of all staff and the computer system and these checks shall be documented. The minimum level of checks to be carried out is 15% of all transactions. As no documentary evidence was available I enquired as to what checks, if any, are carried out by the Department to ensure that the administrative controls, set out in the contract, are operating satisfactorily.

In reply the Accounting Officer stated that a Department official visits the contractor's premises on a regular basis to ensure compliance with the agreed procedures and processes and with the administrative provisions set out in the contract. The checks conducted vary and can incorporate a walk through of the relevant business processes (e.g. data-input, printing, packaging, posting, call centre, archiving, retrieval, etc.), an examination of the manual and electronic records of data input by each staff member as well as discussions with senior management and an examination of error listings.

The Accounting Officer acknowledged that the checks conducted by the Department to ensure compliance have not been documented in a systematic fashion. This issue has now been addressed and a checklist has been devised to evidence ongoing checks. In addition, for the future, the control documents used by the company to evidence checks conducted will be endorsed by the Department upon verification. The Accounting Officer also stated that the Department is satisfied from the checks that have been conducted that the administrative controls in question are operating in a satisfactory manner.

Cattle Movements

The same service provider successfully retained the CMMS contract for the handling, processing and verification of farm to farm bovine movement permits and on-farm death notifications for the year to December 2004.

Movements of cattle, whether for single or multiple animals, can only be made on foot of a movement certificate or permit issued by the contractor on behalf of the Department. The Department is invoiced monthly for the number of certificates/permits of cattle movements - certificates can be for a maximum of 10 animals - issued in the previous month.

However, as the CMMS database records the movement of each individual animal, it is impossible to reconcile the number of movements recorded against certificates issued and invoiced. A reasonableness test is carried out to verify the number of certificates invoiced by confirming that the total cattle movements per the CMMS in the month significantly exceeds the number of certificates invoiced.

The amount paid in 2004 for the issue of cattle movement certificates and the recording of on-farm death notifications was €995,000.

I enquired how the Department verifies that the amount of permits being claimed for is correct. In reply the Accounting Officer stated that the introduction of new technology under the new Animal Identification Movement System in 2005 will allow the Department access a report generating figures for the number of permits issued and this will be used, with effect from July 2005, to verify invoices received from the contractor. The Department will also use the new facility to conduct a retrospective check in respect of invoices paid to date under this contract.

Cattle Numbers — CMMS v Central Statistics Office

The Central Statistics Office (CSO) publishes a livestock survey every six months that estimates livestock numbers in the State. It was noted that the surveys for June 2004 and December 2004 included notes on a comparison of numbers with those on the Department's CMMS. The June 2004 survey indicated that total cattle numbers were some 6% higher on the CMMS than the CSO estimate at that date. At December 2004 it showed them to be some 5% higher. Both surveys noted that the CSO was continuing to compare the CMMS and CSO survey figures at farm level to provide a more detailed analysis and explanation of the reasons for the differences between the two data sources.

I asked what measures the Department had taken to establish the reasons why the CSO livestock survey figures for bovines are significantly lower that those of the CMMS, if a reconciliation has been carried out between the CMMS and CSO figures and, if so, what was the result. In reply the Accounting Officer stated that the CSO livestock survey figures for bovines are estimates based on sample surveys linked to the *June 2000 Census of Agriculture* whereas the CMMS statistics are based on a count on a specific day of individual animal tag numbers whose animal events (births, movements, calvings and exits) have been

notified variously by farmers, marts, exporters and factories. CMMS is a dynamic database and the total figures for the live animal population will vary from day to day in line with the addition of new notifications. It is the Department's view that the important issue is the level of accuracy, reliability and credibility of the CMMS database. The Department has taken a number of measures to ensure the accuracy of the database and is satisfied that it has an accuracy level in excess of 99% at this point.

In regard to the issue of a reconciliation being carried out between the CMMS and CSO figures the Accounting Officer stated that since 2000 there has been regular and ongoing contact between the Department and the CSO to compare the results of livestock surveys conducted by the CSO with data from the CMMS database. Initial feedback from the CSO showed that the highest level of discrepancy arose in respect of female animals in dairy herds and were caused by retagging issues, past inaccuracies in the CMMS database and delays in notifications. It is understood that the draft report of the CSO Statistical Potential of Administrative Records project envisages the eventual use of CMMS as a definitive source of control totals for the survey estimates of cattle data.

Animal Health Computer System

The new Animal Health Computer System is a fully networked computer system with dial-up internet access for veterinary practitioners and is designed so that animal health data for individual animals can be integrated with individual animal movement monitoring data recorded on the existing CMMS.

It was noted that the sum contracted for the system in 2001 was €5.8 million and that payments to 31 December 2004 amounted to approximately €8.7 million. The final payment of €304,000 was made in April 2004. I enquired as to the reasons for the cost overrun of €2.9 million, representing 50% of the original contract sum.

In reply the Accounting Officer stated that a number of factors led to delays and increased costs over and above the original contract price. The lapse of time between the design of the system, which was completed in August 2000 and its development, which ran from April 2001 to October 2003, advances in technology, changes in the Department's IT infrastructure and additional business needs resulted in the need for adaptations and additions to the original systems design. The original contract provided for single development, system test and user acceptance test phases with a pilot run due in September 2002. However, because of the number of adaptations and additions to the original systems design, including the need to respond to urgent business requirements arising during the development phase itself, a series of additional development, system test and user acceptance test phases were required followed by a pilot run in November 2003 and system roll-out which took until February 2005 to complete. In addition, progress on the project was significantly delayed in 2001 when key resources were diverted to deal with the Foot and Mouth Disease crisis.

Conclusion

On balance I was generally satisfied with the results of my examination of those aspects of the National Beef Assurance Scheme which were reviewed in the course of the audit and with the explanations provided by the Accounting Officer. There is always scope for improvement and the Department is aware of certain weaknesses but it is actively working to address them.

Chapter 13

Department of Transport

13.1 West-Link Toll Bridge

The M50 is a 40km orbital motorway around Dublin, running from the M1 at Dublin Airport to the N11 at Bray. A 3.2km section of the motorway, from the N3 (Navan Road) to the N4 (Sligo Road) includes two side-by-side bridges spanning the River Liffey (West-Link Bridge). This section of the M50 is a toll road. The first bridge opened in March 1990 and the second in September 2003.

This was the second toll scheme in the State. The first was the East-Link toll bridge where tolling rights had been granted to National Toll Roads Ltd (NTR) and which opened in October 1984.

Government Decision

In 1982, NTR had approached Dublin County Council seeking agreement in principle to construct and operate a toll facility across the River Liffey to the west of the city between the N3 and N4 national primary routes. Following discussions and negotiations involving the State, Dublin County Council and NTR, NTR submitted a proposal to Dublin County Council in May 1984.

In October 1984, the Government agreed, in principle, to a proposal from the Minister for the Environment (the Minister) to the conclusion by Dublin County Council of negotiations with NTR[19]. The memorandum to Government noted that if the State finances were not so constrained and if substantial capital investment was being put into road improvement then it could afford to forgo the possibility of tolling the road and of private sector investment.

In the circumstances then prevailing and given the relatively underdeveloped state of the national roads, tolling options had to be considered. The memorandum noted that while tolls were not generally applied to ring roads in European countries, the Western Parkway route was one of only a few routes which could potentially provide an economic return to a private investor without the necessity for State subsidies or guarantees. The proposal to Government noted that the proposed project yielded an after tax return of 18% to NTR by comparison with a gross yield at the time from Government bonds in the region of 15%.

The Western Parkway is the section of the M50, approximately 12.2km in length, from the N81 (Tallaght Road) to the N3 (Navan Road). Its construction was completed in 1990 and was funded by the State except for the 3.2km toll road section.

Toll Scheme

The Local Government (Toll Roads) Act, 1979 provided that road authorities may, with the consent of the Minister, make toll schemes for public roads. Section 9 of the Act provided that the road authorities may, with the consent of the Minister, enter into an agreement (Section 9 Agreement) with another party to provide, maintain, manage and operate toll roads[20].

In October 1987, Dublin County Council, pursuant to a toll scheme made in 1985 and approved by the Minister in December 1986, entered into a Section 9 agreement (the Agreement) with a private company,

[19] The negotiations were conducted with Conor Holdings Ltd, a private company with a major shareholding in National Toll Roads Ltd.

[20] Under the Roads Act 1993, as amended by the Planning and Development Act 2000, the power to levy tolls on national roads, make toll bye-laws and enter into agreements with private investors is now vested in the National Road Authority.

West-Link Toll Bridge Ltd, a wholly owned subsidiary of NTR, under which that company would construct the 3.2km toll road including the first bridge. In return, the company would be granted tolling rights to the road for a period of 30 years after which the road would revert to the State.

Second Bridge Construction

While the construction of a second bridge was not covered by the provisions of the 1987 Agreement, it was recognised from the outset that a second bridge would be built if traffic volumes rose to around 56,000 vehicles per day. In 1985 a senior engineer in Dublin County Council had pointed out that at this volume of traffic, the reduced level of service would make it necessary to construct the second bridge. By 1998, the 56,000 per day traffic threshold had been reached. The bridge was opened in 2003, by which time daily traffic was around 40% above the 56,000 threshold.

Licence Fee

The Agreement provided that NTR would pay a proportion of Gross Toll Revenue (GTR) to the State when the average daily traffic volumes over a year exceeded 27,000. The proportion, referred to as the licence fee, would commence at 30% of the GTR for the first 8,000 vehicles in excess of 27,000 and would rise in accordance with increases in traffic volume measured in intervals or bands as outlined in Table 28.

Table 28 Licence Fee Bands

Band	Average Daily Traffic Limit	Proportion of GTR payable to State
	First 27,000	-
1	27,001 to 35,000	30%
2	35,001 to 45,000	40%
3	Over 45,000	50%

In June 2001, the NRA entered into a revised agreement with West-Link Toll Bridge Ltd (the supplemental agreement), under which the company would construct a second bridge in return for a revised toll scheme. The revised scheme added a fourth band to the licence fee structure under which the State would receive 80% of GTR for traffic volumes over an agreed fourth band figure for the relevant year, as set out in the supplemental agreement. The fourth band commenced at 79,000, in 2001, and was to increase in annual tranches to 126,000 by 2020. The 80% threshold has not been reached to date. In 2004, the fourth band would have applied if daily traffic volumes exceeded 88,000. The daily traffic volume for that year was around 84,800.

On the basis of the agreed bands the yield from licence fees achieved and projected is set out in Table 29. The yields for the years from 2005 onwards are based on agreed forecast traffic volumes.

Table 29 Yield from licence fee 1990 to 2020[a]

Period	Average daily traffic over the period	Licence fee as proportion of GTR
1990 –1994	13,500	-
1995 – 1999	42,300	16.7%
2000 – 2004	75,200	25.3%
2005 – 2009	93,000	*32.7%*
2010 – 2014	105,800	*34.8%*
2015 – 2020	114,500	*36.0%*

[a] Projected yields are shown in italics.

Taxation

At the time of the 1987 agreement, the rate of Corporation Tax was 50%. It was assumed, at that time, that NTR would not be liable for the payment of municipal rates in respect of the toll road and, at that point, VAT did not apply to toll charges.

There have been a number of changes to taxation and other charges in the period from 1990 to date

- West-Link Toll Bridge Ltd became liable for municipal rates on the toll road from 1992
- VAT has been applied to toll charges since September 2001 following a ruling by the European Court of Justice
- The rate of Corporation Tax has fallen steadily over the period, from 50% in 1987 when agreement was reached to 12.5% from January 2003
- Income tax rates and capital gains tax rates have also changed over this time.

Proceeds of Tolling

Table 30 sets out the GTR at the bridge and the appropriations to the State, excluding Corporation Tax, for the period from 1990 to 2004. €79,672,000 has been received by the State since the facility was put in place. The gross revenue in the period was €310,056,000.

Table 30 Toll Revenue and Licence Fee 1990 to 2004[21]

Year	Gross Proceeds[22]	Licence Fees	Municipal Rates	Appropriations to the State (excluding Corporation Tax)
	€000	€000	€000	€000
1990	1,834	-	-	-
1991	4,046	-	-	-
1992	5,243	-	294	294
1993	5,940	-	309	309
1994	6,719	-	324	324
1995	8,224	-	335	335

[21] The figures in this table have not been adjusted to 2004 values.
[22] Excluding VAT

1996	11,296	-	347	347
1997	20,749	3,043	356	3,399
1998	26,689	5,817	367	6,184
1999	29,668	7,309	378	7,687
2000	31,045	8,079	390	8,469
2001	33,703	9,220	2,875	12,095
2002	36,857	7,585	3,025	10,610
2003	39,369	8,044	3,176	11,220
2004	48,674	15,094	3,305	18,399
Totals	**310,056**	**64,191**	**15,481**	**79,672**

Source: Department of Transport (the Department), South County Dublin and Fingal County Councils.

Cost of the M50 to date

The West-Link facility provides access to a 40km motorway standard ring road around Dublin, which in turn gives access to all national primary routes out of the capital city.

The construction of the M50 has been, with the exception of the toll road, funded by the State at a cost of around €1.1bn in 2004 values. Toll charges at the West-Link Bridge are expected to be around a further €1.1bn in 2004 values for the period 1990 to 2020, excluding VAT. When account is taken of direct appropriation of funds (€0.44bn) to the State in the form of licence fee, municipal rates and corporation tax the net cost to the public of the current M50 facility, before taking account of income and capital gains tax, is around €1.76bn in 2004 values. These figures do not take account of the cost of a proposed upgrading of these facilities to cater for user demand.

To the extent that the profits available to the shareholders of NTR are distributed, additional income and capital gains tax will accrue to the Exchequer.

Scope of the Review

Because of public concerns about the operation and cost of the toll road I decided to

- compare the economic cost of the facility with its cost to users
- review the return to NTR
- review the return to government
- consider the options available to the State under its agreement with NTR..

No Cost Benefit Analysis (CBA) was carried out for the West-Link project. The memorandum to Government in 1984 stated that while no CBA had been carried out on the proposed M50, there could be no doubt that given its national importance, the existing traffic congestion and projected traffic flows over the various sections, the investment would provide a substantial real return.

Because of the extended period of the development of the M50 network over the last three decades it is recognised that CBA would not be very informative in this instance and the project may be best viewed as

a measure to remedy a major gap in the roads infrastructure. Accordingly, in the absence of a quantification of the benefits from the project no analysis has been made of the economic value of the facility to users.

Costs to Users

The cost of the facility to users is equivalent to the GTR. This section reviews the outturns on foot of the contracts taking account of the GTR projected originally and those now projected or achieved. Two issues in relation to cost were examined in the course of audit

- what was the relationship between the cost of the infrastructure and the aggregate amount paid by road users
- whether, in negotiating the second bridge contract, a reasonable degree of balance was achieved in at least maintaining that relationship.

Relationship between Project Cost and Charges

I reviewed the relationship between the cost of the facility to the users at the inception of the original agreement with NTR and the outturn expected on the basis of experience to date and current projections.

In comparing the economic cost of the facility with the cost to users all rates and taxation have been excluded. The facility refers to the 3.2km section of the M50 which is a toll road. For the purposes of this comparison no account was taken of the State investment in infrastructure on other parts of the M50 since they did not form part of the tolling scheme.

Analysis of the projections at the negotiation of the original agreement shows that the users would pay around €3.70 for each €1 in whole-life costs[23] when expressed in 2004 values. Expected revenue from toll charges and the whole-life costs of constructing and operating the first bridge at that time are set out in Table 31. The 2004 values of the cash flows set out in that table provide the most realistic basis for comparison because it expresses the cash flows in constant values.

Table 31 Expected Revenues and Whole-Life Costs – Original Agreement

	Original Estimates 1990 - 2020		
	Toll Revenues	Whole-Life Costs	Ratio of Revenue to Costs
	€m	€m	
Gross Cash Flows	758	111	6.8 : 1
Cash Flows at 2004 Values	678	182	3.7 : 1

Source: Gross Cash Flows at time of negotiations in 1984 - Department of Transport
Analysis of Gross Cash Flows by Office of Comptroller and Auditor General

By the time the second bridge was being negotiated, the M50 road system had been further developed and the number of users had increased. Because of this increased use, road users were, by then, paying in the

[23] Whole-life costs aggregate capital and running costs of the facility.

aggregate around €5.20 for each €1 in whole life costs. Table 32 sets out the position at the time the contract for the second bridge was being negotiated.

Table 32 Revenues and Whole-Life Costs - 1999

	Outturn and Estimates[a] 1990 - 2020		
	Toll Revenues	Whole-Life Costs	Ratio of Revenue to Costs
	€m	€m	
Gross Cash Flows	1,332	137	9.7 : 1
Cash Flows at 2004 Values	1,026	197	5.2 : 1

Sources: Gross Cash Flows - Department records, NTR published accounts.
[a] Cash Flows combine actual outturn from 1990 to 1998 and projected cash flows for the period from 1999 to 2020. VAT is excluded.
Analysis of Gross Cash Flows by Office of Comptroller and Auditor General

The costs borne by users are a factor of the toll rates and the traffic volumes. These are examined separately in the following sections.

Toll Rates

Under the toll scheme provisions toll charges may not exceed a certain level (maximum tolls). NTR may, however, charge less than the maximum toll if it so chooses. The maximum level is calculated by adjusting a base toll by reference to the Consumer Price Index (CPI)[24]. The base tolls, in 1990, ranged from 38c (30p) for motor cycles and 76c (60p) for cars up to €4.57 (£3.60) for certain commercial vehicles. The base rate for cars was adjusted upwards following the negotiations for the construction of the second bridge.

The 1987 and 2001 agreements provide that if the State instructs NTR to charge a toll lower than the maximum toll, then the State would be required to compensate the operator. These provisions effectively guaranteed that the real value of the tolls could be maintained independent of the volume of traffic. Currently, NTR charges less than the maximum rate for large commercial vehicles. Maximum tolls and tolls charges in 2005 are set out in Table 33.

Table 33 Toll Charges – West Link Bridge 2005

Vehicle type	Maximum Toll[a]	Actual Toll[a]
	€	€
Motorcycles	0.80	0.80
Motor Cars	1.80	1.80
Buses and Vans	3.10	3.10
Commercial vehicles, 2 axle	6.10	4.50
Commercial vehicles, 3 axle	7.60	5.20
Commercial vehicles, 4 axle	9.20	5.60

[a] Inclusive of VAT

[24] Annual increases are rounded to the nearest 10c. Value Added Tax is applicable to tolls since 2001. VAT at the prevailing rate is added to tolls prior to rounding.

Impact of Traffic Volumes

Traffic volumes have been considerably greater than anticipated in the estimates that informed the setting of the toll charges. The original estimates had been based on an assumption that only the Western Parkway section of the M50 would be open to traffic and did not take account of the likely impact on traffic volumes when the additional sections would be completed.

From 1990 to 1996, the volume of traffic at the toll road was below the original estimates. In 1991, the first full year of operation, traffic volumes were around 54% of the estimates. Volumes have risen each year and by 1996 were around 91% of the estimates. In 1997, the year following the opening of the section of the M50 from the N3 to the M1, volumes rose sharply to almost 45,600 per day which was around 65% in excess of the original forecast. In 2004, the traffic volume was over 2.5 times the original estimate.

Traffic volumes at the West-Link Bridge, and the original estimates, are set out in Table 34.

Table 34 Average daily traffic volumes 1990 to 2004

Year	Original Proposals	Actual
1990	20,300	6,800
1991	21,300	11,500
1992	22,300	13,800
1993	23,500	15,200
1994	24,600	16,700
1995	25,900	20,000
1996	27,000	24,700
1997	27,700	45,600
1998	28,400	57,500
1999	29,200	63,900
2000	29,900	67,300
2001	30,600	71,100
2002	31,300	74,700
2003	32,000	78,100
2004	32,800	84,800

Whereas toll charges rise broadly in line with inflation, there is no mechanism in the agreements to provide for a reduction in toll charges if volumes exceed the estimates which informed the setting of the base tolls. The increase in the volumes above the original estimates resulted in additional costs to users of €350m in 2004 values giving a higher return to the operator as well as increasing the amount of revenue accruing to the State.

Second Bridge Negotiations

A detailed proposal for the construction of the second bridge submitted by NTR in September 1999, following negotiations between NTR and the NRA, had the following main financial features

- The costs of providing the second bridge would be met through an increase in the toll charge for cars[25]. The maximum charge for cars under the 1987 Agreement would increase by around 17% from January 2005 with interim increases in the period 2000 - 2004. There was also a proposal that a further 10c be added to the toll, to be paid in full to the NRA. This provision has not been invoked by the State.
- While the existing licence fee structure would continue to apply, a fourth band was to be added in order to reduce the possibility that NTR would make windfall profits in the event that traffic volumes would exceed those projected. The fourth band was to be set at a level that was 6.5% above compromise traffic forecasts agreed between the NRA and NTR.
- Municipal rates were being charged, at that time, on what is known as the "contractors" basis but there were indications that they would be levied in the future on the "profits" basis. Under the profits basis the rateable valuation of the toll road would be far greater. It was proposed that if rates continued to be assessed on the lower contractors basis, the difference between rates assessed on the two bases would be paid by NTR to the NRA, using an agreed formula.

In addition, it was agreed that the toll road must be maintained in a manner that guarantees it will have a residual life of 15 years when it is handed back to the State in 2020.

In December 1999, the Board of the NRA approved the proposal. In doing so it took account of an independent assessment which it had commissioned. The assessment, delivered in November 1999, had noted that the NRA's negotiating position was constrained by two factors

- the original agreement was not open for negotiation and
- the NRA was not in a position to build the second bridge with either public funds or to procure a competing private sector party to do so as NTR had the sole right to toll that section of the M50.

VAT was imposed on toll charges prior to an agreement being signed and the Board approved an amended proposal taking account of VAT in June 2001.

NTR bore the cost of construction (€27m in 2004 values) and will incur additional running costs of €7m in 2004 values. However, as the extra projected toll revenue of €74m arising from the agreement attracts licence fee at 50%, the bulk of the net toll revenue after taking account of those costs will accrue to the State (€37m). Although it could be argued that the users were already paying aggregate tolls at a level sufficient to remunerate the investment by virtue of volume increases in excess of those originally envisaged, it could also be argued that because there was no mechanism in the 1987 agreement to cover the second bridge financing, the achievement of an overall reduction in the ratio which the cost to users bears to the total costs incurred by NTR, when taken together with a net marginal return of only €3m to NTR, might be viewed as achieving a reasonable negotiating result.

After account is taken of the financial adjustments arising out of the second bridge negotiation, the cost to users by way of toll revenue is around 4.8 times the whole-life costs of the toll road including the two bridges, or around €869m more than the cost when expressed in 2004 values. Table 35 sets out the position following these negotiations.

[25] The base level for all other tolls remained at the levels specified in the original agreement.

Table 35 Revenues and Whole-Life Costs including Second Bridge - 2004

	Outturn and Latest Estimates[a] 1990 - 2020		
	Toll Revenues	Whole-Life Costs	Net Toll Revenue
	€m	€m	€m
Gross Cash Flows	1,454	170	1,284
Cash Flows at 2004 Values	1,100	231	869

Sources: Gross Cash Flows - Department records, NTR published accounts.
[a] Cash Flows combine actual outturn from 1990 to 2004 and projected cash flows for the period from 2005 to 2020. VAT is excluded.
Analysis of Gross Cash Flows by Office of Comptroller and Auditor General

Adjustment of Car Tolls

The figures in Table 35 take account of the impact of adjustments to the toll on cars agreed in the negotiations about the construction of the second bridge in 1999. These adjustments were as follows

- a revised interim toll level for cars of €1.20 applying for the period 2002 to 2004
- calculation of the toll levels from January 2005 by reference to a base level of €1.20 at January 2000 indexed for inflation thereafter.

In addition, the imposition of VAT with effect from September 2001 led to the introduction of certain transitional measures. The charge to the user was increased to €1.30 between September 2001 and December 2003. Because NTR had to remit VAT on the revised toll charge its net toll revenue fell below the previously agreed level of €1.20 for 2002 and 2003. The State compensated NTR in order to maintain the company's VAT exclusive toll revenue at the agreed level.

In addition, it was agreed that the increased toll charge arising from VAT would lead to a certain volume of car users diverting to alternative routes. The proportion which would divert was agreed at around 4%. In order to compensate NTR for the anticipated fall in demand it was agreed that the State would pay additional compensation in 2003. The total compensation paid by the State was €6.4m of which around €0.5m was attributable to compensation in respect of the diversionary effect of the increased tolls.

The transitional arrangements also provided that in 2004 the car toll would further increase to €1.50 giving a toll charge of €1.24 exclusive of VAT. This increase of 4c per car in excess of the charge agreed in 1999 prior to the imposition of VAT resulted in users paying an additional €1m in toll charges in 2004.

Licence Fee Underpayment

The agreements provide that the amount of GTR payable to the State (licence fee) may be audited by the auditor of West-Link Toll Bridge Ltd or by any suitable person as may be agreed by the NRA and West-Link. The agreements also provide that the NRA may request copies of and access to all relevant documentation and records on which the calculation of the licence fee and any deduction therefrom is based. In the event of any disagreement, the matter can be decided by arbitration.

Under this arrangement, the auditor of West-Link Toll Bridge Ltd annually confirms

- the amount of the licence fee
- the turnover upon which that licence fee is based
- the overall traffic volume for the year
- the accuracy of the computation of the licence fee and
- that the computation has been performed in accordance with the Agreement.

Notwithstanding this, my audit established that the amounts paid to the State for the years 2002 and 2003 were incorrectly calculated. Under the 2001 Agreement the compensation paid to NTR should have been treated as an element of GTR because GTR is defined in that Agreement as tolls collected or receivable together with the licence fee credit. This should have resulted in just over €1.8 million extra being paid to the State by way of licence fees. In addition, rounding of the compensation payment per car to the nearest cent by NTR resulted in a further underpayment of €171,000. Details are set out in Table 36.

Table 36 Licence Fee Underpayment 2002 and 2003

	Comptroller and Auditor General Calculation		NTR Calculation		Underpayment
	€	€	€	€	€
Toll Proceeds 2002 and 2003	76,225,477		76,225,477		
Licence Fee Credit	6,260,078				
GTR		82,485,555		76,225,477	
Licence Fee	23,873,880		22,060,335		
Licence Fee Credit	(6,260,078)		(6,431,161)		
Licence Fee payable		17,613,802		15,629,174	
Underpayment					**1,984,628**

I enquired of the Accounting Officer

- the exact circumstances that gave rise to the non-detection of the underpayment
- what measures have been taken or are proposed to recover it and to monitor and validate future remittances.

In regard to the non-detection of the underpayment, the Accounting Officer informed me that this arose because the checking procedures in the Department had not been adapted to take account of the changed definition of GTR included in the 2001 Supplemental Agreement. This agreement provided that a licence fee credit due to NTR in respect of 2002 and 2003 would be included as part of the GTR for the calculation of the licence fee payable to the State. This was not done by NTR and the error was not identified by NTR's auditors, the NRA or the Department.

In regard to the recovery of the underpayment of the licence fee in respect of 2002 and 2003, she informed me that the Department had taken the matter up with NTR. NTR have accepted that an underpayment has occurred and have undertaken to immediately recoup €2m. In order to assist in confirming the precise amount of the underpayment and to deal with other queries relating to the calculation of the fee, NTR have been asked to provide details and explanations relating to the calculation

of GTR and the licence fees payable thereon back to 1997. When this work has been completed, the provisions in the agreement relating to interest on late payments will be invoked and repayment of the amount underpaid will be secured in full.

In regard to the arrangements for the monitoring and validation of future remittances, the Accounting Officer stated that the provision of a certificate from NTR's auditors confirming the accuracy of the payment is an important part of the control system for the validation of the licence fee. In addition, procedures are in place in the Department for checking the remittances. She assured me that, since the Department of Transport was established, the Department has continually moved to strengthen and improve its financial control systems. However, in light of the seriousness of the error that has arisen in this instance, she has instructed that arrangements for validating the correctness and accuracy of the licence fee payment from NTR be reviewed as a matter of urgency. Decisions on measures to strengthen the Department's arrangements for monitoring and validating future remittances will be taken in light of the outcome of the review which is already underway.

Return for the Private Operator

At the time of the Government decision in 1984 it was estimated, in the proposal by the private operator, that the after tax rate of return on the project would be around 18%.

By 1999, prior to the agreement to construct the second bridge the projected after tax rate of return to NTR for its investment was around 25%[26], based on the outturn to that date and the forecasts which informed the negotiations for the second bridge. Following the construction of the second bridge and taking into account the additional investment by NTR as well as the outturn to 2004 and the revised forecasts, the projected after tax return has fallen by around 1% to 24%.

NTR's Distributable Income

Changed tax structures over the period 1987 – 2004 impact on the ultimate distributable income of NTR. In order to examine the effect of these changes, the distributable income of NTR has been calculated under two separate scenarios for the now estimated traffic volumes – firstly, using the taxation structures ruling in 1987 (original scenario) and secondly, using the rates which applied up to 2004 or are projected thereafter (current scenario).

On this basis, the same gross revenue is projected to result in an increase of €141m, in 2004 values, in NTR's distributable income as set out in Table 37.

Table 37 NTR Distributable Income from the West-Link Project (2004 values)

	Current Scenario			Original Scenario		
	€ m	€ m	Share of GTR	€ m	€ m	Share of GTR
Gross Toll Revenue[a]		1,100			1,100	
Costs						
Capital Costs	(131)			(131)		
Operating Costs	(100)	(231)	21.0%	(100)	(231)	21.0%
Direct payments to Government						

[26] Internal rate of return for NTR.

Licence Fee	(285)			(285)		
Corporation Tax	(80)			(291)		
Municipal Rates	(70)	(435)	39.5%	-	(576)	52.4%
Revenue to NTR		434	39.5%		293	26.6%

[a] VAT is excluded.

Change in Return to Government

The return to government arising out of the bridge project is not equivalent to the direct payments made to it by NTR. This is because the income distributed by NTR is taxable in the hands of its shareholders and is, therefore, an additional source of revenue.

In order to examine the likely effect of the revenue attributable to government which was projected at the inception of the agreement compared with what is currently estimated, I took account of the following factors

- the changes in municipal rates, corporation tax rates, tax credits on distributions and income tax rates over the period 1987 to 2004
- the projected distribution pattern of the NTR Group as indicated in their financial statements for the years 2001 - 2004.

Assuming total efficiency in tax collection, the estimated overall return to government has altered between 1987 and 2004 as projected in Table 38. The assumption has been made that all previously non-distributed profits will be distributed by way of dividends when the tolling period expires in 2020. In addition, it has been assumed that all shareholders in NTR are liable for income tax at the top rate and that the dividend income is not sheltered from income tax. The income tax revenue shown is the maximum that can accrue to the State under both scenarios.

Table 38 Revenue accruing to Government — West-Link project 1990 to 2020 (2004 values)

	Current scenario - projected share[a]		**Original scenario - projected share[a]**	
	€m	Share of GTR	€m	Share of GTR
Licence Fee	285		285	
Corporation Tax[b]	80		243	
Municipal Rates	70		-	
Income Tax[b]	136		125	
	571	51.9%	653	59.4%

[a] Excluding VAT.

[b] Corporation Tax liabilities of NTR and Income Tax liabilities of shareholders have been adjusted for the effect of tax credits on dividends. These credits were abolished in 1999. Under the original scenario, the tax credits apply for the full period.

However, if the company were to be wound up and remaining assets distributed by way of a capital distribution, the tax accruing to the State would be around €22m less in the current scenario and around €4m less in the original scenario than that shown in the table.

Ultimately, after taking account of all tax revenues, the share of GTR accruing to government has fallen by around €82m or 7.5% of GTR. The difference between the share of the revenue expected to accrue to the State and the share that would have accrued under the revenue-sharing understanding at the time of the original agreement has arisen principally due to the fall in the rate of Corporation Tax[27]. On the other hand, it is projected that revenue of €70m will arise from the imposition of municipal rates with effect from 1992.

There are two ways of viewing this outcome. On the one hand, it is arguable that changes in Corporation Tax rates and other charges imposed by public bodies are part of the normal business risks associated with any project, and that any additional profit, arising from the fall in corporate tax rates, which has accrued to NTR is no more than the benefit accruing to any other business.

On the other hand, it might be considered that commercial agreements involving the State as a party are struck so as to achieve a particular distribution of revenue. Taxation is part of the intended distribution when the State is involved. There may be merit in future partnership arrangements, in putting a mechanism in place to maintain a reasonable distribution in the event of major tax fluctuations in either direction.

Non-reclaimable VAT

VAT has been applied to toll charges since September 2001. The State has, therefore, increased its take at the expense of those road users who cannot reclaim VAT. Analysis carried out by consultants for the NRA indicated that around €99m in 2004 values, in non-reclaimable VAT would be paid by users of the toll bridge and would accrue to the State.

Impact of Upgrading on Revenue Sharing

The NRA currently proposes to upgrade the M50 facilities by widening the carriageways and altering interchange layouts. The traffic volumes accommodated by the M50 are projected to increase as a result of this work. Under the 2001 agreement

- the original sharing arrangement will hold until the traffic projections agreed in 2001 are exceeded by around 6.5%
- thereafter, the State would receive 80% of the GTR for traffic volumes in excess of this level.

Table 39 compares the average daily traffic volumes projected in the 2001 supplemental agreement with the fourth licence fee band above which State will receive 80% of the GTR.

Table 39 Licence Fee – Fourth Band

Year	Current projection[a]	Threshold for fourth band
2005	86,463	92,000
2006	89,872	96,000
2007	93,250	99,000
2008	96,298	103,000
2009	99,183	106,000
2010	102,056	109,000
2011	103,918	111,000
2012	105,889	113,000

[27] The nominal rate of Corporation Tax in 1987 was 50%. After taking account of tax credits the effective rate was 38.7%, in cases where a company distributes 100% of profits. The rate stood at 12.5% in 2004.

2013	107,641	115,000
2014	109,545	117,000
2015	111,259	118,000
2016	112,888	120,000
2017	114,423	122,000
2018	115,857	123,000
2019	117,310	125,000
2020	118,518	126,000

[a] These are the volumes projected in the 2001 Supplemental Agreement.

The proposed upgrading investment will have the effect of further increasing the revenue accruing to NTR as it is likely that the traffic volumes will then exceed the current projections. While NTR will receive 50% of GTR up to the commencement of the fourth band, additional revenue accruing to NTR will be restricted to 20% thereafter.

Options Available to the State

Under the existing arrangements the State may abolish or reduce tolls or limit any increase in them. However, this would trigger compensation entitlements under the agreement.

Broadly speaking, the provisions are

- If the tolls are reduced, or not increased in line with the indexation mechanism, the State must compensate NTR for the shortfall in toll revenue. The amount of compensation payable over the duration of the agreement is the difference between the reduced toll revenue and the toll revenue in the year before any such adjustment, indexed in accordance with the agreement.
- If tolls are abolished, the compensation is the total amount of toll revenue paid, less the licence fee, in the 12 months immediately preceding the date of the abolition of the tolls. This compensation would be payable in each year for the duration of the agreement and would increase in accordance with the indexation provisions.

The Department has informed me that the NRA is currently in negotiation with NTR on a range of issues affecting the West Link agreement, including a move to barrier free tolling and the funding of the proposed upgrading works on the West Link section of the M50.

Review Methodology and Sensitivity Testing

Review Methodology

Except as otherwise stated, the analysis in this review has been conducted using outturns or projected cash flow data which formed the basis of negotiations. These have been expressed in 2004 present values (2004 values) derived using a rate of 5% (excluding inflation) to adjust the value of pre-2004 estimates or outturns to 2004 levels and to discount post-2004 cash flow projections in order to bring them back to 2004 values.

Impact of Discount Rates

A private operator may use a different discount rate than the State. In order to test the variation in the ratio of revenue to costs at different discount rates, the cash flows were also discounted at 3% and 7%.

Impact on ratio of revenues to whole life costs

In all cases, the ratio of revenue to costs had risen by 1999 from the time of the original contract and had fallen somewhat from the 1999 level following the construction of the second bridge. The ratios of revenue to costs at the various discount rates are set out in Table 40.

Table 40 Ratio of Revenues to Whole-Life Costs

	3% discount rate	5% discount rate	7% discount rate
At time of contract, 1987	4.4 : 1	3.7 : 1	3.2 : 1
Prior to agreement to construct second bridge, 1999	6.3 : 1	5.2 : 1	4.3 : 1
Following construction of second bridge	5.7 : 1	4.8 : 1	4.0 : 1

The ratio of revenue to costs is greater at the lower discount rates because a greater proportion of costs were incurred at the earlier stages of the project while a greater part of the revenues will arise in the later years. The effect of using a higher discount rate is to place a lower value on the later cash flows.

Impact on revenue sharing

There was some difference in the proportion of GTR accruing to government after taking account of all tax revenues and assuming that the State would receive the maximum income tax revenue. The share of GTR expected to accrue to the government at the different discount rates is set out in Table 41.

Table 41 Proportion of revenue accruing to Government 1990 to 2020

	3% discount rate	5% discount rate	7% discount rate
Current projected share	55.2%	51.9%	48.9%
Original projected share	62.5%	59.4%	56.3%

Chapter 14

Department of Health and Children

14.1 National Treatment Purchase Fund

Introduction

The Waiting List Initiative (WLI) was introduced in 1993 as a short-term initiative to tackle the problem of significant numbers of public patients waiting excessively long periods for elective (i.e. non-emergency) hospital procedures. However, the initiative continued until 2003 by which time it had been funded on an annual basis to a total cost of €290 million. My Value for Money study on the Waiting List Initiative published in November 2003 pointed to the scope for co-ordinating waiting list funding more effectively, and to the fact that up to half of WLI funding was generating activity indistinguishable from activity funded through the normal budgetary processes applicable in the publicly funded health sector.

The National Treatment Purchase Fund (NTPF) was announced by the Minister for Health and Children in April 2002, as a key initiative of the Health Strategy, to treat patients who have been longest on hospital in-patient waiting lists. Funding for the initiative was provided in a distinct Subhead of the Vote for the Office of the Minister for Health and Children, from 2002 onwards. The amounts provided were, €5m (2002), €30m (2003), €44m (2004) and €64m (2005) and these were administered through the Department of Health and Children (the Department) and by the NTPF on an administrative basis until 1 May 2004 when the Minister for Health and Children, in exercise of the powers conferred on him by the Health (Corporate Bodies) Act, 1961, formally established the NTPF as a statutory Health Body.

The remit given to the Fund was to focus on those patients waiting longest for hospital procedures and to purchase treatment for them primarily in the private hospital system in Ireland, Northern Ireland and Britain. It may also make use of any capacity within public hospitals to arrange treatment for patients.

The 2001 Health Strategy[28] set a target that by end of 2004 no public patient would wait longer than three months for treatment. The Strategy visualised the development of a national waiting time database by the proposed National Hospitals Agency. This database would help channel patients awaiting treatment to an appropriate hospital with sufficient capacity. The management and classification of waiting lists was to be reorganised in several important ways and used in the operation of the NTPF.

Waiting lists would

- be categorized by waiting times, broken down to sub-specialty/procedure level
- include the referring GP's name
- be available to GPs
- show consultants' names as an aid to decisions by GPs regarding referrals
- allow GPs to notify significant changes in the medical status of patients and to propose that the priority of a patient awaiting treatment be reviewed.

[28] Department of Health and Children, *Quality and Fairness: A Health System for You.* Government of Ireland, 2001, pp. 104-105.

NTPF Operations

The NTPF arranges treatment for patients waiting longest for treatment. Hospitals have been informed that any NTPF work undertaken in public hospitals must be over and above core funded activity and should not displace the normal duties of these hospitals. While it is the Fund's policy to endeavour to ensure that consultants do not predominantly treat patients from their own public hospital waiting lists, there are exceptions in relation to the treatment of children and for instance, in certain cases for reasons of procedural or patient complexity.

Reference Prices

The Department has in place a programme to collect, categorise and interpret data related to the types of cases treated in the Public Hospital system. This programme – Casemix – categorises each hospital caseload and allows the comparison of activity and costs between different hospitals. One of the benefits of Casemix measurement is the extent to which it provides a common language for service planning, management and development that is meaningful to both clinicians and managers. Currently 37 hospitals participate in the Casemix programme.

NTPF state that Casemix is one tool used as a benchmark by the NTPF in price negotiation when appropriate to the treatments being procured. However, NTPF state that Casemix is not all-inclusive in the context of price negotiation with hospitals, as it does not comprehend the full service provided to NTPF patients in all cases, such as

- routine pre and post operative visits,
- tests required for specific procedures,
- capital costs and depreciation considerations which arise for private hospitals in some instances.

While the Casemix model has not been designed as a pricing benchmark, the Department has stated that it welcomes greater use of the data for monitoring and evaluation purposes and considers that it is best used to raise questions for discussion.

Referrals

Patients can be referred to the NTPF by their GP, hospitals or Consultant, or they can contact the NTPF directly. NTPF has funded the treatment of 23,379 patients up to end of 2004 – 1,920 in 2002, 7,832 in 2003 and 13,627 in 2004. Of the 13,627 patients treated in 2004, 12,762 were referred by public hospitals and 865 came through the lo-call line. Currently, the threshold for eligibility for NTPF treatment is three months waiting on an In-Patient or Day Case Waiting List. Patient permission is required before the NTPF organise treatment arrangements.

If it is necessary to arrange treatment in Britain or Northern Ireland, the NTPF will organise and pay for travel and accommodation for the patient and an accompanying person.

Audit Objectives

The examination sought to ascertain

- how the NTPF determined the price paid for procedures purchased
- the relevance of Casemix costs to NTPF activity
- the proportion of procedures purchased within and without the public health sector
- the contribution made by the NTPF to achieving the objective set out in the 2001 Health Strategy to reduce the numbers of persons waiting for treatment for an unacceptable length of time.

Treatments for the 13,627 patients funded in 2004 fall into 456 procedure groupings. The unaudited financial information recorded in the NTPF Annual Report for 2004 shows expenditure of €40,560,258 on direct patient care expenses in the year.

For the purposes of my examination the top eight procedures by volume were selected for detailed examination. Expenditure on these in 2004 was approximately €15.5 million or 38% of direct patient care expenditure (excluding ancillary costs). These 8 procedures accounted for 3,809 procedures paid for by the NTPF in 2004 or 28% of all treatments funded by the NTPF in that year.

Audit Findings

Price Negotiation

The price paid by the NTPF for treatments purchased from public and private hospitals is agreed by negotiation. The negotiation process culminates in a service agreement between hospitals and the NTPF whereby hospitals agree to provide the NTPF with agreed services. NTPF vets participating consultants for suitability. Only approved consultants are placed on a panel and are permitted to perform procedures for the NTPF.

NTPF stated that for the purposes of price-setting, NTPF uses the tools available to it as guides and benchmarks in seeking competitive prices. These are built into the NTPF comprehensive pricing database and include

- the Casemix system costs
- estimated insurers' prices
- consultant costs based on the insurers' Schedule of Fees
- prices proposed by peer hospitals.

The price negotiation process is a detailed exercise that is influenced by a number of benchmarks, prevailing prices, capacity requirements, complexity requirements and geographic considerations.

NTPF Negotiated Prices for Funded Procedures

I obtained details of the prices negotiated by NTPF for procedures with both private (Ireland and UK) and public sector hospitals. As well as using its other benchmarks in the negotiation of 2004 prices, NTPF had regard to the Department's Casemix Peer Group Report which classifies treatments carried out on patients into high level Diagnostic Related Groups (DRG). The precise treatments actually provided under the negotiated agreements cannot be ascertained until the patients are discharged from the treating hospitals.

Table 42 shows the percentage by which the highest negotiated prices exceeded the lowest prices for the 8 most common procedures arranged by the NTPF in 2004. The most costly procedure negotiated was €15,895 while the least costly amounted to €378. The Department has pointed out that prices agreed by the hospitals may vary according to the cost base of individual hospitals and the nature and age of patients being treated.

I have acceded to a request by the Accounting Officer of the Department not to disclose the prices paid for procedures by the NTPF on the basis that the publication of commercially sensitive information would affect NTPF's negotiating position and as a result its capacity to deliver a value for money service.

Table 42 Comparison of prices achieved by NTPF across the eight most common procedures

Procedure		% Highest exceeded Lowest
Cataracts	Inpatient	87%
	Day Case	76%
Varicose Veins (one leg)	Inpatient	61%
	Day Case	44%
Total Hip Replacement (excluding revisions)	Inpatient	72%
Skin Lesions	Inpatient	126%
	Day Case	217%
Coronary Angiogram	Inpatient	0%
	Day Case	20%
Total Knee Replacement (excluding revisions)	Inpatient	71%
Grommets (< 17 years)	Inpatient	54%
Laparascopic Cholecysectomy	Day Case	206%
	Inpatient	215%

Casemix Cost Comparison

In order to evaluate whether the NTPF has procured treatments at the most economically advantageous cost relative to that recorded in the Casemix programme it would be necessary to consider – at national or hospital level – how the price paid compared with the corresponding Casemix cost. This type of comparison has not yet been undertaken by the NTPF. An example of the variation that can occur is illustrated by the procedure labelled in Table 42 as Coronary Angiogram. An analysis of a sample of the discharge details for patients treated under this heading by the NTPF, carried out on its behalf by the ERSI, classified the patients into two discrete DRGs. The Casemix costs for these DRGs varied by some 84%.

It is worth noting that the average NTPF negotiated price for Coronary Angiogram was under half the Casemix cost of the lower of the two DRGs identified. In contrast, the average negotiated price for Grommets was more than twice the national average cost recorded in the Casemix 2005 model for the most likely corresponding DRG.

While acknowledging that Casemix was not designed as a benchmark for price-setting, these variations point to the necessity from a value for money perspective to ensure that the full potential of Casemix is exploited as an evaluation tool. This would help in any assessment of the relative cost effectiveness of NTPF funding of treatment as against other funding arrangements e.g. the allocation of the same funds directly to publicly funded hospitals whose patients have been treated by the NTPF.

Accounting Officer's Response

Regarding apparent variations between the Casemix and NTPF data in relation to costs for particular procedures, the Department of Health and Children has advised that great care should be taken concerning the interpretation of the two sets of data. Casemix operates by classifying hospital patient data into over 600 Diagnosis Related Groups (DRGs). DRGs are the classification of patients into discrete groups which have similar attributes and resource intensity. The Casemix Peer Group Report generates a national aggregated, average cost per case by DRG and excludes capital and depreciation costs. The Department has therefore advised that Casemix provides the costs of treating patients with similar conditions rather than the cost of individual procedures or patients. Furthermore, information on diagnosis was not collected by the NTPF for referred patients. This is an essential variable required for Casemix classification and may affect conclusions drawn regarding prices negotiated by the NTPF and the Casemix costs.

He pointed out that the cost for Grommets in its Casemix model for 2004, based on 2002 costs, was radically reduced following the revision of the Casemix system for the 2005 model. The casemix tool available to the NTPF in 2004 was the 2002 cost data, i.e. 2004 casemix Peer Group Review. Using the 2004 casemix price for grommets would result in the NTPF price amounting to 62% of casemix costs. The Department has acknowledged this apparent anomaly and is actively reviewing it.

Hospital Referral Pattern Analysis

In 2002 the NTPF published a Patient Information Booklet and this was revised and reissued in 2004. Both booklets suggest that it is more likely that a patient will be treated in a private rather than a public hospital

- *The NTPF will then proceed and arrange treatment for you in most cases in a private hospital*
- *In a small number of cases, you may receive treatment within a public hospital in Ireland.*

My examination considered the extent to which NTPF procedures were carried out in private or public hospitals and the extent to which a patient was treated in the same hospital from which s/he was referred albeit via the NTPF. The results of this part of my examination are set out in Table 43.

Table 43 Referral Patterns of Hospitals utilising NTPF Services

	Total Referred	Public to Private Referrals	Public to Public Referrals	Public to Public %	Same Hospital Referrals	Same Hospital Referrals %
Cataracts	1,467	950	517	35%	511	35%
Varicose Veins (one leg)	657	564	93	14%	79	12%
Total Hip Replacement (excluding Revisions)	460	80	380	83%	205	45%
Skin Lesions (Simple)	352	86	266	76%	260	74%
Coronary Angiogram	333	240	93	28%	89	27%
Total Knee Replacement (excluding Revisions)	205	76	129	63%	62	30%
Grommets (< 17 years)	191	26	165	86%	128	67%
Laparascopic Cholecysectomy	144	113	31	22%	30	21%
Total	**3,809**	**2,135**	**1,674**	**44%**	**1,364**	**36%**

Of the 3,809 cases examined 1,674 or 44% were carried out in a public hospital. This is consistent with NTPF statistics for all treatments procured by it in 2004. Referrals to public hospitals for treatment ranged from 14% for varicose veins to 86% for Grommets.

An examination of referral patterns for the eight procedures sampled revealed that 36% of procedures (out of a total of 3,809) were carried out in the same public hospital from which the referral had been made. Same hospital referrals over the eight procedures ranged from 12% for varicose vein procedures to 74% for procedures to remove skin lesions.

It was also established that the documentation maintained by the NTPF did not systematically record information relating to the referring consultant and the consultant carrying out the surgical procedure to enable the NTPF to guard against the risk of excessive self-referral. However, the NTPF maintains that the referring and treating consultants are known to it. The NTPF informed me that its new patient management system, implemented in July 2005 incorporates processes to obtain this information in every case and thus strengthen the information base from which the NTPF can operate its monitoring activities.

Given the extent of same hospital referral of waiting list patients as outlined in Table 43, I asked the Accounting Officer to explain how it is possible for each of these hospitals to have a waiting list problem for the procedures in question and, at the same time, a capacity to undertake a substantial number of additional treatments requested by the NTPF.

Accounting Officer's Response

The Accounting Officer informed me that the predecessor of the NTPF Board had agreed that, for 2004, the use of public capacity could account for 30% of total NTPF activity, once public core service planned activity was not compromised. The Department has recently advised NTPF that use by the Fund of public facilities should be limited to 10% of its total referrals for treatment.

He pointed out that there were several reasons why it was imperative to use public capacity for shortening waiting times for surgery. It is acknowledged that minimal paediatrics capacity (in terms of both volume and expertise) exists in the private sector. In order to offer the benefits of NTPF to children there may be no other option but to utilise spare public capacity.

Other situations that compelled the use of public or "in-house" capacity were cases where for reasons of clinical or patient complexity it was clearly best practice to have certain patients treated by their own Consultant in the hospital where they were on the waiting list. Not to have used this facility would have effectively barred this cohort of patients from accessing the NTPF scheme. The NTPF considers that these activities should be excluded from the computation of the referral patterns in Table 43. This would have the effect of disregarding all public hospital to public hospital referrals for Total Hip Replacement, Total Knee Replacement and Grommets.

The Accounting Officer added that according to the Health Strategy, the NTPF might make use of spare capacity in public hospitals and pointed out that elective activity in hospitals does not take place 24 hours per day and 7 days a week. Therefore using theatres and beds outside of normal working hours is one way of creating extra elective capacity. Allowing public hospitals to undertake work under the NTPF initiative also incentivises hospitals to perform extra work and to treat more patients over and above core funded activity.

Same hospital referrals are necessary where the level of expertise provided is not readily available in other hospitals. This expertise is required for complex surgery, in the case of elderly patients and where children are involved. This activity is carried out often by staff working overtime, who come in at weekends or who extend theatre time on occasions.

Waiting Lists

The Department last published quarterly waiting list data to 31 December 2003. Waiting list data for 2003 is summarised in Table 44.

Table 44 Public In-patient Waiting List 2003 Target Specialties[29] Summaries

	3 to 6 Months	6 to 12 Months	12 to 24 Months	24 months Plus	Total
Number of Adults Waiting for Target Specialties					
March 2003	3,780	4,394	2,488	2,294	**12,956**
June 2003	4,023	4,327	2,308	1,944	**12,602**
September 2003	4,145	4,238	2,165	1,493	**12,041**
December 2003	4,245	4,472	2,080	1,257	**12,054**
Number of Children Waiting for Target Specialties					
March 2003	485	376	204	117	**1,182**
June 2003	554	368	195	113	**1,230**
September 2003	672	490	168	76	**1,406**
December 2003	483	522	129	61	**1,195**

While no waiting list figures have been published in respect of 2004, the numbers of patients awaiting treatment at the end of 2004 will undoubtedly have improved and stabilised relative to what might have been expected as a result of

- The 23,000 treatments purchased by the NTPF
- The residual impact of the final tranche of WLI funding of €44 million in 2003
- Other initiatives implemented by Ministers since 2001.

In May 2004, the Minister announced the transfer of responsibility for the collation and publication of surgical waiting list data to the National Treatment Purchase Fund (NTPF). At the same time the NTPF indicated that in excess of 4,000 patients could be removed from the Department's reported figure and that it was expected that additional removals would result from further validation of the data by the NTPF. In October 2004, the NTPF conducted an analysis of waiting list data from hospitals, which indicated that

- Data focuses on volumes, not length of time patients are waiting
- Statistics had not been validated and were not reconcilable from one period to the next
- Data did not capture changes in patients' status, i.e. treated, temporary unavailability, no longer in need of treatment

[29] Cardiac Surgery, E.N.T., Gynaecology, Opthalmology, Orthopaedics, Plastic Surgery, General Surgery, Urology, Vascular.

- Data were not treated in a consistent manner and could be up to 6 months out of date.

As I was concerned that access to reliable and independently verified data on patients awaiting treatment is essential to be able to assess the impact of the NTPF initiative on the treatment backlog, I sought the Accounting Officer's observations.

Accounting Officer's Response

In his response, the Accounting Officer pointed out that over the period of the Waiting List Initiative, the Department had sought to improve waiting lists reporting by Health Boards and Voluntary Hospitals. The 2001 Health Strategy specifically acknowledged the need to further improve the management of waiting lists and as a result responsibility for waiting lists was transferred to the NTPF.

He confirmed that as a result of NTPF analysis of waiting list data, NTPF decided in December 2004 not to publish waiting list figures, but instead opted to develop a National Patient Treatment Register which would focus on the waiting times of individual patients rather than statistically based waiting lists. It was announced in May 2005 that it was intended that the register would be implemented on a phased basis in 2005. Funding of €1 million has been provided from within the NTPF's allocation for this in 2005.

Waiting list data for this register will be supplied to the NTPF by individual hospitals. The Register will contain patient specific details (including name and contact details for the first time) as forwarded by hospitals. Patients waiting for treatment the longest can now be identified and will be contacted by the NTPF with an offer of treatment.

It is intended that the register will

- Track the progress achieved in reducing waiting times
- Be accessible to patients and General Practitioners
- Show patient status
- Provide the healthcare system with an accessible and accurate tool for waiting list data, and a tool that reconciles changes in patient status
- Inform patients and GPs about prospective waiting times and referral choices
- Assist in reducing waiting times to achieve the Health Strategy commitment that all patients on in-patient and day cases waiting lists will be treated within three months.

NTPF point out that the register will be a national on-line system and will capture current patient status. Hospitals will continue to be responsible for validating and changing patient status on the system. NTPF will operate an audit process of the system.

Chapter 15

Department of Social and Family Affairs

15.1 Personal Public Service Numbers

The PPS Number is a unique client identifier used by Departments and Agencies for accessing Government Services. PPS numbers are issued by the Department of Social and Family Affairs (the Department) and up to 1991 had also been issued by the Revenue Commissioners (as the Revenue and Social Insurance number – RSI).

The Department's Central Records System (CRS) currently holds about 5.9 million records and is the core of the Department's client oriented functions. It is the source database for the new Public Service Identity (PSI) system provided for in the Social Welfare (Miscellaneous Provisions) Act, 2002.

The Department set up the Client Identity Service (CIS) in 2000 to manage the PPS number registration system.

Issue of PPS Numbers

Table 45 gives details of PPS numbers issued in the last 4 years.

Source	2001	2002	2003	2004
Newborns	56,000	71,000	63,000	69,000
Local Offices	111,000	92,000	78,000	123,000
Asylum Seekers	10,000	11,000	8,000	4,000
Other	45,000	45,000	44,000	25,000
Total	**222,000**	**219,000**	**193,000**	**221,000**

Table 46 shows a breakdown of applications in 2004 by EU and non-EU nationals.

Nationality	Number
Ireland	87,000
EU States excluding Accession States	38,000
EU Accession States[30]	58,000
Other Countries	36,000
Total	**221,000**

Registrations at Birth

PPS numbers now issue automatically following communication of birth registration from the General Register Office's recently developed computerised civil registration service. All major hospitals provide inputs to the system.

Local Office Applications

General applications for PPS numbers are mainly processed by 125 local and branch offices. Applications must be supported by birth certificate and/or valid photographic identity e.g. Passport or National Identity Card and evidence of residence in the State. Applicants are also required to state the reason for their application.

[30] Since May 2004

Staff are required to check the authenticity of supporting documents and refer doubtful cases for checking by document fraud experts. Suspect documents cannot be held if applicants insist on their return. From August 2004, local office staff were instructed to refuse applications only where there was proof of identity fraud. A tolerance is allowed where some non-nationals may not be able to produce certain documents.

Asylum Seekers

PPS number applications by asylum seekers who have obtained identity cards from the Office of the Refugee Applications Commissioner are processed by a dedicated unit in liaison with that office.

Other Applications

Community Welfare Officers employed by Health Boards allocate PPS numbers to applicants for Supplementary Welfare Allowance who do not have a PPS number.

The Pension Services Office allocates PPS numbers to pension applicants who have not previously got a PPS number, mostly non-resident cases with pension entitlements in Ireland including pre-1953 cases.

PPS numbers are allocated by individual scheme units to persons who make application for a welfare scheme but who are not previously registered.

Client Identity Service also issues PPS numbers, mainly to solicitors in respect of estate cases.

Recent Reviews of the CRS System

Reviews and audits have been carried out on the system for processing and registering applications for PPS numbers in the past five years as follows

- Internal Evaluation of Identity Fraud - 2000
- Internal Audit Review – 2003
- Southern Region Identity Project – 2004
- External Data Quality Audit – 2004.

The reviews indicated that

System Issues

- More than one PPS number could be allocated to a client when processing was completed on the same day by different members of staff. In a test 41 duplicates were found in one month.
- The system name check facility to establish that a PPS number had not already been allocated to the client was not applied to non-nationals because the system did not recognise foreign names
- Fraudulently obtained PPS numbers could not be deleted, flagged or rendered unusable.

Processing Issues

- 32,000 PRSI contribution records forwarded by Revenue could not be traced
- Source documents were not being requested or verified where exceptional or one-off applications *e.g.* estate cases, were being made. There were no checks on further activity in these cases
- Key fields on client records were not always completed or accurate. An external audit of data consistency and completeness in 2004 found an overall level of quality of 88%. 10,000 invalid PPS numbers needed to be corrected or purged and 35,000 – 50,000 cases needed address amendments
- Acceptance of asylum seekers' identity cards conflicted with the rigid demands made of other applicants.

Consequences

- Many bogus applicants already had PPS numbers and frequently were asylum seekers in receipt of state benefits
- The use of bogus PPS numbers was giving their holders entitlements to welfare benefits
- The internal evaluation in 2000 tested a random sample of 1,593 PPS numbers issued to purported EU applicants (deemed high risk). 10% of these turned out to have been fraudulently obtained. There was also a significant number of 'suspicious' other cases.
- The internal evaluation in 2000 estimated losses at €25 million to €50 million per annum
- PPS numbers could be used to help open bank accounts, obtain credit cards etc. The system might be discredited
- A Client Identity Service Control (CIS Control) investigation into employers' recruitment practices confirmed that considerable numbers of PPS numbers had been obtained on foot of false documentation or were being used by persons to whom they did not belong.
- The work permit system was being circumvented by identity fraud.

Review Recommendations

Key recommendations made arising from these reviews were to

- Implement procedures for notifying and flagging misused numbers
- Notify employers of the requirements for employing non-nationals
- Establish a multi-agency task force to recommend action on identity fraud.

How these findings were addressed by the Department

The main actions taken by the Department in response to these findings were to

- Put in place a training programme to create an awareness of identity fraud and control needs
- Introduce more rigorous processing at public counters
- Install ultra-violet scanning equipment
- Ask suspect applicants to apply in the language of their declared nationality

- Refer suspect cases to CIS Control for investigation.

In 2003, the Department established a liaison with the Garda National Immigration Bureau. This liaison has resulted in estimated monthly savings of approximately €300,000 mainly from asylum seekers involved in identity and welfare fraud.

Revenue Internal Audit – 2004

An internal audit carried out by the Revenue Internal Audit Unit confirmed that improperly obtained PPS numbers were used to access State services and benefits and that non-nationals, in particular, presented a serious risk. The absence of tax record details on such persons was a problem. It also found that passports and driving licences could no longer be relied on as means of identity. Checks over a 2-week period at the public counter of the Central Revenue Information Office cast doubts on the validity of the identity of 70 callers who presented a PPS number at the counter. Revenue Internal Audit was of the view that there was a low level of awareness of identity fraud issues and related abuses among Revenue staff.

The audit unit recommended formalising communications with the Department to ensure appropriate action is taken by Revenue in identity fraud cases. It also recommended a working group to counter the risks to Revenue posed by such fraud.

Client Identity Service Control (CIS Control)

Referral Activity

The Department's CIS Control monitors identity fraud issues, assists in drawing up procedures for processing applications, investigates suspect documents and provides document recognition training to Local Offices. Table 47 provides details of Local Office referrals to CIS Control for 2002 to 2004.

Table 47

Year	2002	2003	2004
Number of referrals	635	466	752
Number of referrals found fraudulent	204	142	324
Arrests	12	44	69

An analysis of the fraudulent cases for 2004 shows that 303 of the applications were from non-nationals who presented false/forged documents purporting to be from EU States, 20 were other non-national documents and 1 was Irish documentation.

Monitoring Activity

CIS Control monitors the issue of PPS numbers in Local/Branch offices for unusual trends, mainly the targeting of offices by human traffickers.

- An examination of the PPS Number application process at a Branch Office revealed extensive non-compliance with Departmental procedures between 2001 and 2003
- Branch Office Inspections carried out in 2004 revealed risk patterns in 4 Branch Offices during 2004. 95 bogus applications were found at 3 offices with a smaller number in the other.

- An inspection of 'hijacked'[31] PPS numbers at an employment agency, found 35 cases where false/forged documentation had been supplied in support of applications for employment. A data matching exercise with the agency's records revealed up to 20 cases of double identity where Supplementary Welfare Allowance was claimed under one of the identities.
- 314 compromised PPS numbers were identified in extended tests, including cases claiming welfare under an alternative PPS Number.

Audit Assessment

My review of the processing and control systems in place indicates that the detection of identity fraud and the prevention of issue of PPS numbers to bogus applicants or the issue of duplicate PPS numbers to persons already in possession of a valid PPS number is very much dependent on the vigilance of counter staff. It is vitally important that these staff have sufficient back up available to them and the support of a tried and tested quality assurance system.

The completeness and accuracy of data on CRS is vital to ensure the reliability of client identification available to the Department. This is even more crucial since the database is to be the foundation of the proposed new Public Service Identity System. It is clear that the principle of a unique identifying number for each client is fundamental to the success of that project. At the same time the Department's welfare and social insurance schemes, and the Revenue Commissioners' tax collection systems are dependent on the integrity of the data underpinning the CRS.

My review of the operation of the CIS Control unit found that

- Investigation work has been beneficial in identifying bogus registrations
- The Unit is also beneficial in detecting abuses of the welfare system
- There are difficulties in establishing the real identities of some suspect cases
- There is need for adequate resources to ensure bogus cases are promptly dealt with
- There is need for feedback on cases referred to other sections and agencies for follow up
- There is also need for a structured approach to tackling identity fraud among potentially affected agencies.

In the light of the importance of the system for allocating PPS numbers, I sought the Accounting Officer's views on the findings of my examination.

Accounting Officer's Response

The Accounting Officer agreed that the history of the issuance of RSI/PPS numbers reveals considerable shortcomings. As a general comment, he was of the view that the position overall was better than the audit assessment appeared to indicate. As well as putting in place and continuously improving operational structures, the Department had taken a strategic approach to improving the functions of the PPS number and this had led to the development of a number of strategic projects.

[31] Legitimately obtained PPS numbers which are irregularly used by another.

When the Department took over the PPS number registration process in 2000, it was recognised from the outset that the CRS database had been in existence from 1979. It was not at that time envisaged that the RSI Number (now the PPS Number) and related data would be used for the purpose of supporting all public services. His Department recognised that the system required improvement. An external audit, commissioned by the Department in 1996 found that, where the Department held data, it tended to be accurate but did note areas where data was incomplete. He is of the view that considerable improvement in the integrity of the data has been achieved. This is evidenced by improvements shown in Table 48.

Table 48 Trends in Data Quality 1998 to 2004

Date	January 1998	February 2002	February2004	December 2004
Total Clients	5,336,795	4,823,257	5,187,193	5,298,078
With Date of Birth	86.89%	94.03%	94.83%	95.3%
With a Verified Date of Birth	34%	64%	68%	70.0%
Mother's Birth Surname	42%	65%	68.3%	70.0%

The CIS policy on data cleanup has been that direct contact with the client has not been considered necessary, efficient or optimal from the client service perspective when other areas of the Department are already in contact. However, CIS is examining situations where a number of agencies have had difficulty establishing the correct data for a client and is considering contacting the client in these instances.

He said that significant measures have been and are being taken to deal with both the results of the historical shortcomings and with future challenges in this area. He pointed out that, while the Department has taken a lead in implementing several measures of importance within the overall 'eGovernment' area, the topic cannot be considered solely as being one within its area of responsibility. Proposals in connection with the development of a framework for a public service card, known as the Standard Authentication Framework Environment or SAFE, and based on the PPS number, are currently being worked on under the aegis of an interdepartmental group and, associated with this, proposals are being developed for a national identity management and privacy protection policy. It is expected that this programme of work will be completed within the next 18 months.

Departmental Role

It is the Department's view that its responsibilities centres around the registration process, leading to the allocation of a PPS Number, and subsequent authentication and eligibility checking in respect of its own services. While the Department is aware of the value of possession of the PPS Number it would not be practicable for the Department to pursue the eligibility aspect of the use of the PPS Number for all these other users' purposes or to pursue written confirmation of their clients' reason for obtaining the PPS number.

He stated that the Department supports other agencies in their establishment and use of the PPS Number. Agencies have been issued with a Code of Practice on the PPS Number, which lists the documents that can link the PPS Number to the individual. Likewise, an information leaflet on the PPS number also addresses this. Employers have been advised by Revenue to seek back up confirmation that the quoted PPS Number belongs to the individual using it.

Identity Fraud

The Department has always been aware of identity fraud in the context of persons claiming social welfare benefits. There are legitimate concerns about 'identity fraud' and a need for a robust control system to address these concerns. The Department has an ongoing operational strategy under development for further improvement in identity fraud controls. Since 2000, considerable progress has been made in advancing and improving this area of work although there is, undoubtedly, scope for further improvement. Allocation of the PPS Number as an identity reference number needs to focus on the production of sufficient evidence to establish the uniqueness and integrity of the identity. Procedures at registration, and supporting structures *e.g.* CIS Control, have concentrated on supporting the detection of bogus identities at registration.

The Accounting Officer pointed out that Internal Evaluation of Identity Fraud in 2000, which estimated potential losses from identity fraud of between €25 million to €50 million, was carried out soon after the Department had taken sole control of the registration process. The estimate was highly speculative and based on the possibility of fraudulent claiming rather than on actual experience.

Operational Structures

He informed me that the Department is satisfied that counter staff in local offices are fully competent to perform the PPS number registration function with appropriate back-up services and this is the approach which is being taken.

A planned reduction of the number of offices allocating PPS Numbers to one per county will allow for increased co-ordination and the dissemination of document expertise. CIS Control will be able to support an increased co-ordination and training role. It is not proposed that a back office function will be established, as this would not support the face-to-face process.

The Department also plans to incorporate its inspectorate more closely in this work, in order to increase its focus on the issue of hijacked and bogus identities, as well as improving the support to local offices at registration.

The Accounting Officer indicated that major improvement plans included flagging temporary and inactive PPS numbers, highlighting numbers requiring an identity recheck and the possible publication of suspect numbers. In this regard the Department is engaged in a process of flagging inactive or dormant records and to date 600,000 have been flagged.

Legal advice has been obtained which states that the Department can retain documentation for checking and the introduction of a specific supportive legislative provision is also under consideration.

The Department plans to remove the PPS number allocation function from Branch offices and negotiations have already commenced on this.

In relation to "recent arrivals in the country", the Department has data sharing arrangements with the Garda National Immigration Bureau and Office of the Refugee Applications Commissioner for increased cross-departmental co-operation on identity procedures for those with limited identity documentation. The Department considered an Internal Audit recommendation for an alternative numbering system for asylum seekers but rejected the recommendation as being contrary to the policy of a single unique identifier for all public services.

Fraud and Error Surveys/Identity checks

Since 2004, a client identity check has been included as an integral part of the fraud and error survey process. Inspectors are asked specifically to confirm identity as part of their investigations. Surveys have been undertaken and completed on the Child Benefit and Family Income Supplement Schemes, with resulting fraud and error rates of 2.3% and 3.2% respectively. Identity was not a significant issue for either of these schemes. A survey on the Disability Allowance scheme, which commenced in early 2005, is almost completed; the initial indications are that identity is also not a significant issue for this scheme.

15.2 Agency Services - Encashments

The Department of Social and Family Affairs makes payments to its customers by means of cheques, electronic fund transfers (EFT), personalised payable orders (PPOs), post drafts and postal vouchers. Up to 59 million payment instruments are issued annually.

Charges to the accounting records of the Department are based on statements of encashment received from An Post and on payment issue records from the bank. A fundamental control in the preparation of the financial statements is the reconciliation of An Post/Bank statements to the accounting records involving the matching of payments issued to encashments. A number of matters were identified on audit as follows

An Post

- The service agreement with An Post requires it to supply to the Minister — before the 31st day of March in each year — statements, certified by An Post's statutory auditors, of the volume and value of transactions processed by it in the preceding year. None have been provided in recent years.
- Over a period of three and a half years, An Post claimed almost €2 million in respect of encashment documentation categorised as 'Lost in Transit' but no details were provided.
- The matching of the Department's record of issues to claims for their encashment by An Post revealed unreconciled items totalling in excess of €800,000. The types of unreconciled items were; no apparent issue; wrong amount; cashed after it had already been cashed; cashed after stopped. An Post applied stop payment notifications in only 40% of cases.
- The full value of An Post claims including items in dispute was charged to the accounting records as scheme expenditure.

Banks

The reconciliation of bank balances to the accounting records for old Punt accounts and recently opened euro accounts revealed unexplained differences. The differences on four of the Punt accounts were charged to scheme expenditure. The Department could not provide listings of outstanding cheques.

I sought the views of the Accounting Officer on these matters.

Accounting Officer's Response

Payment and Agency Reconciliation Project

The Accounting Officer informed me that work on a new Payment and Agency Reconciliation Project (PARP) commenced in autumn 2002 following a detailed internal review which highlighted a number of issues including difficulties in reconciling some of the Department's bank and An Post accounts.

The objective of PARP is to provide an integrated reconciliation solution, which will reconcile all the Department's payment instruments and the associated agency accounts. The systems to be replaced have been in operation since 1986 and are not linked to the Department's main financial recording system. The project is now proceeding to tender and implementation stages. It is envisaged that a new system will be in place by end 2007.

An Post

Reconciliation of Claims

The Accounting Officer stated that An Post provides the Department with monthly claims. The procedures used to reconcile these claims have been in existence since the introduction of the service agreement with An Post.

The Department has identified some changes that are necessary to the existing accounting arrangements and is consulting with An Post with a view to having these changes effected.

While the majority of the encashments reported by An Post can be verified, there are always small numbers of exceptions. An Post is notified of these exceptions. The current systems and accounting arrangements do not provide the Department with an independent means of verifying whether these exceptions have been reflected in amendments to the claims submitted to it by An Post.

The Department is also pursuing the introduction of new procedures to facilitate the handling of exceptions and the introduction of suspense accounts pending resolution of exceptions.

An Post has, to date, declined to make any changes to the current arrangements as its accounting systems cannot accommodate the changes proposed because of the level of detail required by the Department. The Department's proposals would require fundamental changes to An Post's systems and it is not in a position to make these changes.

The Accounting Officer said that it may not be possible to effect any change in the Department – An Post arrangements until a new service agreement comes into force. The Department is however reviewing accounting procedures for the An Post account, to determine if some changes to the existing arrangements can be effected independently of An Post.

Certified Statements

As regards the provision of certified statements, the Accounting Officer confirmed that An Post has not supplied certified statements for a number of years. It was not possible to have this certification shortcoming rectified in time for the 2003 Annual Statement. For 2004, An Post was formally notified in January 2005 that a statement certified by their Statutory Auditors would be required. This certification was to be provided before 31 March 2005, but has not been received to date.

'Lost in Transit' Claims

The Accounting Officer informed me that claims in respect of lost encashment documentation for the period November 2000 to June 2004 arose when this documentation failed to turn up at An Post processing offices. A particular problem related to some of the 467 non-automated post offices.

Following a review by the Department's Internal Audit, An Post was requested in January 2005 to

- Consider the introduction of more secure and accountable arrangements to handle and manage encashment documentation
- Submit claims to the Department in respect of lost documentation from post offices in a more timely fashion.

Claims made by An Post for post offices that make high value and recurring 'lost in transit' claims were also of concern to the Department.

The Department has asked An Post

- For details of the actions taken to investigate high value and recurring claims
- To outline measures introduced to prevent further repeat claims for lost documentation.

Reconciliation Exceptions

The Accounting Officer outlined the position in relation to each type of personalised payable order exception referred to

No Apparent Issue

These occur where there is an encashment but no corresponding issue. An Post has rejected claims made by the Department for these and has consistently maintained that they were valid encashments but, arise due to scanning errors or errors in the Department's issue records.

In January 2005, An Post disputed a claim for €167,000 made by the Department for these on the basis that they arose because of printing errors. The Department has raised the issue of print quality with its printers. The rate of exception in this instance is consistent with the print error rate of 0.003% and 0.006% considered by the printers as inevitable.

The Department is currently reviewing its options in relation to these cases. The Department may insist that An Post recovers all the relevant vouchers to physically confirm they are valid encashments. This would however incur additional costs for both the Department and An Post.

It may pursue other options to provide a better value for money solution.

Wrong amount cashed

Where the encashment amount differs from the issue amount An Post has undertaken to reimburse the Department.

Cashed after Cashed

This category arises where a payment item is cashed twice in error by the post office. An Post has not accepted this claim category and has not reimbursed the Department to date.

Wrong Amount and Cashed after Cashed claims for the period 2001(part) – 2004 amounting to €631,542 were notified to An Post in April 2004 and January 2005.

Cashed after stopped

These cases arise when the Department requests An Post not to cash a voucher (i.e. place a stop on it) but the voucher is still paid by the post office.

The Department's systems automatically refer such cases for investigation to line sections. An Post is billed for overpayments arising due to post office error. Otherwise the matter is referred to the Department's Debt Management Section for follow-up recovery of the overpayment.

In 2004, approximately 4,250 cases were investigated by the line sections. Refunds were sought from An Post in 67 instances. An Post refunded €31,000 in respect of 47 cases.

Banks

The Accounting Officer informed me that the reconciliation differences with the banks have arisen as a result of the complex nature of current reconciliation processes.

Reconciliations were finalised on four Punt Accounts in August 2003. Any remaining balances on the bank statements were transferred to the parallel EURO bank accounts. Unreconciled balances, which relate mainly to unmatched cheque payments, were re-charged to scheme expenditure.

In parallel with the PARP project, considerable work has taken place to resolve unreconciled differences. Progress has been achieved and appropriate adjustments reflected in the accounts. Work continues to resolve the remaining unreconciled amounts. The Accounting Officer informed me that at the end of the process, Department of Finance sanction may be sought to write off or otherwise resolve any remaining unreconciled amounts.

A detailed report of outstanding cheques is not currently available. Steps have been taken to address this particular concern and it is expected that listings will be available for the audit of the 2004 Social Insurance Fund financial statements.

15.3 Overpayments

The Department of Social and Family Affairs administers some 50 welfare schemes paid through Vote 38 and the Social Insurance Fund. Expenditure on assistance and insurance schemes was €5.82bn and €5.08bn respectively in 2004.

Tables 49, 50, 51 and 52 outline overall expenditure on various schemes over the period 2000 to 2004, and for the same period, the amounts recorded as overpayments, the amounts of overpayments attributed to fraud or suspected fraud and the Department's cumulative record of recovery since 2000.

Table 49 Scheme Expenditure

	2000 €m	2001 €m	2002 €m	2003 €m	2004 €m
Social Insurance	2,993	3,517	4,198	4,649	5,081
Social Assistance	3,425	3,983	4,940	5,460	5,821
Total	**6,418**	**7,500**	**9,138**	**10,109**	**10,902**

Table 50 Number and Amount of overpayments recorded for recovery (Numbers shown in brackets)

	2000 €m	2001 €m	2002 €m	2003 €m	2004 €m
Social Insurance	6.39	6.79	9.72	10.60	12.04
	(15,252)	(15,786)	(23,723)	(26,174)	(26,131)
Social Assistance	20.59	19.26	19.41	28.77	44.23
	(18,110)	(14,274)	(15,084)	(17,459)	(20,000)
Total	**26.98**	**26.05**	**29.13**	**39.37**	**56.27**
	(33,362)	**(30,060)**	**(38,807)**	**(43,633)**	**(46,131)**

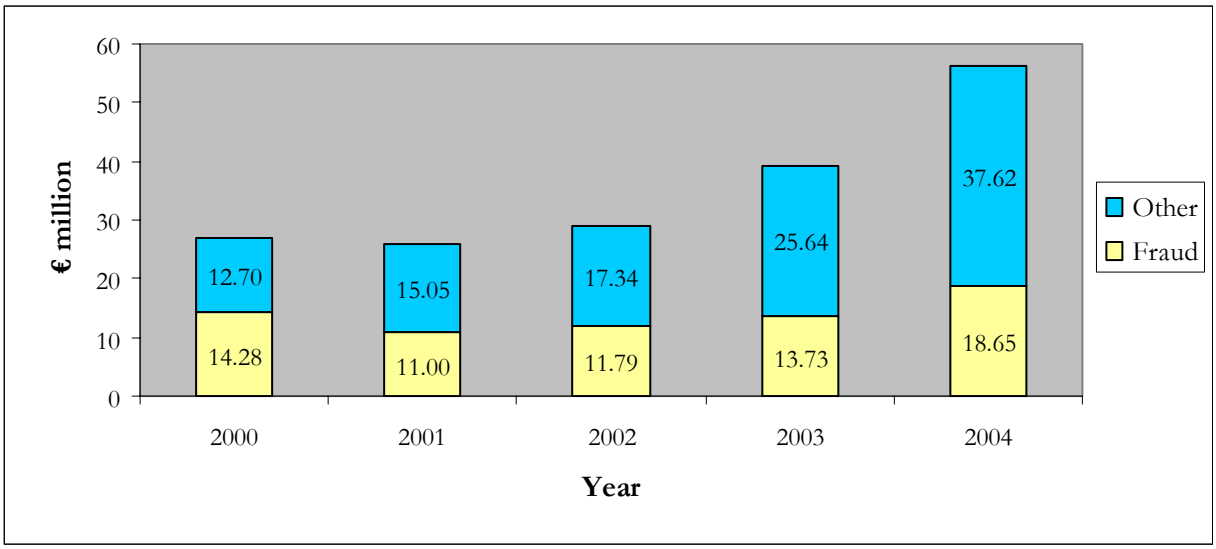
The increase in the value of Social Assistance overpayments recorded in 2004 was mainly attributable to the specific targeting in that year by the Department's Earnings Review Unit of persons in receipt of Unmarried Lone Parent and One Parent Family payments. This work had commenced in 2003. See also Table 51 below

Table 51 - Number and Amount of overpayments attributed to fraud or suspected fraud (Numbers shown in brackets)

	2000 €m	2001 €m	2002 €m	2003 €m	2004 €m
Social Insurance	3.39	3.27	4.43	5.00	6.19
	(5,159)	(5,321)	(8,089)	(9,567)	(10,723)
Social Assistance	10.89	7.73	7.36	8.73	12.46
	(7,466)	(5,350)	(5,696)	(7,114)	(8,435)
Total	**14.28**	**11.00**	**11.79**	**13.73**	**18.65**
	(12,625)	**(10,671)**	**(13,785)**	**(16,681)**	**(19,158)**

The amount of overpayments attributed to fraud or suspected fraud compared to total overpayments since 2000 is summarised in Figure 1.

Figure 1



The Department's record of recovery of overpayments during the period 2000 to 2004 is shown in Table 52.

Table 52 Departments record of recovery of overpayments 2000 to 2004

	2000 €'000	2001 €'000	2002 €'000	2003 €'000	2004 €'000
Overpayments not disposed of at 1January	60,581	64,374	65,452	70,621	85,953
Overpayments recorded for recovery	26,982	26,049	29,130	39,367	56,275
Less					
Overpayments recorded in prior years cancelled	(447)	(668)	(394)	(381)	(693)
Sums recovered in cash	(7,464)	(9,873)	(8,892)	(10,397)	(11,506)
Sums withheld from current entitlements	(4,999)	(5,185)	(6,734)	(6,521)	(8,332)
Net amounts written off as irrecoverable	(10,279)	(9,245)	(7,941)	(6,736)	(6,396)
Overpayments not disposed of at 31 December	**64,374**	**65,452**	**70,621**	**85,953**	**115,301**

Of the €115,300,783 overpayments outstanding at 31 December 2004 - €42,531,270 dates from 2004; €24,614,415 from 2003; €14,817,063 from 2002 and €33,338,035 from earlier years.

Shortcomings in the Overpayments Recording System

In my Value for Money Report on the Evaluation of Control Activity in the Department completed in November 2003 I drew attention to shortcomings in the system for recording overpayments.

In 2004, the Department's Internal Audit also drew attention to significant limitations in the reporting and recording system for overpayments. Other recent Internal Audit reports highlighted discrepancies between the records maintained by scheme payment sections and local office records and central overpayments system records.

Matters reported were

- Revised claim decisions applied from a current date simply to avoid having to raise an overpayment.
- Overpayments and recoveries not reported or substantially in arrears
- Recovery not pursued
- Recoveries notified to the overpayments system for which there was no corresponding overpayment record.

In the course of an audit of the Pensions Service Office carried out by my Office in February 2005, it was found that in a sample of overpayment records with ongoing recoveries some could not be traced to the overpayments system. This finding was confirmed by a matching exercise which had been independently carried out by the Department and which had identified 1,947 such records.

In view of the importance of the overpayments data as a measure of the Department's performance in relation to the proper distribution of welfare payments and the effectiveness of control activity, I asked the Accounting Officer for his observations on issues highlighted by his Department's own reviews and those arising from my audit. In particular, I invited his comments on the accuracy of the data provided by the overpayments system.

Accounting Officer's Response

The Accounting Officer informed me that the computer system for recording overpayments and recovery details currently in use in the Department has been in place since 1987. It is essentially a stand-alone system and does not interface with the Department's other computer systems. It requires a high degree of manual inputting of data, which is a time consuming process.

The manual nature of the notifications of overpayments and recoveries as well as the number of steps to be taken means there is a time lag between the overpayment/recovery occurring and the recording of the information on the system. The result is that data on the overpayments system is not always up to date. There is an increased likelihood of incomplete or incorrect data being entered on the database as well as the omission of other data from the database. The process is both slow and labour intensive.

He added that while management in Disability Benefit Unit disputed the extent to which revised decisions were applied from a current date, additional measures were put in place following the internal audit to ensure that the correct procedures were followed. As legislative provisions require that retrospective decisions should apply in all fraud cases guidelines are being prepared to emphasise this and ensure consistent application across all schemes.

As regards the problems experienced in the Pensions Service Office, he said it was unclear whether the recovery details in question had been notified for updating onto the overpayment system. These cases are now being examined in order to establish the amount recovered and whether the details have been

forwarded for updating to the overpayments system. They are time consuming to deal with and to date a total of over 600 of these cases have been dealt with.

He pointed out that the effective pursuit of overpayments on a continuous basis in respect of closed claims (customers not currently in receipt of welfare) is subject in a number of instances to the resources and other exigencies that exist in local offices. In 2004, four regions undertook projects to expedite the recovery of overpayments for closed claims. The projects have been evaluated and, as a result, guidelines are currently being drafted to develop best practice in local offices to ensure that available resources are targeted effectively with particular reference to customers who have returned to employment. In addition, procedures are being drafted to include a role for the Inspectorate in the process.

He informed me of initiatives taken recently to improve the accuracy, completeness and timeliness of the data on the current overpayments system

- All payment areas were reminded of their responsibilities in relation to overpayments and their recovery
- Cases where there have been difficulties associating recoveries with the relevant overpayments were examined and as many of these as possible were entered on the overpayments system in time to be reflected in the 2004 accounts. Unresolved cases have been sent to the relevant pay area for additional details.
- The first phase of a new overpayments system is scheduled to go live early in 2006.

15.4 Prosecutions

Cases involving abuse of the system are considered with a view to taking legal proceedings. Prosecutions are taken against employers who fail to carry out their statutory obligations and persons who defraud the social welfare payments system. Prosecutions can either be by summary or indictment proceedings. Civil proceedings are taken to facilitate the recovery of scheme overpayments or the collection of PRSI arrears. Such cases are only taken where it has been established that the debtor has sufficient means to discharge the debt.

During 2004, 476 criminal cases (2003 - 355 cases) were forwarded to the Chief State Solicitor's Office for prosecution as shown in Table 53.

Table 53 - Criminal cases forwarded to the Chief State Solicitor

	2004	2003
Unemployment Assistance	191	146
Unemployment Benefit	226	158
Disability Benefit	9	29
One Parent Family Payments	23	1
Other Schemes	10	7
Offences Committed by Employers	17	14
Total	**476**	**355**

A total of 259 criminal prosecutions (2003 – 186 prosecutions) involving social welfare recipients were finalised in court in 2004. The total amount of overpayments assessed in these cases of persons who attempted to or obtained benefits/assistance fraudulently was €1,116,492 (2003 - €1,007,332). The results of these 259 court cases and the penalties imposed are given in Table 54.

Table 54 - Results of Court Cases involving Social Welfare Recipients

	Fines Imposed[32]	Community Service	Imprisoned	Probation Act	Proven No Penalty	Adjourned/ Liberty to Re-enter	Bound to peace
Unemployment Assistance	63	2	21	21	8	7	3
Unemployment Benefit	67	1	12	17	6	-	4
Disability Benefit	12	-	2	5	1	-	-
One Parent Family payments	-	-	-	-	-	1	-
Other Schemes	2	-	1	-	3	-	-
Total	**144**	**3**	**36**	**43**	**18**	**8**	**7**

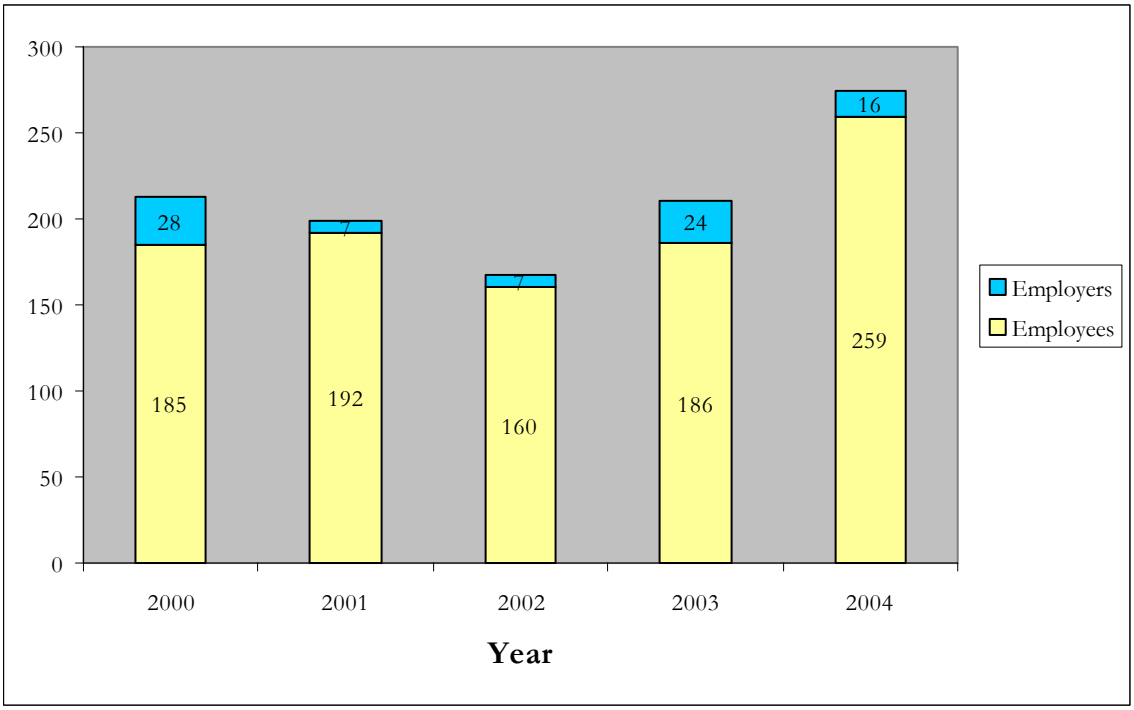
Prosecutions of 16 cases involving employers (2003 – 24 employers) were also finalised with 14 being fined[33] and 2 struck out.

[32] Fines to a value of €68,886 were imposed by the courts (€54,711 in 2003 in 93 cases)

[33] Fines to the value of €7,039 were imposed by the courts (2003: €15,228 in 16 cases).

The number of prosecutions finalised in the courts since 2000 is summarised in Figure 2.

Figure 2



A total of 68 civil cases have been forwarded to the Chief State Solicitor's Office since 2000. Table 55 details the history of civil cases forwarded and the cases still before the courts or awaiting a court date.

Table 55 Civil cases sent to the Chief State Solicitor's Office

	2000	2001	2002	2003	2004	Total
To CSSO	6	14	11	21	16	68
Finalised	1	5	1	2	2	11
Pending	5	9	10	19	14	57

Of the eleven cases finalised two have been recovered on civil bills, in one case a judgment mortgage has been awarded, six are being recovered by instalment and two were not pursued due to the circumstances of the debtor.

Chapter 16

National Treasury Management Agency

16.1 National Debt

The National Treasury Management Agency has the statutory function of borrowing moneys on behalf of the Exchequer and managing the National Debt on behalf of and subject to the control and general superintendence of the Minister for Finance.

Expenses incurred by the Agency in the performance of its functions are met from the Central Fund. The Agency incurred expenditure of €18.6m on administration in 2004 (€15.1m in 2003).

Under the provisions of section 12 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 on the Appropriation Accounts, to make also a report to Dáil Éireann regarding the correctness of the sums brought to account by the Agency in the year. The Agency's accounts for 2004 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 thereof before both Houses of the Oireachtas.

I am satisfied that the accounts properly present the transactions of the Agency in 2004 and its balances at year end.

Table 56 shows the outturn for the National Debt in the five year period 2000-2004.

Table 56 National Debt 2000 – 2004

	National Debt Outstanding €m	Debt Service Cost €m
2000	36,511	2,575
2001	36,183	2,379
2002	36,361	2,169
2003	37,610	2,277
2004	37,846	2,203

The composition of the National Debt[34] at 31 December 2004 is shown in Table 57.

Table 57 Composition of National Debt as at 31 December 2004

	€m
Medium/Long term Debt	31,864
Short term Debt	3,527
National Savings Schemes	4,518
Less: Domestic Liquid Assets	(2,063)
National Debt	37,846

The Agency's performance in regard to its activities is independently measured by an international accounting firm who are specifically engaged for that purpose. The rationale and basis of the performance measurement was agreed with the Department of Finance. It was determined that, measured on a net present value basis against an independent benchmark portfolio, savings attributable to the Agency's management in the year amounted to €28.44m.

[34] The National Debt is stated on the basis of nominal amounts of principal originally borrowed.

16.2 Savings Bank Fund

The audit of the Post Office Savings Bank is carried out on my behalf by the auditors of An Post subject to my right to carry out further audit tests which I consider necessary.

In 2005 they reported to me on their audit of the 2004 accounts. I accept their opinion that the accounts of the Post Office Savings Bank give a true and fair view of its transactions for that year-end and of its year-end balance.

In addition to managing the National Debt, the National Treasury Management Agency is responsible for the investment and management of funds remitted to the Exchequer by the Post Office Savings Bank. The Exchequer is responsible for the repayment to the Bank of all such funds and for meeting interest charges thereon.

The state of affairs of the fund at year-end is shown in Table 58.

Table 58 Post Office Savings Fund

	2004 €m	2003 €m
Liability in respect of funds due to depositors and creditors	1,304	1,126
Value of related investments held by Post Office Savings Bank Fund (at cost prices)[35]	1,315	1,136
Surplus at 31 December	11	10

[35] The market value of the investments held by the Fund was €1.2m more than their cost price.