# Comptroller and Auditor General

# Annual Report

# 2005

***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 — 2005

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 2005 in accordance with Section 3 of the aforementioned Act.

**JOHN PURCELL**

**Comptroller and Auditor General**

12 September 2006

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# Chapter 1

# General Matters

# 1.1 Financial Outturn

The publication *Audited Appropriation Accounts of Departments and Offices for 2005* (Prn.A6/0430) includes a summary which shows the amount to be surrendered as €774.84m. This is arrived at as shown in Table 1.

**Table 1 Outturn for the year 2005**

| | €000 | €000 | €000 |
|---|---|---|---|
| *Estimated Gross Expenditure* | | | |
| Original Estimates | 39,843,648 | | |
| Supplementary Estimates | 79,139 | | |
| Deferred Surrender 2004 | 236,967 | 40,159,754 | |
| *Deduct: -* | | | |
| *Estimated Appropriations-in-Aid* | | | |
| Original Estimates | 3,671,439 | | |
| Supplementary Estimates | (12,167) | 3,659,272 | |
| Estimated Net Expenditure | | | 36,500,482 |
| Actual Gross Expenditure | | 39,250,208 | |
| *Deduct: -* | | | |
| Actual Appropriations-in-Aid | | 3,813,835 | |
| Net Expenditure | | | 35,436,373 |
| Surplus for the Year | | | 1,064,109 |
| Deferred Surrender 2005 | | | 289,268 |
| **Amount to be Surrendered** | | | **€774,841** |

The amount to be surrendered represents 2.12% of Estimated Net Expenditure as compared with 1.72% in 2004.

## Extra Exchequer Receipts

Extra Receipts payable to the Exchequer as recorded in the Appropriation Accounts amounted to €252,052,839.

## Surrender of Balances of 2004 Votes

The balances due to be surrendered out of Votes for Public Services for the year ended 31 December 2004 amounted to €568m. 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

# Revenue

# 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 2.7 to 2.10 refer to matters arising from this examination.

## Revenue Collected

Revenue collected under its main headings in 2005 is shown in Table 2.

**Table 2 Revenue Collected[1]**

| | Gross Receipts €m | Repayments €m | 2005 Net Receipts €m | 2004 Net Receipts €m |
|---|---|---|---|---|
| Income Tax | 14,177 | 2,837 | 11,340 | 10,695 |
| Value Added Tax | 15,591 | 3,465 | 12,126 | 10,717 |
| Excise | 5,549 | 158 | 5,391 | 5,066 |
| Corporation Tax | 6,003 | 500 | 5,503 | 5,335 |
| Stamp Duties | 2,693 | 20 | 2,673 | 2,070 |
| Custom Duties | 234 | 8 | 226 | 174 |
| Capital Acquisitions Tax | 261 | 12 | 249 | 190 |
| Capital Gains Tax | 2,016 | 34 | 1,982 | 1,528 |
| **Total** | **46,524** | **7,034** | **39,490** | **35,775** |

Of the net receipts of €39,490m, a total of €168m was paid during 2005 under Section 3 of the Appropriation Act, 1999 from the proceeds of tobacco excise to the Vote for Health and Children. €39,240m was paid into the Exchequer which represented a prepayment of €250m. The amount prepaid at the end of 2004 was €332m.

[1] Total gross collection amounted to €54.2 billion as levies and fees such as PRSI (€7.5 billion), Health Levy (€139m) and Environmental Levy (€18m) are collected for other Departments.

# 2.2 Tax Written Off

The Revenue Commissioners have furnished me with details of the €143m of taxes and PRSI written off during the year ended 31 December 2005. 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 | 2005 €'000 | 2004 €'000 |
|---|---|---|
| Value Added Tax | 48,433 | 72,369 |
| PAYE | 23,992 | 36,862 |
| Corporation Tax | 15,431 | 8,326 |
| Income Tax | 23,839 | 16,385 |
| Capital Gains Tax | 2,264 | 868 |
| Other Taxes | 4,653 | 1,120 |
| PRSI | 24,689 | 36,618 |
| **Total** | **143,301** | **172,548** |

**Table 4 Grounds of Write Off**

| Grounds of write-off | 2005 No. of Cases | 2005 €'000 | 2004 No. of Cases | 2004 €'000 |
|---|---|---|---|---|
| Liquidation/Receivership/Bankruptcy | 1,263 | 69,928 | 2,097 | 88,519 |
| Ceased trading – no assets | 2,032 | 34,981 | 2,760 | 40,447 |
| Deceased and Estate Insolvent | 132 | 1,340 | 176 | 1,350 |
| Uneconomic to pursue | 60,911 | 19,358 | 19,359 | 23,162 |
| Unfounded Liability | 187 | 2,160 | 209 | 1,983 |
| Cannot be traced / Outside Jurisdiction | 588 | 9,680 | 586 | 9,615 |
| Compassionate Grounds | 206 | 1,627 | 248 | 2,322 |
| Uncollectible due to financial circumstances of taxpayer | 439 | 4,225 | 706 | 5,150 |
| Examinership | 4 | 2 | 0 | 0 |
| **Totals** | **65,762** | **143,301** | **26,141** | **172,548** |

In 2005, €3.9m 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 largest single amount written off in 2005 was €8.2m in respect of Corporation Tax owed by a company in receivership. There were five other cases where the amount written off was greater than €1m.

**Revenue**

The Internal Audit Branch in Revenue undertakes an annual examination of tax write offs. The 2005 audit examined a sample of 192 cases representing 32% (€45m) of the value of non-automated write offs (€140m). In one of the cases examined involving a write off of €211,200, the tax liability was based on system-generated estimates for a company which Internal Audit found had never traded. As a result of the internal audit, the write off was reversed and the estimate discharged instead. In another case involving the write off of €94,851, Internal Audit raised questions in relation to the evidence on file supporting the grounds of write–off i.e. compassionate grounds. The District concerned is re-examining the case and is to furnish a full report to Internal Audit on the outcome. Internal Audit also examined the results of the ten automated write off runs and confirmed the application of the authorised selection criteria for each run.

# 2.3 Outstanding Taxes and PRSI

Table 5 reflects the activities and transactions in the twelve-month period ended 31 March 2006. Table 6 sets out an aged analysis of the balance outstanding at 31 March 2006. 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 2006 | |
|---|---|---|---|---|---|---|---|
| **Balance at 31 March 2005** | **Tax or Levy** | **Net Charges Raised** | **Paid** | **Written Off** | **Balance at 31 March 2006** | **Under Appeal** | **Available for Collection** |
| **€m** | | **€m** | **€m** | **€m** | **€m** | **€m** | **€m** |
| 289 | VAT | 11,056 | 11,067 | 51 | 227 | 69 | 158 |
| 161 | PAYE | 10,100 | 10,106 | 18 | 137 | 1 | 136 |
| 176 | PRSI | 7,350 | 7,340 | 21 | 165 | 1 | 164 |
| 292 | Income Tax (Excluding PAYE) | 2,807 | 2,808 | 15 | 276 | 59 | 217 |
| — | DIRT | 184 | 184 | 0 | 0 | 0 | 0 |
| 140 | Corporation Tax | 4,436 | 4,474 | 11 | 91 | 27 | 64 |
| 148 | Capital Gains Tax | 2,200 | 2,206 | 1 | 141 | 85 | 56 |
| 3 | Capital Acquisitions Tax | 249 | 249 | 0 | 3 | 0 | 3 |
| 8 | Abolished Taxes | 0 | 0 | 0 | 8 | 0 | 8 |
| — | Relevant Contracts Tax[2] | 0 | 0 | 0 | 37 | 11 | 26 |
| **1,217** | **Total Debt** | | | | **1,085** | **253** | **832** |
| **2.5%** | **Debt as a % of gross collection** [3] | | | | **2%** | **0.5%** | **1.5%** |

[2] RCT was incorporated into Revenue's main ITP system on a phased basis commencing in November 2002. The RCT "state of file" which provides an analysis of debt levels was completed in early 2006 and facilitates the inclusion of RCT debt for the first time.

[3] Gross collection in 2004 was €48,705m and in 2005 was €54,157m.

**Table 6 Aged Analysis of Debt at 31 March 2006**

| Tax | Total tax outstanding at 31 March 2006 | Amounts outstanding for 2005 | Amounts outstanding for 2004 | Due for 2001 to 2003 | Due for earlier periods (i.e. > 5 yrs old) |
|---|---|---|---|---|---|
| | €m | €m | €m | €m | €m |
| VAT | 227 | 30 | 49 | 117 | 31 |
| PAYE | 137 | 73 | 23 | 26 | 15 |
| PRSI | 165 | 97 | 26 | 29 | 13 |
| Income Tax | 276 | 4 | 73 | 66 | 133 |
| Corporation Tax | 91 | 19 | 8 | 27 | 37 |
| Capital Gains Tax | 141 | 6 | 24 | 18 | 93 |
| Capital Acquisitions Tax | 3 | 0 | 0 | 1 | 2 |
| Abolished Taxes | 8 | 0 | 0 | 0 | 8 |
| RCT | 37 | 12 | 9 | 12 | 4 |
| **Total** | **1,085** | **241** | **212** | **296** | **336** |

# 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. Revenue changed the categorisation of its audit activities in 2005 to reflect the fact that the intervention by Revenue depends on whether the risk is perceived to relate to one or more tax or duty heading or to specific issues or transactions. Assurance Checks are not audits but interventions that may involve tests, verification checks, desk examinations, visits to premises, searches, site visits and telephone contacts for supporting documentation.

The outcome of the 2005 programme of Revenue audits together with assurance activity is summarised in Table 7.

**Table 7 Revenue Audit and Assurance Activity**

| Category | 2005 | | 2004 | |
|---|---|---|---|---|
| | No. of audits completed | Yield €m | No. of audits completed | Yield €m |
| Comprehensive Audits | 5,077 | 323.3 | 4,058 | 382.3 |
| Multi Tax/Duty Audits | 1,220 | 52.3 | 848 | 18.4 |
| Single Tax/Duty Audits | 6,173 | 122.8 | 4,409 | 68.4 |
| Single Issue/Transaction Audits | 1,744 | 26.6 | 256 | 4.1 |
| Verification Audits[4] | 0 | 0 | 6,750 | 76.4 |
| **Total Audits[4]** | **14,214** | **525** | **16,321** | **549.6** |
| Assurance Checks[4] | 98,981 | 50.4 | n/a | n/a |
| **Total Interventions** | **113,195** | **575.4** | **n/a** | **n/a** |

(n/a indicates figures not available)

## Comprehensive Audits

To facilitate the recording of audit activity under the new audit categories, a new case management system – Audit Case Management – was introduced in July 2005. As a transitional measure spreadsheets were used to record audit activity under the new categories and, because of the administrative burden, Regions were not required to analyse settlements by settlement bands. Therefore, analysis by settlement bands was not available for 2005.

The yield of €323.5m from the 5,077 comprehensive audits completed includes interest charges of €124.6m and penalties of €52.7m. The highest settlements were €4.1m for Income Tax and €9.5m for Corporation Tax. Comprehensive audits were completed in 1,249 bogus non-resident account cases with settlements totalling €57.2m and in 1,594 offshore assets cases with settlements totalling €151.8m.

[4]Some activities classified as verification audits in 2004 e.g. VAT refund verification checks, are classified as assurance checks in 2005.

# Risk Analysis System

A risk analysis system (REAP) was piloted in four Revenue Districts in 2005 and will be implemented in all Districts in 2006. The system analyses the information available on taxpayers by running a set of queries or rules through a database of taxpayer information, scoring the results and ranking the cases according to those scores. The rules have been derived from the knowledge and experience of Revenue auditors and are refined to take account of new risks and data sources. Based on the system ranking District officers analyse and assess the risk in each case to select suitable cases and decide on the appropriate intervention.

# Random Audits – Taxpayer Compliance Testing Programme

Revenue introduced the Taxpayer Compliance Testing Programme in 2005 to replace the Random Audit Programme. The purpose of the programme is to measure and track compliance with tax legislation and to ensure that all taxpayers run the risk of being selected for audit. 411 cases were selected for audit under the 2005 programme. 53 of the selected cases were "dropped" as the taxpayer had ceased trading, had never traded or was recently deceased. Additional tax liabilities were established in 91 of the 298 cases that were finalised. Settlements totalling €1m were agreed in those 91 cases. The outcome of the finalised cases is summarised in Table 8. Analysis of the results of the 2005 programme will be performed when the outstanding 60 cases are finalised.

**Table 8 Taxpayer Compliance Testing Programme - Finalised Cases by Size of Additional Liability**

| Additional Liability | Number of Cases Finalised | % of Finalised Cases |
|---|---|---|
| Nil | 207 | 69% |
| < €2,000 | 27 | 9% |
| €2,001 to €5,000 | 24 | 8% |
| €5,001 to €10,000 | 13 | 4% |
| €10,001 to €20,000 | 11 | 4% |
| €20,001 to €50,000 | 14 | 5% |
| > €50,001 | 2 | 1% |
| **Total** | **298** | **100%** |

# 2.5 Prosecutions

Under Revenue's 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 2005, 91 cases of serious tax evasion were referred to the Division for consideration and 30 were accepted for investigation with a view to prosecution.

Twelve convictions were obtained in the ten cases decided in court in 2005. Summary details of the cases are set out in Table 9.

**Table 9 Convictions during 2005 for Serious Tax Evasion**

| Occupation/Activity | Fine | Custodial Sentence |
|---|---|---|
| Oil Distribution Company | €4,000 | — |
| and | | |
| Director of above Oil Company | €7,400 | 3 months prison sentence |
| Stainless Steel & Engineering Company | €15,000 | — |
| and | | |
| Director of above company | —- | 3 month prison sentence |
| Retired Farmer | €125,000 | 2 year prison sentence if fine not paid within 3 months |
| Sales Administrator | €10,800 | 3 month prison sentence suspended on condition of 120 hours community service |
| Contract Cleaning and Security | — | 6 month prison sentence suspended on condition of 240 hours community service to be completed within 12 months |
| Endodontist | €4,500 | — |
| Building Sub Contractor | €18,700 | 6 month suspended prison sentence on each of 4 counts to run concurrently |
| Disc Jockey and Promoter | €13,887 | — |
| Veterinary Surgeon | — | Pleaded guilty in 2005, awaiting sentence |
| Shoe Retailer | — | Pleaded guilty in 2005, awaiting sentence |

Of the 84 cases of serious tax evasion on hands in the Investigations and Prosecutions Division at the end of 2005, 36 remained under investigation at June 2006 and seven had been closed. The status of the other 41 cases was

- 5 are with the Revenue Solicitor's Office
- 12 have been submitted to the DPP
- The DPP has issued directions to prosecute in 9 cases
- Bench warrants have been issued in 1 case
- 14 cases are before the court.

In addition, there were 12 convictions for serious Customs and Excise evasion in 2005.

# 2.6 Special Investigations

Table 10 sets out the payments made to the end of June 2006 as a result of each of the Special Investigations being carried out by Revenue. A short summary of progress to date in the investigations follows.

**Table 10 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. 8,500 | €390m |
| NIB | 465 | €57m |
| Ansbacher | 289 | €62m |
| Pick Me Up Schemes | 71 | €0.8m |
| Mahon Tribunal | 27 | €30m |
| Moriarty Tribunal | 18 | €8m |
| Offshore Assets | 13,990 | €826m |
| Undisclosed Funds – Life Assurance Products | 5,150 | €398m |
| **Total** | | **€2,223.8m** |

## Underlying Tax on Bogus Non-Resident Accounts

A total of 3,675 taxpayers paid €227m under the Voluntary Disclose and Pay Scheme whereby underlying tax relating to funds deposited in bogus non-resident accounts was required to be paid by 15 November 2001 to avail of the incentives of a cap of 100% on interest and penalties and an undertaking not to prosecute or publish details of the settlement. Revenue selected 268 of these cases for liability review. 208 of these were accepted as being correct, additional payments of €5,816,408 were required in 54 cases and six cases are still being examined. Payments on account of €1,097,769 have been received in four of the six open cases. All cases were reviewed for eligibility and 17 cases were deemed to be ineligible. Ten of these have been settled with additional liabilities of €1,669,325. One of these cases was prosecuted and received a two year suspended sentence. The remaining seven cases are at various stages of investigation.

Revenue used their powers under Section 908 of the Taxes Consolidation Act, 1997 to obtain information from financial institutions to help identify bogus non-resident account holders who did not avail of the Voluntary Disclose and Pay Scheme. Eighteen orders under Section 908, seeking information on account holders from 26 financial institutions, were granted. At June 2006, payments of €390m had been received from bogus non-resident account holders over and above the proceeds of the voluntary scheme.

Revenue estimates that the likely future yield from the DIRT underlying tax investigation will be of the order of €20m and will arise over the next couple of years.

## Offshore Investments via National Irish Bank

Investigations have concluded in 430 of the 465 cases identified as having invested in an offshore investment scheme operated by National Irish Bank. Settlements totalling €51m have been made in 308 of these cases while the other 122 cases had no liability. Investigations are continuing in the remaining 35

cases and payments on account of €3.2m have been received from 12 of these. Over and above these amounts National Irish Bank has paid €3.1m in respect of Capital Gains Tax on compensation it paid to certain investors. Revenue estimates that a further €4m should be paid and that the investigation will be concluded within approximately 12 months.

# 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.

Ten High Court orders have been obtained against financial institutions and third parties requiring the production of books, records and documentation. Some 220,000 documents have been received under the terms of the High Court Orders. Also, documentation has been received on foot of the June 2004 High Court order which allowed for access to certain documentation relating to clients of Ansbacher named in the High Court Inspectors' Report and those persons found by the High Court Inspectors to have failed to co-operate with their enquiry.

A total of 210 cases have been settled to date, 83 of which had total liabilities of €50.77m. This includes a settlement of €7.5m with a Cayman Islands based bank. The other 127 cases settled had no liability and include 66 non-resident cases covered by the provisions of Double Taxation Agreements, as well as 18 cases covered by the 1993 Amnesty provisions. Payments on account of €11.16m have been received in 27 of the 79 on-going cases. As some of the cases are likely to proceed to the Courts, it is not possible for Revenue to predict either the potential yield or the time frame to completion.

# 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 the 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. 44 cases have been settled for a total of €552,344 including interest and penalties. Payments totalling €226,165 have been received in connection with ten other cases including Tribunal cases which are still to be finalised. It is proving difficult to conclude certain cases because of the age of the payments, which were made in the 1980s or early 1990s, and the lack of documentation and records gives rise to difficulty in confirming liability. It is not possible for Revenue to estimate with any degree of accuracy the final outcome and yield in connection with outstanding matters.

# Tribunals

Matters disclosed at the Moriarty and Mahon Tribunals, which suggest that tax evasion may have occurred, are being investigated as they come to notice. Eighteen cases are being investigated as a result of the Moriarty Tribunal and two cases have been settled for a total of €6.3m. Payments on account of €1.4m have also been received. Twenty-seven cases are being investigated as a result of the Mahon Tribunal and four of these have been settled for €26.5m; payments on account of €3.6m have also been received.

The Moriarty Tribunal is nearing completion and it is not expected that further cases will arise. Revenue does not know if any additional cases will arise from the Mahon Tribunal or when that Tribunal will conclude. In relation to the cases being investigated, a further yield of €5m over the next two years is expected.

# Offshore Assets

This investigation is concerned with those who have not paid tax due on funds held in offshore accounts and investments. The voluntary phase of the investigation required taxpayers to give Revenue notice of their intention to make a qualifying disclosure by 29 March 2004 and submit a statement of disclosure and any payment due by 10 June 2004. The benefits of meeting these deadlines were mitigation of penalties, settlement details would not be published and there would be no prosecution. Disclosures were received from 13,651 taxpayers and €650m was received both from this phase of the investigation and from two earlier investigations.

As a follow-up to the voluntary phase, nine High Court orders have been obtained requiring financial institutions to supply details of transactions by their customers relating to offshore operations. Revenue has been receiving information in relation to these Orders but it is not anticipated that all data will be received before the end of 2006. "Challenge letters" have issued in a number of cases and more will issue during 2006. Further information and court orders will be required to identify persons who could not be identified from the information originally submitted. A further €175.7m has been received since the voluntary scheme, arising from reviews of the voluntary submissions and payments from some 339 taxpayers who did not avail of the voluntary scheme. This follow-up work is likely to run for at least a further two years and the final yield from the investigation may approach €1 billion.

# Life Assurance Products

Investigations into the use of life assurance investment products to hide undisclosed income or gains began in 2004. The voluntary disclosure phase of the investigation set a deadline of 23 May 2005 for those who invested undisclosed funds greater than €20,000 in such products to give notice to Revenue of their intention to make a voluntary disclosure. Full disclosure and payment was then required to be made by 22 July 2005. The benefits to the taxpayer in availing of the voluntary scheme were that the settlement details would not be published, there would be no prosecution and penalties would be mitigated in accordance with the Code of Practice for Revenue Auditors. About 10,000 notices of intention to make disclosures were received and some 5,150 taxpayers made payments of €398m under the voluntary scheme.

The second phase of the investigation involves identifying those who did not avail of the voluntary scheme. Revenue used new powers provided in the Finance Act 2005 (section 140), which allows it to sample the information held by a life assurance company that relates to a class or classes of policies and policyholders, where there are circumstances which suggest that such policies have been used to invest untaxed funds. The information obtained can only be used to assist in making an application to the High Court for an order to have wider access to the information. Revenue has completed the sampling work in 14 assurance companies. The information gathered from that work and from the voluntary disclosures is being used to assist in applications to the High Court for orders directing assurance companies to furnish details on individual policyholders and policies to Revenue (11 orders were applied for and made in July 2006). Revenue expect this investigation to take a number of years to complete and the final yield may exceed €500m.

# 2.7 International Aspects of Revenue Operations

In an open economy and in an era of rapid and extensive movement of persons, goods, investments and services across national frontiers, the international aspects of Revenue's operations have extended far beyond the traditional customs area to become an important element of the administration of all taxes. While the customs area retains importance both in the prevention of criminal activities, and through a shared responsibility for the external frontier of the EU, Revenue also ensures that effective tax administration is maintained through the development of double taxation agreements, information exchange, the implementation and operation of relevant EU Directives, participation in EU Working Groups, and ensuring that Irish tax administration interests are reflected in the taxation policies of the EU, the OECD and the World Customs Organisation.

I examined some aspects of Revenue's operations that have a strong international element and, in particular, considered the extent to which Revenue is systematically and efficiently making full use of the provisions and arrangements in those areas in order to optimise the assessment and collection of taxes and duties. The areas reviewed were Double Taxation Agreements (DTAs), Mutual Assistance for Direct Taxes and for Recovery of Claims, and VAT Carousel Fraud.

## Double Taxation Agreements

Section 826 of the Taxes Consolidation Act 1997 contains the legislation under which Ireland's DTAs or tax treaties are negotiated and subsequently ratified by the Irish Government. Generally, the agreements cover income tax, corporation tax and capital gains tax. Ireland has presently DTAs in force with 44 countries[5]. New treaties with Argentina, Egypt, Kuwait, Malta, Morocco, Singapore, Tunisia, Turkey, Ukraine and Vietnam are under negotiation. Existing treaties with Cyprus, France, Italy and Korea are in the process of re-negotiation, and procedures to bring into force a new treaty with Chile and a protocol amending the existing treaty with Portugal were completed by Ireland in December 2005.

DTAs are predominately based on the OECD Model Tax Convention on Income and Capital and are drawn up to eliminate double taxation and to clarify situations where a taxpayer might find himself subject to taxation in more than one country. Generally, the agreements provide that the taxpayer will only be taxed in one country or, if both countries retain the right to tax, the taxpayer is entitled to a tax credit in the country of residence against tax paid in the other country. The agreements counter any harmful effects that double taxation would otherwise bring to the exchange of goods and services and the movement of capital. The agreements also provide for the exchange of information between the tax authorities to prevent tax avoidance or evasion.

Where a DTA does not exist with a particular country, there are unilateral provisions within the Irish Taxes Acts, which allow credit relief for tax paid in other jurisdictions in respect of certain types of income (e.g. dividends and interest). The Direct Taxes Interpretation and International Division (DTII) of Revenue is responsible for dealing with all enquiries in respect of DTA matters.

Although most of Ireland's DTAs are based on the OECD model, all of them contain non-standard provisions. Examples of non-standard provisions include

[5] Australia, Austria, Belgium, Bulgaria, Canada, China, Croatia, Cyprus, the Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, India, Israel, Italy, Japan, Republic of Korea, Latvia, Lithuania, Luxembourg, Malaysia, Mexico, the Netherlands, New Zealand, Norway, Pakistan, Poland, Portugal, Romania, Russia, Slovak Republic, Slovenia, South Africa, Spain, Sweden, Switzerland, the United Kingdom, the United States of America and Zambia

- Ireland – Australia: contains rules for taxing gains on assets specifically referred to in the agreement.
- Ireland – Estonia: the residence of a business entity is to be decided by mutual agreement between the countries. The terms of the agreement may not apply to such and entity if agreement cannot be reached.
- Ireland – Switzerland: a partnership organised under the laws of Switzerland is deemed to be resident in Switzerland. A partnership organised under the laws of Ireland is not provided for.
- Ireland – Spain: the country in which a company is resident has the right to tax gains on the disposal of its shares by a resident of the other country provided the shareholder had at least a 25% interest in the company in the year preceding disposal.

The Accounting Officer informed me that in the context of globalisation of business, it is Government policy to continue to expand Ireland's network of DTAs. The network has already been substantially expanded - from 23 DTAs in 1994 to the 44 that are now in force. Ireland has signed and completed the ratification process in respect of a 45th country and DTAs are being negotiated with ten other countries. In addition, first round negotiations will take place with a further three countries this autumn. Revenue has also recently re-negotiated its treaty with Portugal and is currently re-negotiating four other existing DTAs. He pointed out that it should, however, be understood that DTAs are a bilateral process.

In relation to regular review of DTAs, he stated that existing DTAs are kept under general review. Where identified problems arise, consideration is given to requesting negotiations with the other country to amend the treaty. Where weaknesses are identified in one treaty, others which contain similar provisions are reviewed also. He pointed out that this is a rolling process. Portugal is an example of a case where Ireland proposed amending the treaty to avoid the non-taxation of capital gains. Another is the UK treaty which was amended by a protocol in 1998 to reflect various domestic law changes.

The Accounting Officer pointed out that each country, including Ireland, adapts the OECD model to its own domestic laws and policies and that the provisions that are ultimately included come about through a process of negotiation. All of Ireland's DTAs depart to varying degrees from the OECD model but it should be borne in mind that the OECD model is only that – a model – and that there is also a UN model tax convention. All of the examples of non-standard provisions illustrate the point that departures from the models reflect the domestic tax laws and policies of the countries concerned. Ireland proposes several departures from the OECD model in tax treaty negotiations. For example, it is Revenue policy to seek an exemption from source taxation of aircraft leasing income because of the large aircraft leasing industry in Ireland and a zero rate of withholding tax on interest payments, because of the open nature of Ireland's economy and the location of international banking and treasury businesses in Ireland. He stated that the agreement with Switzerland contains the provision regarding partnerships because Switzerland, unlike Ireland, treats a partnership as a separate entity from the partners. The definition of partnership was, therefore, included to protect Switzerland but does not in any way undermine the Irish tax position. The language in the capital gains article of the Spanish agreement reflects the UN model tax convention which is the model the Spanish use.

## Tax Information Exchange Agreements

In 2000 the OECD called on countries with tax haven characteristics to cooperate with OECD work in combating tax evasion by exchanging information with tax authorities in OECD countries based on a model Tax Information Exchange Agreement (TIEA). Revenue is currently negotiating TIEAs with the Isle of Man, Jersey, Guernsey, the Cayman Islands, and the British Virgin Islands. If these negotiations are successful the agreements will provide for the exchange of bank information on request, as well as information on the beneficial ownership of companies, partnerships and trusts. The Accounting Officer informed me that consideration would be given to agreeing TIEAs with other jurisdictions in the light of experience with the current negotiations.

# Mutual Assistance – Direct Taxes

DTII is responsible for the exchange of information between Revenue Authorities under the provisions of Double Taxation Agreements and also under the EU Directive 77/799/EEC[6], as amended, which provides for mutual assistance (exchange of information) in relation to direct taxation. Exchange of information requests to Revenue relate to issues such as

- Is the individual/company resident in Ireland for tax purposes?
- What taxes are they registered for?
- What tax have they paid?
- Do they own any property in Ireland?
- How many employees does a company have?
- Who are the directors and shareholders of a company?
- Contract verification
- Bank information.

Details of requests are logged on to a database and DTII search Revenue's systems to obtain the required information. If the requested information is not readily available, the details are requested by DTII from the liaison officer in place in each District and the liaison officer provides the requested information to DTII for forwarding to the requesting country. Requests issued by Ireland are forwarded by various sections of Revenue through the liaison officers to DTII who forward the request to the other country. Details of the extent of the exchange of information in the years 2003 to 2005 are set out in Table 11.

**Table 11 Direct Taxes Requests for Information 2003 – 2005**

| Year | Requests Received | | | Requests Issued | | |
|---|---|---|---|---|---|---|
| | Received | Completed in Year[7] | Cases Open[7] | Issued | Completed in Year[7] | Cases Open[7] |
| 2003 | 155 | 159 | 143 | 21 | 8 | 50 |
| 2004 | 145 | 176 | 112 | 24 | 0 | 74 |
| 2005 | 117 | 114 | 115 | 13 | 1 | 86 |
| **Total** | **417** | **449** | | **58** | **9** | |

Information is also exchanged automatically and spontaneously between countries. Spontaneous exchanges occur where the tax authorities of one country believe that they have information that would be of assistance to another country. Certain routine information is exchanged automatically between countries e.g. information relating to taxpayers with addresses in another country who receive a refund of Irish withholding tax (e.g. professional services withholding tax, relevant contracts tax and dividend

[6] EU Directive 77/799/EEC and subsequent amendments were transposed into Irish law by various Statutory Instruments. Statutory Instrument 367 of 2005 gave effect to the latest two amending directives and also consolidated and gave effect, in one set of regulations, to Directive 77/799/EEC, as amended.

[7] Cases in these columns include cases received/issued in earlier years.

withholding tax). The level of automatic and spontaneous exchanges of information in relation to Direct Taxes in the years 2003 to 2005 are set out in Table 12.

**Table 12 Number of Automatic and Spontaneous Exchanges 2003 - 2005**

| Year | Automatic | | Spontaneous | |
|---|---|---|---|---|
| | Received | Issued | Received | Issued |
| 2003 | 21 | 10 | 38 | 1 |
| 2004 | 27 | 11 | 51 | 3 |
| 2005 | 20 | 13 | 44 | 2 |
| **Total** | **68** | **34** | **133** | **6** |

I asked the Accounting Officer whether he considered that the volume of automatic and spontaneous exchanges of information received by Revenue was consistent with the level of economic activity by Irish residents abroad as indicated by Revenue's recent major investigations, its examination of property abroad and general economic reporting. In response, the Accounting Officer stated that the level and extent of spontaneous reports received from treaty partners is dependent on the knowledge and skills of revenue officials in these jurisdictions and the extent to which those officials can readily identify Irish residents engaged in business transactions within these jurisdictions. In general, business transactions are conducted through corporate vehicles and it may not be apparent from the more complex transactions, where there may be a number of corporate vehicles, that the ultimate ownership lies with Irish residents. The recent Revenue investigation in relation to offshore accounts focussed on subsidiaries and affiliates of Irish financial institutions which had operations outside the State. In the main, these subsidiaries and affiliates had operations in what were traditional tax havens and exchanges of information would not have occurred with these jurisdictions. Revenue has recently initiated a series of meetings with a number of these jurisdictions with a view to concluding tax information exchange agreements. Overall, while the level of spontaneous reports received may not appear significant, the reports received are of a high quality and are considered a useful tool in ensuring compliance with the tax code. Revenue's experience, which is also the experience of other OECD members, in receiving automatic exchanges of information is that the accuracy and usefulness of the information received varies from country to country. Often, insufficient detail in the information provided prevents Revenue from using the information properly. The types of information held by revenue authorities in OECD countries varies and therefore, some information which would be of interest to Revenue may not be held by those countries. Other countries do not engage in automatic exchanges of information yet. Efforts are being made at OECD level to improve the exchange of information system. In May 2006 the OECD released a manual to provide practical assistance to officials dealing with exchange of information for tax purposes and to help member countries in designing or revising national manuals. Also, a sub-group of the OECD Working Party on Tax Avoidance and Evasion was set up to improve the technical and operational aspects of exchange of information for direct taxes. Two current topics being addressed are

- Increasing the efficiency of exchange of information processes and to ensure exchange of information can be used more effectively in a compliance context
- Monitoring the OECD standards for automatic exchange and identifying new types of information to be exchanged automatically.

He stated that Revenue is confident that the recommendations from the aforementioned work will enhance the effectiveness of the exchange of information system among OECD members.

The Accounting Officer informed me that Revenue in the past did not automatically exchange bank information with treaty partners and therefore, in relation to the bogus non-resident accounts, would not have provided such details to other jurisdictions. However, following the implementation of the EU Savings Directive, Revenue is now providing bank information to Ireland's EU treaty partners relating to interest arising in the State on or after 1 July 2005.

# Mutual Assistance – Recovery of Claims

EU Directive 76/308/EEC[8], as amended, provides for the exchange of information in respect of, and the recovery of, claims made by other member states in respect of debts due to that State for VAT, income and capital taxes, import and export duties, etc. Directive 2002/94/EEC sets out the detailed rules for implementing the provisions of Directive 76/308/EEC[8].

These mutual assistance arrangements are designed to ensure

- cross-border provision of any information that would be useful in the recovery of claims
- instruments and decisions, including those of a judicial nature, that relate to a claim and/or its recovery are notified to addressees in other member states
- member states that have exhausted the means of recovery of uncontested claims in their own state can recover the claim in other member states as appropriate.

## Requests for Information Relating to Claim Recovery

Under Article 4 of the EU Directive, a member state may make a request for information relating to the recovery of its claim in another member state. When Revenue receives a request they are obliged by the Directive to provide any information, which would be useful to the applicant authority in the recovery of its claim. However, Revenue is not obliged to supply information

- which it would not be able to obtain for the purpose of recovering similar debts, or
- which would disclose any commercial, industrial or professional secrets, or
- the disclosure of which would be liable to prejudice the security of or be contrary to the public policy of the state.

Requests for information are received in a central liaison office known as VIMA[9]. The requesting state provides the name and address of the person to whom the information to be provided relates and the nature and amount of the claim in respect of which the request is made. The details are recorded on a database and an acknowledgement is forwarded to the other member state. The details of the request are forwarded to the relevant area of Revenue to obtain the information requested. When the requested information has been collected, the details are supplied to VIMA who forward the data to the requesting state's central liaison office.

Requests for information to another Member State generally arise from a Revenue audit. The request is sent through VIMA to the other member state's central liaison office and all details are recorded on a database. When the reply is received the details are forwarded by VIMA to the relevant Revenue office.

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[8] Statutory Instrument 462 of 2002 (as amended by Statutory Instrument 344 of 2003) consolidates and gives effect to Directive 76/308/EEC as amended, as well as the detailed rules for implementing that Directive contained in Directive 2002/94/EEC.
[9] VIMA deals with the VAT Information Exchange System, INTRASTAT (gathering statistical data from traders), and Mutual Assistance.

The number of requests for information received and issued in relation to recovery of claims in each of the last three years is set out in Table 13.

**Table 13 Requests for Information for Recovery 2003 - 2005**

| Year | Received | Issued |
|---|---|---|
| 2003 | 2 | 0 |
| 2004 | 16 | 3 |
| 2005 | 14 | 8 |
| **Total** | **32** | **11** |

I sought the observations of the Accounting Officer on the low level of requests for information for recovery issued by Revenue (as reflected in Table 13) and requests for information in relation to direct taxes (Table 11). In reply, the Accounting Officer stated that low awareness and the length of time involved are factors that may influence the number of requests. In order to increase awareness, Revenue issued exchange of information guidelines on its internal website in October 2004 and followed this up with a series of talks to staff in the Dublin area in late 2004 and early 2005. A number of liaison officers have also been appointed throughout the organisation to promote and facilitate the use of the exchange of information system. It is hoped that this will, over time, lead to greater use of exchange of information under treaties. Although the numbers have not increased significantly as yet, a marked improvement in the quality of the requests being drawn up at local level has been noted. Unnecessary and incomplete requests for information have been reduced and the requests are now more focused and targeted. The Accounting Officer recognises that more work needs to be done to promote the exchange of information and Revenue is examining ways to further heighten awareness internally. A high priority is being given by the OECD to assisting countries in obtaining timely and high quality information from treaty partners. One of the initiatives the OECD has taken is to set up a secure website for competent authority staff dealing with exchange of information matters containing, for example, country-specific information, current list of competent authorities, useful public website links in each country and a guide to sources of information in each country. The use of this website will help to reduce unnecessary or incomplete requests by making as much information as possible available in each country. Other areas being given priority include (i) the implementation of streamlined procedures and, where appropriate, standardising procedures and forms and (ii) the greater use of information technology. Ireland participates at OECD level on all of these issues and has contributed to the secure website.

# Requests for Claim Recovery

Under Article 6 of the EU Directive, at the request of a member state, the requested state shall recover claims in accordance with the laws, regulations or administrative provisions applying to the recovery of similar claims arising in that member state.

The Collector General is the competent authority in Ireland for issuing requests for recovery to other member states, and to collect debts on behalf of other member states. Prior to May 2006, incoming requests were received via VIMA but the Collector General now receives the cases directly from the other member state.

## Requests for Recovery Received by Revenue

Requests for recovery received are recorded on a database. A demand in writing is then issued to the taxpayer and the sum outstanding becomes due and payable seven days from the date of the issue of the demand. If the written demand is unsuccessful, the Collector General forwards the case to the Revenue

sheriff for collection. If the debt remains uncollected, the Collector General can sue for the debt in the District or Circuit courts. Details of requests received for recovery of claims and of cases recovered in each of the last three years are set out in Table 14.

The apparent low success rate in recovery of claims is considered by the Collector General to be due to

- increasing mobility of taxpayers within the EU states
- lack of communication between the taxpayer and the requesting authority regarding his/her movements
- lack of communication between the local tax office and the head office in the applicant country leading to incorrect claims for recovery.

**Table 14 Requests Received for Recovery of Claims 2003 - 2005**

| Year | Received | | Recovered | | % of Value Recovered |
|---|---|---|---|---|---|
| | Number | Value | Number | Value | |
| 2003 | 118 | €2,695,224 | 25 | €638,391 | 24% |
| 2004 | 288 | €11,945,991 | 36 | €1,428,034 | 12% |
| 2005 | 483 | €28,659,125 | 89 | €615,000 | 2% |
| **Total** | **889** | **€43,300,340** | **150** | **€2,681,425** | **6%** |

Note: 182 cases were closed in the year 2005 at the request of the requesting authority following the intervention of the Collector-General. These cases consisted of uncollectible tax of €3,484,868.

In a sample of 16 cases examined, 8 cases had a time lag of at least one month between the Collector General receiving the request and the issuing of the demand letter to the taxpayer. A further sample of 15 cases, which were forwarded to the Revenue Sheriff in 2005, were examined. In five of these, no response had been received from the sheriff at the beginning of April 2006. In most other cases, the Collector General's office had to contact the Revenue Sheriff for a reply. Delays in waiting for the translation of foreign documents were also noted. Information on the number of open cases, number with sheriff, etc. is not readily available from the database and at present is extracted manually. Some requests received dating from 1999 remain open.

As I was concerned that the low recovery rate and the delays noted might indicate that Revenue was not fully meeting its obligations, I sought the views of the Accounting Officer. The Accounting Officer informed me that he is satisfied that Revenue is meeting its obligations in relation to requests to recover tax on behalf of other countries in a satisfactory manner. He noted that the two years (2003 and 2004) for which EU comparisons are available show that Revenue recovered 24% and 12%, respectively, of tax requested compared to an EU average of about 1% and 2%. Even with the fall in collection performance for 2005, Revenue will still probably be around the EU average for that year. The recovery rate in cases where Revenue is requested to recover tax on behalf of other countries needs to be viewed in the context of the nature of the claims involved

- Cases have first of all been subject to all appropriate/available collection activity by the requesting State. The cases therefore have already resisted all attempts at collection.
- Information in relation to addresses is not accurate in many cases.

- Requests for recovery of estimated amounts are received and these often end up with no liability when returns are submitted.
- Many of the taxpayers who are the subject of these claims tend to move regularly between States and while they may have resided in Ireland at some point, they may have moved elsewhere by the time the claim for recovery is received.

In relation to delays in cases where recovery is requested, the Accounting Officer said that the Collector General's Division, on receipt of claims carry out checks to ascertain as much information on the taxpayer as possible in order to make the best decision on the course of action to take in individual cases. In three of the eight cases Revenue had to revert to the applicant State for clarification prior to issuing the demand for payment. In general, demands are issued in the vast majority of cases within a month of receipt of the request. It may also have been the case that internal Revenue arrangements as regards claims recovery could have added to the timespan for processing of claims recovery requests. The fact that all claims and correspondence concerning claims are now transacted directly between the applicant authority and the Collector General's Division will help to minimise delays in processing cases.

## Requests for Recovery Issued by Revenue

A report of non-resident cases with tax outstanding of greater than €20,000 is prepared quarterly[10]. The April 2006 report contained 282 cases and total tax outstanding of €25m. The Debt Management Unit ensures that all avenues open to them have been exhausted in the attempt to collect the debt and appropriate cases are then forwarded via VIMA to the tax authority of the appropriate member state for enforcement.

Details of request for recovery sent to other member states in the years 2003 to 2005 are set out in Table 15. Issues noted from an examination of procedures and cases were

- A relatively small number of requests are issued to other member states
- Many of the cases forwarded by the Collector General's to other member states are based on estimated liabilities. In a sample of 10 cases from 2004, the total sum requested was €1,148,648 and €991,329 of this liability was based on estimated figures. As at April 2006, €100,345 of this estimated liability was collected, the estimated amounts have been reduced by €794,467, and €96,517 remains outstanding.
- One of the cases reviewed from the quarterly report of outstanding taxes was in respect of an Australian resident who owed €247,208. This amount was written off. Revenue is unable to use the authorities in non-EU countries to collect outstanding amounts on their behalf. While provision was made in this regard in the OECD model tax convention[11], Revenue has obtained legal advice to the effect that the inclusion of the provision as set out in the model convention would not be constitutional in Ireland.

[10] Cases with certain "stops" (e.g. liquidation, receivership, under appeal, under investigation, audit) and cases with current balances outstanding are excluded from the report.
[11] Article 27 of the model convention.

**Table 15 Requests Issued for Recovery of Claims 2003 - 2005**

| Year | Issued | | Recovered | | % of Value Recovered |
|---|---|---|---|---|---|
| | Number | Value | Number | Value | |
| 2003 | 41 | €9,096,178 | 6 | €226,019 | 2% |
| 2004 | 20 | €2,787,657 | 17 | €437,210 | 16% |
| 2005 | 48 | €6,110,315 | 23 | €761,726 | 12% |
| **Total** | **109** | **€17,994,150** | **46** | **€1,424,955** | **8%** |

An EU Commission Report in 2006[12] concluded that although there has been a significant increase in the use of mutual assistance for recovery of claims, a substantial gap remained between the amounts for which assistance is requested and the amount actually recovered. Aggregate figures for the EU show that percentage of recovery requests satisfied were 1.13% in 2003 and 1.82% in 2004.

The Accounting Officer informed me that the 282 non-resident cases on the April 2006 quarterly report included all foreign-based registrations and not just those in the EU. Subsequent examination of each case in the context of caseworking will determine the suitability of the case for any particular type of recovery action. For example, examination will show the availability of RCT offsets, subsequent payment of the debt, case having ceased trading prior to the period covered by an estimate of liability by Revenue. Examination of a sample of 50 of the larger liability cases in the listing of 282 indicated that less than 10 of these have the potential for referral for collection under mutual assistance. Cases are selected for caseworking intervention each month by reference to the returns due for the previous month or by reference to the quantum of the tax debt. Priority attention is given to the cases with the largest debt or potential debt. Mutual assistance requests must be preceded by the deployment by Revenue of available collection avenues. In 2005, 349 non-resident cases were referred for solicitor enforcement and in 2004, 372 cases were so referred. In the final analysis, a decision on whether to make a mutual assistance request is made on a case by case basis and will depend on the size of the debt, an assessment of the reliability of available information about address etc. in the foreign jurisdiction and an assessment of the likelihood of success.

In relation to the high level of estimated liabilities included in the sample of cases examined, the Accounting Officer stated that the tax collection system is structured around ensuring, to the greatest extent possible, that where a taxpayer fails to file a return, Revenue makes an estimate of the liability using the best information at its disposal, and undertakes appropriate collection measures to effect recovery. Of their nature, therefore, non-compliant cases will in many instances display an element of estimated liability. Frequently cases respond to the issue of estimates by filing returns and making payment. He said that it is worth noting that of the 10 sample cases examined, one case accounted for 45% of the total amount referred for recovery and 52% of the total estimated amount referred thereby skewing the sample to a very significant extent. It was eventually established that this case never traded and the case was cancelled with estimates discharged on receipt of "Nil" returns. There is much greater difficulty with foreign cases in establishing whether the entity is currently trading, as no local knowledge or sheriff information is available (a feature in resident cases).

[12] Report for the Commission to the Council and the European Parliament on the use of the provisions on mutual assistance for the recovery of claims relating to certain levies, duties, taxes and other measures, 8/2/2006.

The Accounting Officer informed me that Revenue was aware of the likelihood of a constitutional difficulty with the "assistance in collection of taxes" article of the OECD model. The 2002 update to the OECD model added this new optional article, and prior to finalisation of the model, Revenue sought legal advice from the Attorney General. The Attorney General raised concerns about the removal of the jurisdiction of the Irish courts in relation to examining the substance of the foreign tax claim. A footnote to the article is included in the model, partly in response to comments Revenue made, to the effect that in some countries, national law, policy or administrative considerations may not allow or justify the type of assistance envisaged under the article or may require that this type of assistance be restricted, e.g. to countries that have similar tax systems or tax administrations or as to the taxes covered, and for that reason, the article should only be included where each State can agree to provide assistance in the collection of taxes levied by the other State. Given the constitutional difficulty, Revenue has not sought to include the article in its treaties. Other OECD countries also do not include the new Article for similar reasons.

# Missing Trader Intra-Community (Carousel) Fraud

Revenue's Carousel Fraud Team (CFT) is designated as a liaison department in accordance with Article 3 of European Council Regulation (EC) 1798/2003 for the purpose of the direct exchange of information in relation to suspected VAT fraud, particularly Missing Trader Intra-Community or Carousel fraud. Carousel fraud involves a trader carrying out business in high-value low-bulk goods (e.g. computer chips and mobile phones) with transactions in the business taking place over a short period. The transactions are often quite complex with the goods passing through a number of businesses within the EU in a circular fashion, and maybe even returning to the original trader, thereby giving rise to the term "carousel".

The CFT undertakes visits to selected businesses to discover potential missing traders and conduit traders, to investigate current trading for exchange of information purposes, to carry out pre-registration checks on high-risk cases and to be proactive in deterring evasion and fraud. The CFT uses VIMA to verify the validity of VAT numbers. The activities of CFT in 2005 included

- Research into 211 cases, identifying cases suitable for field visits or referral to the appropriate region
- Conducting 93 field visits in known risk sectors for the purpose of gathering intelligence and monitoring the activities of known conduit traders
- The issue of 177 items of spontaneous information to other member States under Mutual Assistance and receiving 95 requests for assistance. The exchange of information in the years 2003 to 2005 is set out in Table 16.

The UK Revenue and Customs compiles estimates of the VAT lost from fraud, avoidance and other non-compliance i.e. the VAT gap. The estimated level of attempted carousel fraud in 2004-05 was put at between stg£1.12 billion and stg£1.9 billion out of a total estimated VAT loss of stg£11.3 billion. Equivalent figures for Germany were €2.1 billion lost to carousel fraud out of a total loss of €17 billion. A similar exercise is not carried out in Ireland. While carrying out such estimates is inherently difficult and a relatively untested area, an assessment of possible losses allows the risks to be assessed, and strategies developed to tackle those risks.

Companies can register in Ireland solely as conduit traders that acquire goods from other member states at the zero VAT rate and supplying them on, also VAT-free, to an intending missing trader in another member state. The action open to Revenue in these cases is to cancel the VAT registration. There is an ongoing risk that the trader will set up under a different name and obtain a new VAT registration number.

The largest case of outstanding taxes written off by Revenue in 2004 (€5.58m) was in respect of a liability arising as a result of a carousel fraud. Revenue received information under mutual assistance arrangements in relation to the supply of computer components to an Irish company. Following an initial Revenue meeting with the company, the company went into liquidation. A Section 23 estimate was raised but the debt was subsequently written off. The Criminal Assets Bureau (CAB) also carries out investigations in relation to carousel fraud cases. A CAB settlement of €3m in respect of a liability arising from a carousel fraud was noted in media reports in 2006.

**Table 16 Carousel Fraud Team - Exchanges of Information 2003 - 2005**

| Year | Requests Received | | Requests Issued | | Spontaneous Exchanges Issued |
|---|---|---|---|---|---|
| | Number | Cases Open | Number | Cases Open | |
| 2003 | 170 | 0 | 10 | 0 | 1,295 |
| 2004 | 150 | 2 | 19 | 7 | 881 |
| 2005 | 95 | 17 | 59 | 30 | 177 |
| **Total** | **415** | **19** | **88** | **37** | **2,353** |

In response to my enquiries as to whether he felt that an estimate of VAT losses would assist Revenue in combating fraud including carousel fraud, the Accounting Officer stated that VAT is the single largest yielding tax and the measures taken by Revenue to safeguard this yield reflect its importance to the Exchequer. The focus is on preventing VAT losses in the first place and responding strongly where prevention does not work. The measures employed by Revenue include audit, sectoral projects, regional special compliance units and a specialist VAT anti-avoidance unit, as well the Carousel Fraud Team. He has no doubt that the targeted deployment of resources in support of these measures represents their most efficient and effective use.

While it may be the case that an accurate estimate of VAT losses could be informative, it is also his view that there would be little point in producing an estimate, that would at best be unreliable and at worst misleading, just for the sake of having one. He concurs with the view that this is a relatively untested area and an inherently difficult one for making estimates.

The Accounting Officer informed me that the issue of carousel fraud was viewed seriously by Revenue and this was evidenced by the existence of the Carousel Fraud Team. He informed me that between 2003 and 2005, 21 conduit traders' VAT numbers were cancelled by Revenue. In relation to taking action against those involved in the case of carousel fraud where €5.8m was written off, he said that the company principals, both foreign nationals, were not resident in the State. One of the directors was known to have an address in Liberia, the other director was believed to be in Antwerp but their exact whereabouts were unknown. The question of pursuing the principals was considered and the decision, based on all of the known facts and the perceived costs of doing so, was that a recovery was unlikely to be effected. Revenue could, and would, recommence activity in this case should circumstances change to an extent that successful prosecution/collection of the debt becomes a possibility. He said that while it is somewhat reassuring that the write off case came to light as far back as 2000 and in the intervening years no further VAT losses have been identified, Revenue has no intention of lessening its focus on carousel fraud. Revenue's success in this area is likely to be due to a number of factors, including the pro-active nature of the Carousel Fraud Team's activities and improved and enhanced exchange of information. Active participation in the Missing Trader Intra-Community international networks, including European Carousel Network, keeps Revenue abreast of current developments and threats in this sphere. He understands that the reported €3m CAB settlement does not involve the recovery of VAT defrauded in the State.

# 2.8 VAT and e-Commerce

## VAT

VAT is an indirect tax on consumer spending. Traders registered for VAT collect the tax on behalf of the Revenue Commissioners on the supply of goods and services to their customers. Each registered trader in the chain of supply charges VAT on their sales and is entitled to deduct from this the amount of VAT charged to them on their purchases. Therefore, the tax is charged on the value added at each stage of the production and distribution cycle. The final consumer effectively pays the VAT as part of the purchase price. Traders are required to register with Revenue where their annual turnover exceeds €27,500 in the case of services and €55,000 in the case of goods. The legislation governing VAT is contained in the Value Added Tax Act, 1972, as amended. In 2005, the net amount of VAT collected by Revenue was over €12 billion.

## e-Commerce

Electronic commerce or 'e-commerce' is generally understood to mean the buying and selling of goods and services over the internet. Goods and services may be supplied business-to-business or between a business and a consumer. Usually, payment is also made on-line, mainly by credit or debit card. The types of transaction involved in e-commerce are

- Ordering of physical goods for delivery by traditional means
- Ordering of services (e.g. airline flights) where the supplier provides the service in the traditional form
- Ordering, and delivery of virtual or digitised goods and services over the internet (e.g. software, music, video).

### OECD/EU Principles and Guidelines

The OECD Ministerial Conference in Ottawa in 1998 agreed that the principles applying to the taxation of traditional trading should also apply to e-commerce. In July 1998, the EU endorsed a number of guidelines drawn up by the EU Commission as a means of ensuring that the EU's VAT system would continue to function in the world of e-commerce. These guidelines are

- No new taxes will be levied on e-commerce but existing taxes, particularly VAT, should be adapted
- The on-line supply of digitised products will be treated as the supply of services
- Services consumed in the EU should be taxed in the EU, regardless of their origin or means of supply. Services supplied by EU traders for consumption outside the EU are not to be subject to EU VAT, but VAT on related inputs would be deductible
- The VAT system must be enforceable
- Electronic invoicing should be allowed within the EU, subject to agreed rules
- Electronic VAT declarations and payment should be possible.

### Revenue Working Group on e-Commerce

In June 1999, an extensive report on Electronic Commerce and the Irish Tax System was prepared by an Electronic Commerce Working Group in Revenue. The report, which was published, identified the tax issues arising from the increased use of e-commerce and considered Revenue's likely responses. The report addressed the impact of e-commerce on all taxes and duties and considered how the internet might

be used to improve tax administration. The report stated that VAT was the one tax where action would be required to protect the tax yield, and that e-commerce issues had an immediacy in the area of VAT as compared with other taxes.

The report also

- outlined the fundamental issues for the taxation of e-commerce as
  - the identification of a transaction
  - the identification of the parties to a transaction (especially the taxpayer)
  - verification of the details of a transaction
  - for VAT, the identification of the correct rules, rates, calculation and remittance to the correct taxing authority
  - the generation of an audit trail
- indicated that, because of the technologies and the global nature of e-commerce, it may be necessary to adapt the procedures and techniques needed to effectively collect and administer these taxes
- considered that Revenue would need to constantly monitor developments in the service provision sector so as to identify new businesses and other internet value-added services.

The on-line supply of digitised goods and services (e-services[13]) to private customers was identified as presenting the greatest challenge. The 'place of supply' determined where VAT was chargeable and the general rule for services at that time was that tax was due in the place where the supplier was established (see Table 17) which dated from an era when services were generally not traded across borders. No VAT was chargeable by 3rd country (i.e. non-EU) businesses supplying e-services to EU consumers[14].

**Table 17 Supply of e-Services - Business to Private Consumers (pre July 2003)**

| Supplier Established in | Customer Resident in | Place of Taxation |
|---|---|---|
| Ireland | Ireland | Ireland |
| Ireland | Other EU State | Ireland |
| Ireland | 3rd Country | Zero Rated |
| Other EU State | Ireland | Other EU State |
| 3rd Country | Ireland | No VAT |

# Objectives and Scope of Audit

There has been a continuing growth in the level of e-commerce both within the country and across EU and international borders. The proper taxation of trade in that area presents particular difficulties to Revenue authorities generally due to aspects of e-commerce such as the absence of a physical business presence or even of the necessity for physical transfer of goods. The objectives of the audit were to

[13] EC Directive 2002/38 provides an illustrative list of e services – website supply; web hosting; distance maintenance of programmes and equipment; supply and updating of software; supply of images, text and information; making databases available; supply of music, films and games; political, cultural, artistic, sporting, scientific and entertainment broadcasts and events; supply of distance teaching.

[14] The 'place of supply' for VAT-registered businesses purchasing e-services from outside the EU was deemed to be the EU country where the business purchaser was located and the VAT implications of such transactions were dealt with in the purchaser's VAT return.

examine Revenue's approach to addressing these issues and ensuring an adequate level of tax compliance in that segment of economic activity. Particular questions raised included

- the extent of e-commerce in Ireland including the volume of e-commerce trade, number of participating businesses, VAT proceeds from e-commerce transactions, whether there has been any overall impact on the tax base
- how Revenue activity has matched up with the challenges and requirements set out in the 1999 e-commerce Working Group Report
- the impact of EU initiatives
- whether current compliance procedures were considered adequate including
    - the extent of Revenue audits in this area
    - evidence of any increase in postal importations related to e-commerce activity.

The audit comprised a review of reports and papers, informal consultation with Revenue officials, and formal correspondence with the Accounting Officer. A transaction-based review of VAT collected that relates to e-commerce is not possible as VAT returns show a business's total VAT without differentiation between traditional trading and e-commerce.

The responses and comments of the Accounting Officer relating to particular points raised in this chapter have been added to the relevant sections of the chapter. His overall summary response on the Revenue approach to VAT and e-commerce, and on the risk that e-business poses to VAT revenues, has been included at the end of the chapter.

# Extent of e-Commerce in Ireland

There are no exact figures for the level of e-commerce trading in Ireland. The Central Statistics Office's (CSO) Information Society and Telecommunications Report 2005 contains material on how information and communications technologies are being used in Ireland, in the home and in business. The report uses data from the CSO's Census of Industrial Population, Annual Services Inquiry and Quarterly National Household Survey. The results of the surveys show

- In 2005, sales using e-commerce accounted for 27% of total manufacturing turnover. In the services sector, sales via e-commerce accounted for 16% of turnover. By applying these details to the value of turnover in the manufacturing sector (€108 billion) and in the services sector (€103 billion), this would indicate e-commerce sales of the order of €46 billion.
- Over half of businesses have made some purchases using e-commerce. The percentage of total purchases made in this way has increased from 6% in 2004 to 10% in 2005. This remains small relative to the percentage of sales by e-commerce.
- In the 12 months to June 2005, over 587,000 people had ordered goods or services over the internet for private use. The most common internet purchases by households are travel and holiday accommodation, films and music and tickets for events.
- Irish enterprises are more likely to sell online than their EU counterparts.

In its budget submission 2006, ICT Ireland[15] noted that the European spend on business-to-consumer electronic transactions would grow to €200 billion in 2006 and that Ireland would account for €400m of that.

In response to audit questions on Revenue's estimate of the volume of e-commerce trade, the impact on the tax base, expected VAT proceeds, and the number of unregistered e-commerce traders identified, the Accounting Officer pointed out that as there is no distinction for VAT purposes between e-commerce and other commerce, estimates of the type mentioned in the question are not required to be made. Based on the ICT estimate the VAT liability at final consumer level would be significantly below €80m for 2006. At a macro level the continued strength of the VAT yield year on year gives no reason to suspect any negative effect on the tax base.

He stated that while Revenue does not differentiate between businesses with or without e-commerce trading activities, Revenue's Special Compliance Units continue to monitor actively all aspects of hidden economy activity and register cases for taxes as appropriate. The units focus on identifying businesses not fully registered with Revenue, and have an intelligence gathering function involving a range of initiatives, e.g. surveillance, door-to-door enquiries, third-party information matching, newspapers, internet information and external databases.

# Supply of e-Services from External Suppliers to EU Consumers

The VAT rule for supplies by non-EU businesses to EU consumers gave non-EU suppliers a competitive advantage over their EU counterparts. In addition, as suppliers of e-services do not need to be located near their customers, there was an increasing risk that the supply of these services from outside the EU would increase. To counteract this, EC Directive 2002/38/EC[16] was introduced with effect from July 2003 and provided that where a non-EU business supplies e-services to a EU private consumer, the place of supply will be the place where the customer resides. The effect of this is that non- EU businesses are required to register in every EU country where they have private customers. An optional electronic services scheme (the scheme) was introduced at the same time allowing such non-EU businesses to register in one EU country and to account for and pay in that country the VAT on all its supplies to EU private customers. The rate of VAT is the rate in the country in which the customer resides. On-line returns are submitted providing a breakdown of supplies to customers in each EU country. The EU country of registration distributes the VAT collected to the other member states in accordance with the returns.

At present there are six overseas traders registered in Ireland under the scheme and one other trader has ceased registration. From the commencement of the scheme to the end of 2005, €17.7m was paid to Revenue by suppliers. Of this, €0.3m was in respect of VAT on supplies to Irish customers and the remaining €17.4m was in respect of supplies to customers in other member states and was paid over to those states by Revenue (with almost half going to the UK). In turn, a total of €1.4m was paid to Revenue by seven other member states under the scheme (77% of which was from the UK). The total Irish VAT received by Revenue under the scheme to the end of 2005 was therefore €1.7m. In total, there are over 900 overseas traders registered under the scheme throughout the EU. Under the terms of the scheme, traders are required to maintain proper records of all transactions and make those records available, on request, to Revenue by electronic means. No checks have been carried out to date by Revenue on those records. It is not clear what sanctions are available to Revenue against those who fail to comply with the terms of the scheme and whether interest and penalties can be imposed.

[15] ICT Ireland is the representative lobby group for the high technology or knowledge sector within the Irish Business Employers Confederation.

[16] Directive 2002/38/EC was transposed into Irish Law in Finance Act, 2003. Revenue's VAT Information Leaflet 2/03 explains the different measures introduced by the Directive.

The Accounting Officer indicated that the six cases registered in Ireland were actively monitored for payments and returns compliance by the Collector General's Division. Further checks were being considered in consultation with Revenue's Computer Audit Services Branch. With regard to the special scheme introduced under the provisions of EU Council Directive 2002/38/EC, no unregistered businesses (all of which would be located outside the EU) trading in Ireland had been identified by Revenue. There was little doubt but that the special scheme has had a significant positive impact on VAT compliance by such businesses in the EU generally. While only six businesses are currently registered under the Scheme in Ireland, some 900 businesses have registered in the EU, and Ireland currently receives more VAT from other Member States than it receives net for itself from businesses registered under the Scheme here. On the question of whether the amount of €1.7m VAT collected under the special scheme is consistent with the level of supplies of e-services by non-EU businesses to Irish consumers, he said that while absolute measures were not available here, comparison was a useful proxy evaluation measure. In this regard the Irish net receipts did not seem unreasonable when compared to the net €59m received in the UK under the Scheme for the same period, given the sizes of the respective economies and having regard to the different broadband penetration rates.

## Commission Report on e-Services Scheme for External Suppliers

The July 2003 directive that switched the 'place of supply' rule for private customers was introduced on a temporary basis for three years. In May 2006, the EU Commission adopted a report to the Council on the operation of the Directive concluding that it had achieved its objectives and operated in a satisfactory manner, and proposed to extend its application beyond June 2006 to 2008. Among the issues noted in the Commission Report were

- the market for downloads and on-line services has matured and become more sophisticated since the Directive was adopted and that sales of digitally distributed music are reported to have tripled during 2005.
- in addition to the amounts collected under the scheme, VAT collected from businesses which opted to establish within the EU are likely to have been significant. The amount is difficult to quantify as businesses opt to set up in the EU for a variety of reasons and it is not possible to identify VAT receipts from particular services. While the rate of VAT in particular countries may have been a factor in the selection of the EU country in which to locate, some businesses appear to have chosen their place of establishment for other reasons.
- there was little indication that a significant number of overseas businesses availed of the option of registering in every EU country where they have customers.
- a further effect on VAT collected was that existing EU businesses no longer had any incentive to move their operations outside the EU to protect their competitive position.
- tax administrations should handle the issue of EU consumers circumventing systems to avoid payment of VAT in the context of materiality and proportionality.
- there were no problems reported by tax administrations in verifying the correctness of returns but this may be because the provisions relating to examining records have not been used on a systematic basis.

The EU Council further extended application of the Directive to December 2006.

# EU Internal Supply of e-Services

While there is no gap in the VAT coverage of supplies from EU businesses to EU consumers, there is an issue as to which country receives the VAT. VAT is a consumption tax and the principle is that the VAT should be a charge in the place of consumption. As can be seen from Table 17, the place of taxation for supplies between EU countries is the country where the supplier is established. Following the introduction of the 2003 scheme, overseas businesses set up operations in the EU and chose to locate in

countries with low VAT rates, and now pay VAT in that country. It was apparent that EU businesses also chose to locate in member states with low VAT rates in order to compete more effectively.

A Commission proposal in 2005[17] sought to address this issue by making such services taxable in the member state where the customer is established. This would mean that the influence of VAT rates on the place of supply would be neutral, as the service would be taxed at the rate applicable in the state of consumption. The Commission had already proposed a "one stop shop" mechanism to allow businesses use a single VAT number for all EU supplies and make VAT declarations to a single electronic portal from which they would be transmitted to the relevant member states. This would make it easier for businesses to meet their obligations when they become liable for VAT in a member state where they are not established. It is understood that discussions of these proposals is continuing at EU level.

# Physical Goods Ordered over the Internet

Goods, including goods ordered over the internet, imported into Ireland from outside the EU are liable to VAT and Customs Duty at the point of importation. However, relief is available for consignments with a value not greater than €22 and gift consignments where the value of the gift does not exceed €45. Separate reliefs are available for travellers who import goods on return from abroad. Revenue staff are permanently based in mail centres to monitor mail imports from countries outside the EU in order to detect contraband and ensure that correct VAT and import duties are paid. Packages are examined on a sample basis to establish that the correct amount of VAT and duty has been paid. The addressee is required to pay all amounts due before the package is released. However, as customs legislation does not provide for the imposition of civil penalties, there would appear to be little deterrent to those who might order package sized goods from overseas suppliers who describe items incorrectly or underdeclare the value of goods to help their customers evade tax.

The low-value reliefs are provided for practical reasons to avoid the need to collect small amounts of tax from private consumers. However, the effect is that goods ordered over the internet from a non-EU supplier are more competitive than those purchased locally. The report of the 1999 Revenue Working Group noted that the small packages relief distorted competition and that this distortion would be exacerbated by the expected increase in the volume of small packages and it may, therefore, be necessary to re-evaluate the relief.

The Accounting Officer confirmed that he was, in general, satisfied with the existing procedures in this area. It is an area that was kept under regular review both from a staffing and procedures viewpoint. He said that the Revenue Internal Audit Branch was conducting an audit of postal importations this year and, obviously, the results of that audit would inform Revenue thinking on the systems and processes currently in place. He had no evidence to suggest that the absence of penalties in addition to seizure of goods was seen as a weakness in the existing enforcement system. However, he added that Article 22 of the revised Customs Code being discussed by the EU at the moment foresaw the inclusion of a range of administrative penalties in all Member States to deal with any breach of community customs legislation. Revenue had established an internal Working Group to prepare the ground in this area, and will be in a position to introduce whatever measures are required if and when the new code enters into force in late 2006 or in 2007.

Equally, he had no evidence to suggest an information gap with regard to public awareness of the possibility of seizure in misdeclaration cases. He considered that any person and**,** in particular**,** any commercial operator who knowingly misdeclared the value or nature of their consignment for tax or duty purposes would have an expectation of the goods being seized in the event of detection. Finally, he confirmed that no increase in the abuse of low value/small package relief had been noted relating to e-commerce activity.

[17] COM (2005) 334 final

# e-Commerce and Tax Compliance

The 1999 Report noted that e-commerce presented challenges in terms of detecting those who tried to remain outside the tax system and those who join the system but do not disclose the full extent of their activity. The report made a number of suggestions with regard to how Revenue might identify e-commerce activity and the parties to such transactions. It considered that Revenue needed to actively look for indications as to whether existing businesses were involved in e-commerce. Websites may be set up offshore or offshore websites might front onshore businesses. Revenue needed to encourage voluntary disclosure of websites; it was proposed that a change in tax forms might ask about e-commerce and obtain details of e-commerce activities. Other possibilities included a requirement that tax numbers be displayed on websites, that stronger proofs of identity be required before domain names were assigned, and that Revenue would consult with other tax authorities in relation to their work in identifying e-commerce activities. The Report also referred to the technical expertise that would be required in order to access the detailed records of e-commerce transactions. That included staff resources and training devoted to computer audit, and access to a means of decrypting data.

Revenue's Computer Services Unit is attached to the Large Cases Division and currently has a complement of 10 staff. The Unit is available to provide training and to assist on audits in all Revenue Divisions.

In relation to the adequacy of current compliance procedures in regard to e-commerce, the Accounting Officer stated that Revenue's compliance activities focused on risk and in that regard he was satisfied as to their adequacy. Given the expected growth in e-commerce, Revenue fully appreciated the need to keep a critical eye on this area.

He pointed out that Revenue assessed major risk in the context of its Annual Risk Programme. Any risks included in this programme also identified clear courses of action to deal with the risk. Materiality and proportionality were relevant concepts in this regard. VAT on e-commerce (with a theoretical maximum tax at risk of significantly less than €80m) was not included in the current annual risk programme and that was indicative of the present assessment. Current assessment included the view that it was necessary to be very active on the international front and that was being done. It was an area, however, that was subject to ongoing review.

E-commerce activities were also monitored by the Special Compliance Units in the course of projects that focused on identifying cases in the hidden economy. The results of their findings to date had not highlighted any areas of major concern in relation to e-commerce transactions.

Furthermore Revenue assessed individual risk through its programme of audit screening by expert auditors, and more recently through the use of the new risk analysis tool, currently being rolled out and available in four pilot districts for over a year, and the sectoral projects initiated in the Regions. In addition, Revenue pursued the filing and payment risks through their returns and payments compliance programmes. In all programmes there was constant risk assessment. Revenue carried out over 14,000 audits in 2005. In an audit all aspects of a business (traditional and electronic) are reviewed as appropriate.

He also referred to the pending availability for examination by Revenue of internet tools from the EU Commission Project Group, to current consideration of further research in the area, and to the continuing expansion of e-audit capabilities through the increase in the use of its Computer Audit Services Branch, the provision of high quality training and the recruitment of a specialist e-Auditor. He noted that the Computer Audit Services Branch had assisted in 82 cases since its establishment almost three years ago.

# Summary Response of the Accounting Officer

From the information available, Revenue considered that despite the growth in e-commerce, the overall risk to VAT revenue remained relatively low, which is a conclusion that has also been drawn by other tax

authorities, most notably the UK. It was noted in the audit report that the ICT 2006 budget submission estimated that Ireland's share of the European spend on business-to-consumer (B2C) electronic transactions would grow to some €400m in 2006. B2C transactions, being the final transactions in the production and distribution chain, were generally regarded as posing the greatest risk of VAT loss; with business-to-business (B2B) transactions VAT was generally passed on through the chain without any great difficulty. Thus, applying the standard rate of VAT of 21% to the ICT estimated amount of B2C electronic transactions would indicate a maximum exposure of some €80m of VAT liability. But even that relatively small amount would have to be scaled down further, when one took into account the not unreasonable assumption that much of the e-commerce business with Irish consumers was by Irish-based businesses, which were already well policed by Revenue under its standard business programs, and that a significant amount of such business would not attract a VAT liability at all; for example, sales of books, most food, medicines and children's clothing are zero-rated for VAT purposes. Thus, in the context of an estimated VAT yield of some €14 billion for 2006, the risk to VAT revenues from e-commerce was seen as relatively minor.

The internet was a genuine global phenomenon and the idea that Revenue, or indeed any other single tax administration should, or could, unilaterally resolve taxation issues that might arise in relation to it would be to ignore this international context. The focus of developments in this area must be, therefore, in multilateral arenas i.e. EU and OECD. For example, in recognition of the need to be able to detect and identify internet trade, a number of EU Member States have developed, or are in the process of developing, electronic tools to facilitate the monitoring of internet trade, the analysis of its trends and the identification of high risk websites and internet supplies. To this end, in March 2006 the EU Commission decided to set up a project group to investigate the tools and techniques available to aid in the detection of traders operating on the Internet. The project group will draft a report for the EU's Fiscalis Committee. The mandate of the group will be to examine, describe and test the existing tools more thoroughly, and to report on the extent to which the tools meet the functionality of the most efficient Internet search tool, and especially how Member States can obtain the tools. Where appropriate, the project group will work on profiles and other relevant ways to facilitate the identification of high-risk traders. Revenue applied for membership of this group in order to identify and acquire the most appropriate tool for its needs and its application had recently been accepted.

The Accounting Officer stated that Revenue would continue to work with its EU and OECD partners with a view to introducing measures and procedures, which best protected the national Exchequer. In this regard, the audit report referred to the EU Commission proposal to make services taxable in the Member State where the customer is established. This is also a principle that has been agreed at OECD level. Certainly, it is envisaged that the Commission's proposals for a "One-Stop-Shop" should facilitate greater compliance by businesses with their VAT obligations generally. These proposals would allow businesses to comply with their VAT obligations in a number of Member States through use of a single web-based portal, and would allow tax authorities access to VAT, business and transactional information across all Member States. The EU Commission's Fiscalis 2013 programme would also provide opportunities for the EU to develop co-operation with third countries, which was required to tackle the increasing international dimension of tax fraud and evasion and which would include information exchange.

He pointed out that, while the June 1999 Report of the Revenue Working Group was quite farseeing for its time, in the context of its subject matter seven years was an extremely long time. For example, at the time the Report was being completed only 14% of Irish people were connected to the Internet, and Broadband was not even mentioned. Revenue was at present exploring the potential or indeed the need for further research in this area in the light of relevant international studies already completed or ongoing, with a view to ensuring that its understanding in this important area was not found wanting.

# 2.9 Assessment and Collection of Capital Gains Tax

Capital gains arising on the disposal of a wide range of assets are subject to Capital Gains Tax (CGT) at a standard rate of 20%, with a 40% rate applying to disposals of certain foreign life assurance and investment products. Capital gains accruing to companies are chargeable to Corporation Tax with the exception of development land and non-trading assets of non-resident companies situated in the State. The self-assessment system applies to CGT and taxpayers must make returns without being requested to do so by Revenue.

A purchaser of certain assets[18] where the consideration for the disposal exceeds €500,000, is obliged to withhold CGT equal to 15% of the sales proceeds and pay it over to Revenue. Tax is not required to be withheld where the vendor produces a clearance certificate from Revenue. The certificate is issued on application provided the vendor is resident, or there is no CGT payable in respect of the disposal, or that CGT payable in respect of the disposal, and previous disposals, has been paid.

**Table 18 CGT Net Receipts 2001 to 2005**

| | 2001 | 2002 | 2003 | 2004 | 2005 |
|---|---|---|---|---|---|
| CGT Net Receipts | €876m | €619m | €1,436m | €1,528m | €1,982m |

The yield from CGT for the years 2001 to 2005 is shown in Table 18. CGT receipts have more than doubled during that period, and have exceeded the annual budget forecast by an average of more than 50% over the last three years. The yield for 2005 was €1,982m which surpassed the net yield of non-PAYE Income Tax of €1,961m.

## Audit Objectives and Scope

While there is an additional risk posed by the one-off nature of transactions in CGT over the repeating nature of some other taxes, this is counter-balanced by the availability for compliance activity of information obtained from applications for clearance certificates and, in the case of certain assets, of data from Stamp Duty transactions. The objectives of my audit in March 2006 were

- To review the extent of Revenue consideration of the implications of the growth of CGT yield
- To test a sample of cases in order to establish the adequacy of the operation of ongoing compliance activity, particularly the follow-up of clearance certificates issued
- To establish the extent to which Revenue was availing of the possibility of cross-checks with Stamp Duty data.

My staff reviewed compliance procedures and examined a sample of cases in one tax district in each of the Dublin and East/South East Regions, and a unit of Large Cases Division. In addition, the question of whether a CGT liability was recorded in a selection of cases sourced from Stamp Duty transactions was examined. Documents and reports were reviewed and, together with the test results, were discussed with Revenue officials.

[18] The assets concerned are land and buildings in the State, mineral assets in the State, exploration or exploitation rights in a designated area, unquoted shares deriving their value from the above assets, unquoted shares received in exchange for such shares qualifying for S584 relief, the goodwill of a business carried on in the State and certain transactions which do not involve the purchaser acquiring an asset.

# Internal Revenue CGT Reports

The reports of two internal Revenue reviews of aspects of CGT were examined. The first, by Large Cases Division in 2004, investigated the extent to which taxpayers may be attempting to reduce their tax liabilities by re-categorising income as gains. More recently, in February 2006, the Office of the Collector General prepared an analysis of CGT yield for Revenue's Management Advisory Committee.

## Large Cases Division Analysis of CGT Taxpayers

As the CGT rate of 20% is less than the higher rate of Income Tax (42%), taxpayers could reduce their tax liabilities by re-categorising income as gains. In 2004, the Large Cases Division carried out an analysis of the largest CGT payers in 2002 and concluded that there was no evidence to indicate that such a practice was widespread.

60 cases with CGT payments of more than €1m were examined and 10 of these were audited[19]. There were no issues arising in 35 of the 60 cases, 8 cases were found to have computational errors or to require technical adjustments with additional CGT of €2.5m being paid, and 17 cases are still under enquiry. Information has been submitted and is being examined in four of the cases under enquiry and information is awaited on relation to the other 13. In one of the four cases where information has been submitted there appears to be possible income to gain conversion.

50 cases where payments of CGT of between €250,000 and €300,000 were made were also reviewed. 11 were audited with the following results

- 2 cases were resolved without further enquiry
- 2 cases had computational errors giving rise to additional payments of €369,424
- 2 cases are under appeal
- 1 case has been recommended for consideration under anti-avoidance legislation[20]
- 4 are still under enquiry, including one case referred to the Valuation Office.

Three of the cases still under enquiry involve possible income to gain conversion. The two cases under appeal also involve income to gain conversion and the additional tax involved is €1.1m. The Appeal Commissioners have requested a written submission from Revenue in one of these cases and in the second case consideration is being given to appointing counsel to represent Revenue at appeal.

## Collector General's Analysis of CGT Yield

In February 2006, Revenue's Management Advisory Committee considered a report prepared by the Collector General on a statistical analysis of the CGT elements of the Form 11 Income Tax Returns for 2004 filed through the Revenue On-Line Service (ROS), and of the largest CGT payments in 2005. The main conclusions and recommendations of the Collector General's analysis were

[19] Supporting documentation, generally the contracts, was requested and examined in the 60 cases. Further action, including a request for more information and/or a meeting with the taxpayer and their agent, was taken in 10 cases.

[20] Section 811 of Taxes Consolidation Act, 1997. Revenue can form the opinion that a transaction has little or no commercial reality but is intended primarily to avoid, or reduce tax or create a tax deduction or refund. Notice is given to that effect and describes the action that Revenue proposes to take. If not appealed or upheld at appeal Revenue is empowered to take the steps described in the notice in order to defeat the tax avoidance scheme.

- The yield from CGT appears to be driven by gains from land sales and, to a lesser extent, equities and property. Continuing strong yield is therefore dependent on the buoyant property market and business profitability.
- CGT is now a significant tax and should therefore attract an equivalent level of compliance attention.
- Although the yield is rising each year, there is no accurate analysis of the levels of non-compliance. Notwithstanding the timing differences between Stamp Duty and CGT, the relationship between the two needs to be exploited to help bridge the compliance gap.
- CGT paid is generally paid on time and only 3% of the 2005 receipts were paid late.
- Further examination of possible shifting of income to gains may be worthwhile.
- Revenue may need to assess the risk to the tax base arising from the movement of significant capital abroad.

The Management Advisory Committee noted the contents of the Collector General's analysis and agreed that CGT needed to attract a significant level of compliance attention. The 2006 business plans would focus on compliance and the Revenue Risk Project Group would consider the risks, including further analysis of the risk of conversion of income to gains.

# Audit Findings

**Follow-up of Clearance Certificates**

Clearance certificates are issued by districts from a database that records details of the certificates. In the Dublin district, details of clearance certificates issued are also recorded on a control spreadsheet to facilitate monitoring and subsequent follow-up. However, at the commencement of the audit, there was no indication on the control spreadsheet of assessment activity in relation to 617 of the 706 clearance certificates issued by the district in the period November 2003 to December 2004, and which had not been exempted as Principal Private Residences (PPRs)[21]. Since March 2006, the District has been working through the cases and comparing the details to the CGT returns, referring cases to other districts and noting further cases as PPRs mainly from information on the return. The updated spreadsheet shows 148 cases not marked as PPRs but where the liability has not been assessed. These 148 cases are being enquired into by the District mainly through the issue of letters requesting the return, or computation, as appropriate.

The district in the East/South East Region did not maintain a control spreadsheet of clearance certificates issued. A reduced level of check applied in that samples of certificates issued were subsequently selected from the database by the relevant compliance and audit districts for follow-up. In the unit of Large Cases Division, an officer is assigned to deal with all the tax affairs of each case and so has a detailed knowledge of all activities in a particular case. For this reason, a control spreadsheet was not required in that area. Instead each officer's case records will note the issue of a clearance certificate.

The Accounting Officer informed me that current standing instructions required a record to be maintained of clearance certificates issued, and for that record to be periodically reviewed with a view to having assessments raised if necessary. He also said that work has commenced on incorporating clearance certificate information into the data warehouse which would facilitate its integration with Revenue's main systems. In relation to the 148 cases on a district spreadsheet, the Accounting Officer has informed me that 53 have since been identified as PPRs, assessments have been raised in 15, assessments were not required (covered by losses, etc) in 29, and 51 are still under enquiry. CGT has been paid in all cases assessed and surcharges for late payment have been imposed in four cases. He pointed out that from

[21] No CGT is payable on gains arising from the sale of PPRs.

November 2006, the computer system will automatically generate a surcharge for every late return. All cases would be pursued to finality. All outstanding cases had received reminder letters, and estimated assessments would be input in the near future as appropriate.

**Examination of Sample of Clearance Certificates**

A number of issues were noted from an examination of a sample of 37 clearance certificates issued by the three districts, and from a review of the taxpayers' records and any subsequent returns. These included instances where

- there was no return or CGT payment for the period to which the clearance certificate related
- the consideration per the clearance certificate issued did not appear to be consistent with that shown on the subsequent return
- there was no note on Revenue's main computerised taxpayer record to indicate that a clearance certificate had been issued.

The Accounting Officer stated that review of the cases with no returns or payments is ongoing. He pointed out that there were many legitimate reasons why the amounts on a clearance certificate and a return might not agree arising from the wide range of reliefs, allowances and exemptions, such as Principal Private Residence and Retirement Reliefs. However, four of these cases have been noted for audit (the audit has commenced in one). He stated that as the issue of a clearance certificate was noted on taxpayer files for information purposes only, procedures in that regard may vary somewhat from Region to Region. However, there would be a general requirement that they be entered as promptly as possible. The manual entering of these notes would become redundant when clearance information was captured in the data warehouse.

**Cross-check with Stamp Duty Data**

During my audit, Stamp Duty payment details were examined relating to 12 property transactions in late 2003 and 2004 where the consideration was greater than €500,000. These involved the sale of property by 16 taxpayers, two of which were companies. A number of issues were identified including

- five cases where there was no return or CGT payment for the period.
- three cases where there were possible inconsistencies between the recorded Stamp Duty details and the subsequent return.

The Accounting Officer informed me that the eight cases identified on the Stamp Duty cross check were subject to ongoing examination.

# Wider Audit Concerns

In addition to inviting the views of the Accounting Officer on matters arising from the cases examined during my audit, I also sought his observations on wider audit concerns arising both from those cases and from a review of the two Revenue reports. In particular, I inquired whether

- Revenue had completed its appraisal of the extent of the shifting of income to gains
- he was satisfied that Revenue was making full use of the valuable information available as a result of the clearance certificates and Stamp Duty payment details
- a formal assessment had been carried out by Revenue of the level of CGT non-compliance
- he was satisfied that current procedures were adequate to ensure that all CGT was promptly assessed and collected.

# Accounting Officer's Response

### Income to Gains Substitution

The Accounting Officer stated that in light of the exceptional growth in CGT yield and because there is a divergence in tax rates between income and capital gains, Revenue's management advisory committee considered it prudent to consider whether there was any evidence that some individuals were shifting income to gains (the substitution effect). In keeping with sound risk management, Revenue would continue to keep such a situation under regular review. The review by Large Cases Division in 2004 did not find evidence to support a serious concern about the prevalence of the substitution effect. However, as a result of the review, Section 817 of the Taxes Consolidation Act, 1997 was amended in the Finance Acts 2004 and 2005 to close off possible loopholes. The Accounting Officer said that the Collector General's analysis quoted figures that broadly supported the earlier Large Cases Division review of the substitution effect. These figures showed that of the 237 taxpayers that paid over €1m in CGT in 2005

- Only 24 individuals had regular CGT liabilities in each of the previous three tax years,
- Only five of the 24 individuals had a CGT liability greater than an Income Tax (schedule D and E) net liability in each of the three years.

One of the Collector General's conclusions i.e. that it may be worthwhile to carry out further examination to confirm there was no substitution effect, reflected the general Revenue view that it was a matter that should be kept under regular review. In support of this, the Management Advisory Committee approved a number of measures. Responsibility for the establishment of a Risk Project Group, had been assigned to the Operations Policy and Evaluation Division and work would commence in the second half of 2006. Because of timing factors it had been necessary to deal with work in this area in the context of the 2007 Business Plans. Besides the Large Cases Division review and the Collector General's paper, he also pointed to a separate exercise carried out in a Dublin Tax District in Spring 2005 on 60 of its largest CGT payers. All cases were screened and audits were carried out on 10 of them. That exercise found only one possible substitution effect case. That case was currently under enquiry with the Anti-Avoidance Unit.

### Cross-check with Stamp Duty Data

The Accounting Officer informed me that there was a strong correlation between the information from the Stamp Duty payment data and clearance certificates, but that there were exceptions where there would not be a complete match between the two declarations e.g. if the value of the transaction was less than €500,000, or for builders disposing of newly constructed houses. Stamp Duty details were returned in relation to property transactions but not all property transactions were subject to CGT, e.g. residential and non-residential (Section 643) development land, which may be chargeable to income tax. Despite these and other exceptions and the timing difference between Stamp Duty and CGT, he is generally satisfied that Revenue was making the best use possible of the information available to it to maximise CGT compliance. He emphasised that use of the information could only be maximised when it was fully captured in the data warehouse and available for risk profiling of individual taxpayers. The Risk Evaluation, Analysis and Profiling (REAP) system included rules on CGT/stamp duty transactions. This system was being implemented nationally and would be further developed over the coming years. Already the system included risk related rules which were used to highlight individual cases. The rules checked cases with regard to the following

- a mismatch between an asset purchase (either from Stamp Duty or CGT data) and declared income
- an asset sale (either from Stamp Duty or CGT data)
- CGT liabilities outstanding or paid late
- a mismatch between a CGT payment and the non-inclusion of CGT information on a return (or the absence of a return), or

- the payment of a CGT liability against declared income.

**CGT Compliance**

In relation to the level of CGT compliance, he said that there was ongoing assessment at central, regional and district level of general risk, including specific taxhead risk. For example, the Collector General's analysis concluded that CGT payment compliance was very high with late payments responsible for only 3% of yield in 2005. In addition, a number of Districts had carried out CGT compliance campaigns and the issues or risks highlighted had been disseminated within Revenue via the Capital Taxes Network. One of those compliance initiatives was an ongoing project in relation to the CGT risk on the disposal of second non-principal private residences by Irish residents, and the disposal in the State of properties by foreign residents. 113 cases were currently under examination, 68 of which were resident and 45 non-resident. CGT risk issues would, of course, continue to be screened as part of the normal ongoing compliance/audit programmes.

**Adequacy of Current Compliance Procedures**

The Accounting Officer stated that CGT was a self assessed tax and that taxpayers were obliged to make returns without being requested to do so by Revenue. Furthermore, CGT was also an event driven tax and Revenue's compliance approach must take those factors on board. He was satisfied generally that current procedures were adequate and adequately employed to ensure compliance with the CGT legislation. Procedures, mainly due to developments in the IT area, were undergoing significant change. Those developments included, for example, the electronic capture of information (either from ROS or paper filed returns), the wide availability of that information for officials via the Integrated Business Intelligence application on the intranet, the use of that information by REAP, and the inclusion of CGT assessing in the mainstream Integrated Taxation Services system. Finally, he mentioned the Operations Policy and Evaluation Division's plans to conduct a risk examination of CGT later this year; some initial scoping work had already taken place.

# 2.10 The Management of Tax Appeals

## Background

A taxpayer who is dissatisfied with a decision or assessment made by the Revenue Commissioners has a right to submit an appeal in writing through Revenue to the Appeal Commissioners. This must be done within a limited period that varies from tax to tax (e.g. VAT: 14 days from date of estimate or 21 days from date of assessment, Income Tax : 30 days from Revenue assessment). The appeal is lodged with the officer of the Revenue Commissioners, formerly known as an Inspector of Taxes, who had been handling the case.

A taxpayer who remains dissatisfied following the decision of the Appeal Commissioners may appeal to the Circuit Court for a complete re-hearing. With the exception of Capital Acquisition Tax, there is no corresponding provision for appeal by Revenue. A point of law arising on a decision of the Appeal Commissioners may be referred to the High Court (or Supreme Court if necessary) by way of *case stated* at the request of either party to the appeal. An overview of the tax appeals process in diagrammatical format is shown in Figure 1. The role of the Appeal Commissioners is represented by the two shaded boxes.

Paragraph 20 of my 1999 Annual Report noted that, as part of the ongoing general review of the systems, procedures and practices applied to the assessment and collection of revenue, I had sought information regarding the annual throughput of appeals cases and the overall summary of outcomes e.g. decided in favour of the taxpayer or Revenue, appealed to the Courts, and of the extent of cases on hand. The response indicated that each case was dealt with on an individual basis from scheduling to hearing. While details of issues of principle were published, the Appeal Commissioners were not a tribunal of record and were not required to, and did not, retain a written record of determinations, proceedings or documents submitted. The Appeal Commissioners or Revenue did not retain statistical or summary records. Revenue estimated that between 500 and 600 cases had been lodged with the Appeal Commissioners in 1999, and that approximately 250 cases were heard and decided annually. The remaining appeals were either withdrawn or settled prior to a hearing.

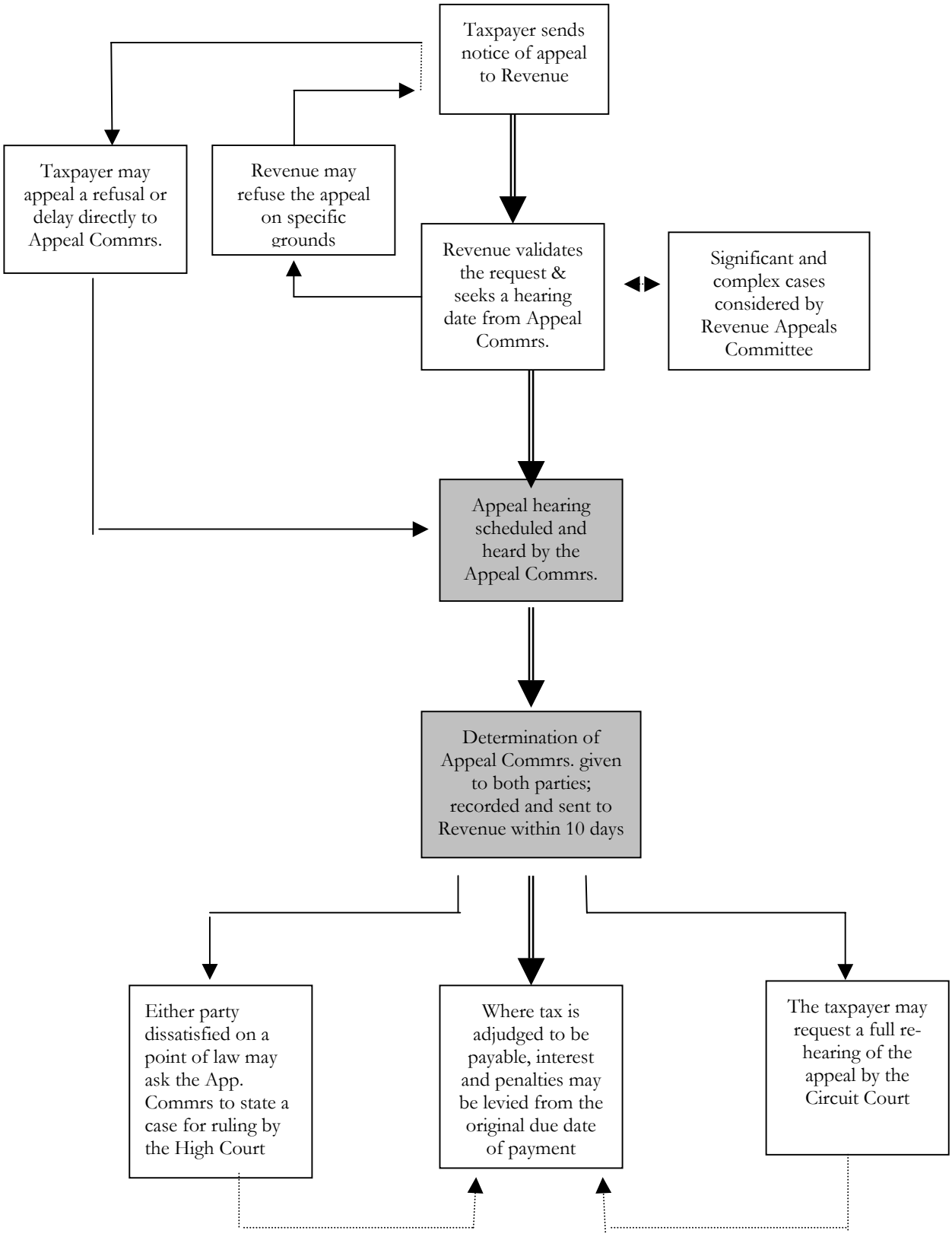
## Tax Appeal Procedure[22]

### Lodgment of the Appeal with Revenue

Each appeal application is reviewed by Revenue to establish that the statutory conditions have been met. An appeal is not allowed in cases where the appeal is outside the relevant time limit, or where all tax due – other than the amount in dispute – has not been paid. Where it is decided that an appeal is not allowable, a notice of refusal is issued by Revenue to the taxpayer. The taxpayer may appeal against this decision directly to the Appeal Commissioners within 15 days of the notice of refusal. A taxpayer can also appeal directly to the Appeal Commissioners at any stage if he feels that there is undue delay within Revenue.

[22] Taxpayers can request that Revenue's handling of their tax affairs be reviewed by a senior Revenue official locally, by another senior Revenue official or jointly by that other official and an external reviewer. This does not interfere with the taxpayer's right to submit an appeal to the Appeal Commissioners. This internal review process was not examined.

**Figure 1 Overview of the Tax Appeals Process**



When it is decided that an appeal is in order, a Revenue form (AH1) outlining the case from both sides is sent to the taxpayer. A taxpayer who is not satisfied with the Revenue outline may complete and return an independent statement on a second form. Revenue forwards the form(s) AH1 to the Appeal Commissioners, together with an estimate of the likely length of time required for the hearing, and a request for a hearing date. The case is listed by the Appeal Commissioners who notify Revenue of the date, venue and time. Revenue then notifies the taxpayer of the hearing details.

## The Hearing of the Appeal by the Appeal Commissioners

The Appeal Commissioners, through Revenue, may request further submissions prior to the hearing, in order to speed up the process and to allow for a review of the case before the hearing begins. Where further information is supplied by the taxpayer prior to the hearing of a case, Revenue may review the case and come to a settlement with the taxpayer. The appeal is then withdrawn. The taxpayer may also withdraw the appeal at any time, for any reason.

Appeals are heard by an Appeal Commissioner at the Dublin headquarters of the Office, or in Circuit Court offices at various locations outside Dublin. Cases are heard *in camera* but taxpayers and Revenue may be professionally represented at the hearings. The decision on an appeal is normally announced on the day of the hearing, with both parties present. The finding is subsequently notified in writing to Revenue (on form AS1).

# Office of the Appeal Commissioners

The Appeal Commissioners are appointed by the Minister for Finance under Section 850 of the Taxes Consolidation Act, 1997 to hear appeals by taxpayers against assessments or decisions of the Revenue Commissioners concerning taxes or duties. Decisions of the Appeal Commissioners are based on findings of fact determined from the evidence presented at the hearing, and by interpretation of tax law. Prior to 1978, appeals were heard by one or other of two Commissioners. Following an increase in workload, a third Commissioner was appointed in that year, but the number reverted to two in 1993 in the aftermath of the introduction of self-assessment.

A separate vote for the funding of the Office of the Appeal Commissioners was established in 2003, with one Commissioner serving as Accounting Officer. Previously, the salaries and expenses of the Appeal Commissioners were paid through the Revenue Vote. The Commissioners are assisted by two support staff, who act as clerks to the Commissioners. The recruitment of a further staff member has been sanctioned by the Department of Finance, but an appointment has not been made. Total expenditure amounted to €344,000 (Est. €561,000) in 2003, €357,000 (Est. €571,000) in 2004, and €399,000 (Est. €607,000) in 2005.

However, outside of the listing and hearing of cases, the Office of the Appeal Commissioners relies on Revenue for the processing of financial transactions and other services such as personnel, training and information technology. The Accounting Officer receives a monthly report on expenditure from Revenue. The arrangements are formalised in a Service Level Agreement between both Offices signed in February 2005.

The Appeal Commissioners' web site is hosted and maintained by the Irish Taxation Institute. There are at present 31 determinations listed on it, 25 relating to 2000, 5 relating to 2003 and 1 case relating to 2005. It also contains a calendar of hearing dates and venues for the current term and a Freedom of Information Guide relating to the Appeal Commissioners. The Commissioners do not issue an Annual Report covering developments or activities, and have not prepared a statement of strategy or a business plan. Statistical or summary records of cases, throughput, outcomes and decisions are not maintained.

# External Reviews of the Operation of the Appeal Commissioners

Arising from the Committee of Public Accounts Parliamentary Inquiry into DIRT, various parties prepared proposals in relation to the role and operation of the Appeal Commissioners, and the issue was also considered in the final report of the Committee of Public Accounts in April 2001. During the period 2000 to 2003, reports and submissions prepared by the following bodies and groups included proposals and recommendations for improving, reforming or extending the tax appeals process as operated by the Appeal Commissioners

- D/Finance Steering Group on the Review of Revenue – August 2000
- Submission of the Institute of Taxation to the PAC Inquiry – February 2001
- Submission by Revenue to the PAC Inquiry – February 2001
- Submission by the Appeal Commissioners to the PAC Inquiry – March 2001
- PAC DIRT Inquiry Final Report – April 2001
- Law Reform Commission Report on a Fiscal Prosecutor and a Revenue Court – July 2003.

## Recommendations Made

Many of the proposals covered the broader aspects of the status and functions of the Appeal Commissioners ranging from appointment of commissioners, jurisdiction, statutory basis, legislative changes, to the extension of the Commissioners' role. However, other recommendations, which are listed in Figure 2, are of more direct interest to this review as they might be seen as indicators of perceived weaknesses in the current operations of the Office of the Appeal Commissioners, and as providing opportunities for improved performance in the area of tax appeals.

**Figure 2 Recommendations relating to Current Operations and Performance of the Appeal Commissioners**

| | D/Fin Revenue Review Group | Institute of Taxation | Revenue Commissioners | Appeal Commissioners | PAC DIRT Sub Committee | Law Reform Commission |
|---|---|---|---|---|---|---|
| Publication of Annual Report | ● | ● | | ● | ● | |
| Comment on areas of Tax Legislation through report | ● | | | | | |
| Provide Separate Vote and Accounting Officer | ● | | | | | |
| AO to conduct a review of adequacy of resources | ● | | | | | |
| Name of the Office does not indicate independence | | ● | | | | ● |
| Formal rules required due to delays in listing cases | | ● | ○ | | | |
| Formal rules req'd due to delays issuing decisions | | ● | ○ | | | |
| Publication of determinations in detail | | ● | | | ● | ● |
| Appointment of a third Appeal Commissioner | | ● | ● | ○ | ● | |
| Review of IT requirements incl. Website | | | | ● | ● | |
| General review of administration systems | | | | ● | | |
| Review of staffing requirements | | | | ● | | |
| Establish a case management system in the Office | | | | ● | | |
| Objectively establish a realistic budget for the Office | | | | | ● | |
| Ending of Revenue responsibility for listing appeals | | | | | | ● |
| Issue concise written determination within 3 months | | | | | | ● |

- Denotes support for the recommendation by the body or group.
  - o Recommendation considered not to be necessary by the body or group.

# Objectives and Scope of the Audit

The statutory appeals process is an important safeguard for the taxpayer in his/her relationship with the tax system. It also provides a reasonableness check on the tax assessment process. My audit sought

- to establish whether there had been any development of the systems, procedures and practices for the management of tax appeals in Revenue and in the Office of the Appeal Commissioners since my 1999 Report
- to consider the extent to which the annual throughput of appeals cases and of case time elapsed in both Offices was indicative of the efficient resolution of appeal cases
- to ascertain whether the outcomes of appeals were analysed and summarised to provide management information within Revenue, or published by the Appeal Commissioners for the benefit of taxpayers in general.

As can be seen from Figure 1, responsibility for the management of tax appeals is in effect shared by two independent Offices who each perform the distinct roles assigned by the Taxes Acts. Notwithstanding

the distinct statutory roles, the audit addressed the appeals process as a continuous one that commences with the lodgment of the appeal and concludes with a determination by the Appeal Commissioner i.e. from the taxpayer viewpoint.

The audit findings are based on the review of procedures and documentation, the analysis of data from Revenue systems, the extraction from Revenue records of the time elapsed at each stage of the appeals process in respect of a sample of cases, on informal discussions with officials in Revenue and in the Office of the Appeal Commissioners, and on formal correspondence with the Accounting Officers of Revenue and the Office of the Appeal Commissioners.

The performance of a case-tracking exercise following a sample of appeal cases through Revenue and the Appeal Commissioners was an important part of the original plan for the examination. However, this could not be completed as the Accounting Officer of the Office of the Appeal Commissioners had a serious doubt as to whether it was within his jurisdiction to supply my Office with the information and documentation requested in relation to taxpayers. He has sought the opinion of the Attorney General in the matter, and that is still awaited. As a consequence, all data analysis and selection and sampling of cases were, of necessity, performed only on Revenue records and case files.

# Tax Appeals Process within Revenue

## Standard Practice

In general, normal and routine appeals are handled on an individual case basis by the officer with previous responsibility for the case. Revenue practice is that tax cases that have been appealed are sent on to an appeal hearing only after every reasonable effort has been made to settle the case by negotiation without conceding any important point of principle. Assistance in relation to presentation and argument of cases is available from the Revenue Legislation Services (RLS) Divisions to individual officers handling appeals. In order to comply with time limits, a case stated to a higher court is demanded by Revenue in all cases where the case officer is dissatisfied with the determination of the Appeal Commissioners or the Circuit Court on a point of law, and the issue is considered sufficiently important to warrant consideration of appealing the matter to the High Court. The demand may be withdrawn subsequently following consideration.

## Referrals to Revenue Central Appeals Committee

Officers are required to refer particular appeal cases to an Appeals Committee within Revenue before the form AH1 is sent to the Appeal Commissioners. The Appeals Committee was formed to identify significant issues that might give rise to concern for the quality and standard of Revenue's approach to "argument appeals", as well as to oversee and co-ordinate such appeals. Specific responsibilities include

- Implementing a consistent and effective approach to the selection and presentation of appeals for the higher courts
- Deciding on whether engagement of counsel should be approved in particular cases
- Ensuring a free flow of information throughout Revenue regarding cases taken to appeal to the higher courts
- Ensuring appropriate technical input is received from the RLS divisions
- Monitoring the timely passage of appeals through the appeal process.

Cases that are required to be sent to the Appeals Committee are

- All cases in which an appeal to the higher courts is likely

- Where an officer considers that counsel should be retained
- Where the point at issue is seen as having wide precedent significance
- Cases involving a significant amount of tax or duty
- Cases involving avoidance and avoidance schemes
- Where a *case stated* has been demanded and the Committee has not already considered the case.

## Information on Progress of Appeals

The Appeals Committee circulates decisions taken e.g. how a case is to be handled, and whether counsel is to be retained, to the individual officers, to regional liaison officers, and to all Assistant Secretaries. In cases where the retention of counsel has been approved, details of the issues are placed on the Revenue intranet for general information of staff. Where the question at issue is already awaiting hearing by the higher courts, or has previously been dealt with in some other way, further similar cases will be returned to the region or division to await the outcome of the previous case or to be dealt with in accordance with the previous decision. The case officer provides the Committee with brief reports at each appeal stage of cases where counsel has been authorised. The Committee makes a six-monthly report to the Revenue Board on the progress of cases under appeal to the higher courts.

## Role of District Manager

In addition to the specific roles of the case officer and the Appeals Committee, the manager of each tax district is expected to be closely involved in

- The selection of cases for consideration by the Appeals Committee
- Ensuring a consistently high standard in the preparation and presentation of the Revenue case at appeals
- Monitoring progress at each subsequent stage in the appeal process.

## Records of Appeal Cases

Revenue does not maintain a central or regional record of tax appeals giving basic control information e.g. a listing of all appeals received, the details and issues involved, current position, date sent to the Appeals Commissioners, and the outcome. As stated above, the Appeals Committee maintains a detailed record of current cases that are under the guidance of the Committee; other cases are a matter for the individual case officer. However, when an appeal is received, it is necessary to suspend all enforcement action for the amount in dispute. This is achieved by the input of a 'Stop' instruction to the taxpayer's computer record – a 'Stop16' for tax cases under appeal.

# Selection and Analysis of Audit Sample

As a statistical or summary record of appeals cases, throughput, outcomes and decisions is not maintained by Revenue, it was necessary for the audit to use the movement in Stop 16s as an activity indicator in these areas. The quality of this information is likely to be good following action taken in response to unfavourable Revenue Internal Audit comments in 2003 on uncleared stops. During the course of audit, a database was obtained of cases where the "under appeal stop" was put on the case in each of the years 2000 to 2005. The database showed the dates on which the stop was inserted and later removed. There were 3,104 cases in total on the database. Table 19 shows the number of cases categorised by the year the stop was inserted and the period of time the stop was in place as at May 2006.

**Table 19 Database of Cases with Appeal Stops**

| Period Stop in Place | Stop put on in year | | | | | | Total |
|---|---|---|---|---|---|---|---|
| | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | |
| 0-6 mths | 142 | 132 | 244 | 197 | 208 | 231 | 1,154 |
| 6-12 mths | 63 | 54 | 63 | 47 | 48 | 46 | 321 |
| 1-2 yrs | 53 | 91 | 46 | 58 | 47 | 7 | 302 |
| 2-3 yrs | 64 | 31 | 38 | 27 | 2 | n/a | 162 |
| 3-5 yrs | 115 | 56 | 13 | 2 | n/a | n/a | 186 |
| Still in Place | 40 | 49 | 54 | 69 | 155 | 612 | 979 |
| **Total Cases** | **477** | **413** | **458** | **400** | **460** | **896** | **3,104** |

While the Stop 16 data does not indicate the ongoing status of each case, an analysis of a random sample of 43 Stop 16 cases up to end 2005 gave the following results

- six had been entered in error (one remained uncorrected from November 2005)
- of the 37 valid appeal cases, only 11 cases had been sent to the Appeal Commissioners by Revenue
- with the exception of one case of 79 months, the time elapsed between the date of receipt of those appeals in Revenue and the cases being sent to the Appeal Commissioners ranged from less than 1 to 27 months; the appeal in the case of 79 months was held up pending the outcome of other cases
- Hearings had been listed in 8 of the cases; the time elapsed between the date of submission to the Appeal Commissioners and the hearing date ranged from 1 to 8 months.
- Of the 8 cases, 3 were settled prior to hearing, 5 were heard, and determinations have been made in 3 of those. The time between hearing and determination in the three cases ranged from 3 to 15 months.
- Cases not forwarded to the Appeal Commissioners had been held in Revenue for periods of 8 to 17 months.

Only three cases from the sample of 37 passed through the full appeals process. The overall elapsed time in those cases three cases was 83 months[23], 30 months and 18 months.

## Audit Issues

The results of the audit sample suggest that the system for handling appeals is not as efficient as it could be, and I sought the views of the Accounting Officers of Revenue and of the Appeal Commissioners.

In particular, I sought observations from Revenue on the lack of records, the management of appeals and control of Stop 16s. As regards the Appeal Commissioners, I asked for information on the throughput of cases, the administration of the Office and the level of implementation of the various recommendations set out in Figure 2.

[23] This total includes the 79 months with Revenue noted earlier.

# Responses of the Accounting Officers

## Length of Time Required in Appeals Cases

The Accounting Officer for the Office of the Revenue Commissioners indicated that the duration of any case within the Appeal Commissioners was not a matter for his Office. He noted that the findings in respect of elapsed time in Revenue did show a large variation between individual cases which tended to reinforce his view that it was the nature of the case that determined the length of time to have it submitted to the Appeal Commissioners, rather than any general delay in the procedures for dealing with it in Revenue. It had to be borne in mind that finalising a case for submission to the Appeal Commissioners was not just a matter for Revenue, the taxpayer was also centrally involved both in providing information and in agreeing the AH1. Taxpayers could at any stage appeal directly to the Appeal Commissioners if they felt that there were undue delays within Revenue. However, complaints in relation to delays were very rare.

Since the introduction of self-assessment, all appeals against assessments were effectively 'argument' appeals. The points at issue could range from a disagreement between Revenue and the taxpayer as to the levels of income disclosed in a return to a difference on the interpretation of a statute. In many cases, estimated assessments were raised while an audit was ongoing, usually in the absence of progress on the audit or where a fundamental difference appears that is unlikely to be resolved by agreement. The raising of an assessment may prompt further negotiations or submission of outstanding material. By their nature, such cases were difficult and took time to bring to a stage where they were ready for submission to the Appeal Commissioners. He also indicated that the change in pattern for 2005 cases whereby the 896 cases received was twice the previous annual average and the proportion of cases resolved within 6 months had fallen from 45% to 26% appeared to be related to two large groups of cases (260 and 290 cases) that had appealed on the same grounds.

The Appeal Commissioners indicated that they were unable to comment on specific cases pending the receipt of specific advices in that regard from the Office of the Attorney General.

## Elapsed Case Time within Revenue

Revenue did not see its role in the appeals process as a controlling one but rather, from the Revenue perspective, as a facilitatory role. That view was supported by the fact that taxpayers could appeal directly to the Appeal Commissioners at any stage if they felt that there were undue delays in Revenue. The role was also a pragmatic one in that many appeal cases were settled between Revenue and the taxpayer without recourse to the Appeal Commissioners.

The cases were dealt with by Revenue in accordance with the relevant legislation. Revenue has studied the recommendations of the Law Reform Commission Report on a Fiscal Prosecutor and a Revenue Court with a view to furnishing its observations to the Department of Finance. In the context of the overall implementation of the package of recommendations, Revenue would have no great difficulty with them insofar as they relate to Revenue. Specifically, it would have no difficulty with the recommendation regarding ending Revenue responsibility in the listing of appeals. However, the Accounting Officer pointed out that this was not primarily a matter for Revenue.

The Appeal Commissioners stated that informal discussions had been held with the Institute of Taxation and with Revenue concerning the suggestion that appeals should be addressed directly to the Appeal Commissioners rather than through Revenue. Those discussions would continue but had not yet reached a stage where a recommendation on the suggestion could be made.

## Other Observations from Revenue

The Accounting Officer pointed out that all important cases were sent to the central Appeals Committee, which maintained detailed records and made six-monthly reports to the Revenue Board. Different levels of records were maintained at various local levels. Information on appeals was presently being analysed by the Strategic Planning Division with a view to providing central and local management with appropriate performance reports.

He stated that while the situation in relation to Stops on the central computer system had improved generally since an Internal Audit report in 2003, some instances of delay in removing them still occurred. A listing of Stops older than three months had issued to all District managers in June, and that would be repeated before year end. A computer query facility to enable regions and district to control and monitor Stops more effectively was being explored at present.

## Other Observations from the Appeal Commissioners

The Accounting Officer stated that the timely passage of appeals through the Office was not hindered by a lack of records. While statistics were not available for earlier years, he provided a summary of cases processed for the years 2002 to 2005 as shown in Table 20.

**Table 20**

| Year | Listed | Heard | Taken Off[24] |
|---|---|---|---|
| 2002 | 441 | 314 | 127 |
| 2003 | 325 | 247 | 78 |
| 2004 | 283 | 219 | 64 |
| 2005 | 228 | 178 | 50 |

He reported that determinations had been handed down, or had been listed for announcement before the end of the current term on 31 July, in respect of all cases fully heard to 30 June 2006, where the Office had received all information requested. Between 10 to 15 appeals were received annually directly from taxpayers in cases where Revenue had considered the appeals to be statutorily invalid. As the Appeal Commissioners were not informed by either party or the Court, he had no information on Circuit Court hearings. He also supplied *case stated* statistics i.e. cases referred to the High Court on a point of law as shown in Table 21.

**Table 21**

| Year | Taxpayer | Revenue | Total |
|---|---|---|---|
| **2002** | 3 | 11 | 14 |
| **2003** | 4 | 0 | 4 |
| **2004** | 3 | 10 | 13 |
| **2005** | 4 | 14 | 18 |

With regard to the administration of the Office, a full review of resources, administration systems and staffing requirements had been completed. He was satisfied that a realistic budget had been established for the Office. The underspend arose because of the failure to recruit a suitable candidate for an additional position sanctioned. The website and general IT facilities satisfied current requirements; however, the publication of further selected cases had been delayed by the absence of the additional staff.

[24] Cases taken off were settled by agreement, or relisted

He stated that a number of the recommendations in Figure 2 had been implemented. In addition, the Commissioners had long accepted that an Annual Report should be published but that it awaited the filling of the sanctioned staff position. Other recommendations were premature and needed more detailed examination and wider consultation.

# Chapter 3

## Garda Síochána

# 3.1 Maintenance of Garda Vehicles

## Outsourcing of Garda Vehicle Maintenance

A consultant's report on Transport Maintenance and Procurement Compliance in An Garda Síochána delivered in July 2002 recommended, *inter alia,* that An Garda Síochána "*outsource the entire maintenance activity including management of the fleet, the contracts and costs, quality service performance management and compliance management to a national service provider or consortium.*"

This recommendation was reiterated in the final report of the Garda Strategic Management Initiative Implementation Steering Group in February 2004. The thrust of these recommendations was that better value for money would be achieved through organising vehicle maintenance in this way.

During the course of audit in Spring 2006, I noted that the repair and maintenance of the Garda fleet, apart from vehicles maintained at the Garda transport garage, was arranged at District level and that this work was generally carried out by main dealers in each District. Competitive tendering did not take place for this maintenance work.

I asked the Accounting Officer why the key recommendation regarding the outsourcing of vehicle maintenance had not yet been implemented.

The Accounting Officer informed me that following the reports on Garda Transport in 2002, the understanding was that a contract for the outsourcing of the maintenance of the entire fleet with the exception of some security vehicles would be put in place sometime in 2003. In light of the complexity of outsourcing the Garda fleet of over 2,000 vehicles, as evidenced by the experience of other Police Forces, it was necessary to engage in lengthy discussions involving the Department of Justice, Equality and Law Reform, the consultants who had prepared the report and An Garda Síochána.

Following the consultant's report a process to draft a Request for Tender (RFT) commenced. Due to the ongoing discussions and a variety of technical reasons the RFT was not finalised within the planned timeframe. When all the factors had been considered it was decided that the project would be outsourced using a two-stage process. A pre-qualifying request for information was issued to the market and the responses were currently being evaluated and a RFT would be issued to the qualifying companies shortly.

This project was due to be completed this year and was being undertaken with the expert assistance of consultants.

He added that as the priority of the remaining small cohort of garage staff was to keep the Garda fleet in a roadworthy condition and ensure its maximum operational availability, staff were not available to organise or supervise a maintenance contract.

## Maintenance Arrangements

I asked the Accounting Officer if he was satisfied that the arrangements to source vehicle maintenance with local main dealers without competitive tendering was conducive to getting value for money particularly in the Dublin area where there are a number of main dealers for the marques used by the Gardaí. In this regard, I noted that payments in the range €200,000 to €420,000 had been made to some dealers/maintenance firms in the Dublin area in the two years 2004 – 2005.

The Accounting Officer stated that for the vast number of Districts outside of Dublin and possibly Cork, there was no alternative to using the local main dealer. In the absence of a national contract whereby costs for servicing could be negotiated centrally, the local dealer would know that he was the only one capable of preserving the warranty and ensuring the safety of Garda members and the public. Otherwise

vehicles would be absent from their Districts for long periods involving consequential costs in terms of fuel and time.

He noted that due to the wide geographic spread and the requirement to minimize downtime of Garda vehicles the nearest approved/or main dealers were utilized at a local level. He stated however, that as the average age of vehicle in the fleet was under 4 years, the majority was under warranty at any time and for this reason, it was considered essential that main dealers aligned to the particular manufacturers were used to preserve these warranties. This was the reason main dealers were used for scheduled maintenance and in order to ensure that members of An Garda Síochána could carry out their duties in safety and with confidence.

## Investigation into Alleged Irregularities

In the course of audit, I became aware that an investigation was underway to establish the facts surrounding allegations of irregularity involving a main dealer in Dublin engaged to maintain some of the Garda fleet.

The Accounting Officer informed me that, in February 2006, the Garda Internal Audit Section conducted a preliminary examination of possible irregularities in the servicing and maintenance of a number of Garda vehicles by a contractor. This examination raised suspicions of improper procedures that may or may not amount to criminal behaviour, including

- Overcharging for labour
- Charging for parts not used
- Using non genuine parts
- Causing loss
- Withholding warranty entitlements.

He said that in the course of the preliminary examination no evidence of criminal behaviour by members of An Garda Síochána or civilian support staff allocated to the Garda Transport Section came to light. In addition, no breaches of discipline in respect of members of An Garda Síochána had been identified to date. As a result of the Garda Internal Audit Section examination, the Garda Bureau of Fraud Investigation was requested to carry out a full criminal investigation into the matter. This investigation was ongoing.

# Chapter 4

# Prison Service

# 4.1 Acquisition of Site for Prison Development

The Prison Service is part of the Department of Justice, Equality and Law Reform. Establishment of a statutory board to manage the Prison Service is planned and, in anticipation of the necessary legislation, an Interim Board has been appointed to advise the Minister on the management and administration of the Service. In May 2003, the Capital Sub-Committee of the Interim Board recommended the building of a new prison on a greenfield site in the Dublin area to replace prison facilities at Mountjoy, most of which are in a very sub-standard condition.

The Prison Service asked the Office of Public Works (OPW) to help in finding a site for the prison development. The OPW commissioned property consultants CBRE to carry out a site search and CBRE reported back to the OPW in September 2003, identifying 17 properties. The OPW subsequently refined the search criteria and CBRE reported back again in January 2004. On this occasion, it identified two properties, one at Balbriggan and the second located at Dunboyne, County Meath. The OPW reported the results to the Prison Service which, in turn, kept the Department informed of developments. The OPW informed me that the Department considered the distance of the sites from Dublin to be too great.

In February 2004, the Department decided to advertise for suitable land. The Prison Service placed an advertisement in one of the national newspapers, inviting offers of sites in the greater Dublin area suitable for the development of a secure prison.

In May 2004, the Department decided to set up a Site Selection Committee, comprising officials of the Department, the Prison Service and the OPW, to assess the various site options. The Committee commenced work on 1 July 2004 and, on 16 September 2004, produced a short list of three recommended sites.

CBRE conducted negotiations with the vendors of the three sites, and reported back on the results. The Department decided to purchase a site of just under 100 acres[25] at Coolquay in north County Dublin, at a price of €31.35m (just over €318,000 per acre). However, on 30 November 2004, the Department was informed that the owner of the Coolquay site was not willing to proceed with the sale. On the same day, the Government authorised the purchase of a site subject to the final decision of the Minister as to location.

A farm at Thornton — in the same general area as the Coolquay land — was subsequently offered to the Prison Service. CBRE wrote to the vendors on 13 January 2005 outlining the principal terms under which the Prison Service was prepared to purchase the land. These included a price of €29.9m for the site.

The Site Selection Committee met on 18 January 2005 and agreed to recommend the purchase of the land at Thornton. A binding agreement to purchase the land was signed by the Prison Service on 26 January 2005. Payment for the land was incurred on the Prison Service Vote in 2005.

For ease of reference, key dates and events in the procurement process are set out in Table 22.

[25] The records of the Department/Prison Service and OPW in relation to the site procurement generally use the imperial unit 'acre' in relation to land area, rather than the metric unit 'hectare'. Acres are used in this report to avoid confusion. 1 hectare = 2.47 acres.

**Table 22 Key dates and events in the purchase of lands at Thornton**

| Date | Event |
|---|---|
| **May 2003** | Capital Sub-Committee of Prison Service Interim Board recommends replacement of Mountjoy on a greenfield site in the Dublin area |
| **Sept 2003** | Prison Service asks the Office of Public Works (OPW) to search for a suitable site. The OPW asks CBRE to carry out a search for a site of between 60 and 100 acres, in the greater Dublin area |
| **Sept 2003** | CBRE reports the results of its property search to the OPW, identifying 17 potential sites |
| **Jan 2004** | CBRE makes a second report to the OPW and, as instructed, present two land options of around 80 acres |
| **3 Feb 2004** | Government agrees on announcement by Minister of intention in principle to replace Mountjoy prison complex with a new prison facility on a greenfield site in the greater Dublin area |
| **11 Feb 2004** | Prison Service advertises in Irish Independent for sites of around 100 acres, within 25 kilometres of central Dublin |
| **23 Feb 2004** | Advertised latest date for receipt of offers of sites |
| **1 July 2004** | 1st Meeting of Site Selection Committee — Committee discusses selection criteria |
| **9 July 2004** | 2nd Meeting — Committee agrees site evaluation scheme; carries out preliminary review of site offers |
| **15 July 2004** | 3rd Meeting — Committee evaluates site options and selects six sites for further investigation |
| **31 Aug 2004** | 4th Meeting — The planning and engineering consultants make presentations to the Committee on the specified sites |
| **15 Sept 2004** | Director General of the Prison Service asks Committee to change evaluation criteria |
| **16 Sep 2004** | 5th Meeting — Committee agrees to Director General's request; recommends negotiations commence in respect of three sites |
| **22 Nov 2004** | CBRE writes to Coolquay vendor with draft agreement; the proposed price is €31.35m for just under 100 acres |
| **29 Nov 2004** | 6th Meeting — Committee agrees to recommend the purchase of Coolquay land |
| **30 Nov 2004** | Government approves site purchase |
| **20 Dec 2004** | Thornton site offered to Prison Service |
| **21 Dec 2004** | The solicitor for the vendor of the Coolquay land writes to CBRE formally withdrawing the land |
| **12 Jan 2005** | Prison Service and CBRE representatives meet with Thornton parties and agree a deal |
| **13 Jan 2005** | Written offer to Thornton vendor to purchase 150 acres at a price of €29.9m |
| **18 Jan 2005** | 7th Meeting — Committee agrees the Thornton site is suitable for development of the prison |
| **26 Jan 2005** | Contract for the purchase of Thornton land signed by the State and the vendor |

This examination was undertaken to assess how the identification and evaluation of the site options were managed and whether the procurement process was conducted in a manner that would ensure the State got good value for money. In carrying out the assessment, I sought to establish the market price for land comparable to the land at Thornton at around the same time.

Lisney Limited were contracted to assist in the examination.

# Defining the Site Requirements

In its May 2003 report on the options for the redevelopment or replacement of Mountjoy Prison, the Capital Sub-Committee of the Prison Service Interim Board recommended the building of a replacement 600-place prison on a greenfield site elsewhere in the Dublin area. They concluded that it would be more cost effective and operationally easier and quicker to build a new prison on a greenfield site than to redevelop the existing complex while it was still in use. They also concluded that building a prison on a greenfield site should result in significantly reduced operating costs, and would allow provision of the work training facilities and recreation areas required for a modern prison, but that could not be provided on the constrained Mountjoy site.

The Sub-Committee's report did not specify the kind of land that should be acquired for the prison site, the location of the land (other than that it should be in the Dublin area), or the amount of land required. The requirements for the site in these respects consequently had to be defined as part of the procurement process.

## Type and Location of Land

Under Section 181 of the Planning and Development Act, 2000, certain developments by or on behalf of State authorities are excluded from the application of the planning code in the interests of national security or the administration of justice.[26] As a result, in its search for a site, the Prison Service was not restricted to buying land in urban areas or land zoned for development. Agricultural land that met the Prison Service's requirement was consequently suitable for consideration.

When the OPW commenced the site search on behalf of the Prison Service in September 2003, it asked CBRE to look for sites in the area bounded by Balbriggan to the north, Navan to the northwest, Naas to the southwest and Ashford to the southeast i.e. a boundary zone 25 to 30 kilometres from the centre of Dublin. The scope of the search was to include agricultural land, land zoned for industrial purposes and institutional land. The OPW later refined its instructions to CBRE, asking them to restrict the search to the area north/northwest of the M50.

When the Prison Service advertised for land offers on 11 February 2004, it specified that it was seeking sites within 25 km of Dublin city centre. The Department has stated that this limit was based on an operational assessment that a site further than 25 kilometres was unlikely to be viable as a Dublin prison. The initial assessment of the sites by the Site Selection Committee was carried out on this basis.

In September 2004, the Director General of the Prison Service asked the Site Selection Committee to consider only sites that were within eight kilometres of the M50 motorway — i.e. about 15 to 16 kilometres from Dublin city centre. He was of the view that the M50 would form a primary artery for the transport of prisoners to and from any new prison, and that any location further than eight kilometres from the M50 would present unacceptable operational difficulties.

[26] Part 9 of the Planning and Development Regulations, 2001 provides for notification procedures to be followed by the State authorities concerned, to ensure that the public is consulted on proposed developments of this kind.

The initial searches carried out by the OPW/CBRE identified a number of sites that were already in State ownership. The OPW has stated that it was aware of all large State holdings of land in and around Dublin and had recently assessed these holdings for uses such as affordable housing, sites for asylum seeker centres, etc. Consequently, it was quickly able to confirm to the Site Selection Committee that there were no suitable State-owned sites available.

## Amount of Land Required

The Mountjoy prison complex stands on approximately 20 acres of land in central Dublin.

The OPW's initial instructions to CBRE were to search for a site of between 60 and 100 acres. The instructions were later refined to a site area of around 80 acres, and CBRE reported on this basis in January 2004.

When the Government approved the Minister's proposal to relocate the prison to a greenfield site on 3 February 2004, it asked the Minister to consult with the Minister for Health and Children on the future of the Central Mental Hospital, Dundrum. A review of requirements for replacement of the hospital concluded that around 20 acres would be optimal to meet its requirements.

The Prison Service advertisement on 11 February 2004 specified that it was seeking a site of "circa 100 acres". The Department has stated that this was its estimate of the area of land required to

- provide single cell accommodation and facilities for the number of prisoners currently in the Mountjoy complex (over 900)
- allow for expansion of the prison in the future
- provide a buffer zone around the perimeter sufficiently deep (70-100 metres) to inhibit drugs being projected into the prison and
- provide for the possibility of the Central Mental Hospital being sited adjacent to the new prison facility.

In September 2004, in the light of apparent difficulties in identifying an ideal site, the Director General of the Prison Service indicated that a smaller site, without provision for the Central Mental Hospital or for future expansion, might be acceptable. He did not specify what reduced area might be acceptable, because the topography and the shape of the site would also have to be taken into account.

The Prison Service subsequently bought 150 acres at Thornton, 50 per cent more than the estimated area required.

The Accounting Officer of the Department has stated that the exact size of the site to be purchased depended on a number of variable factors including

- optimum size taking into account the Central Mental Hospital and possible future development
- availability
- cost
- conditions imposed by the vendor
- future use
- resale potential.

He stated that these were dynamic factors that could not all be assessed in advance or in isolation from the actual sites available, but that there was no ambiguity as to the minimum requirement.

## Site Acquisition Budget

The May 2003 report of the Capital Sub-Committee of the Prison Service Interim Board includes an estimate of €10m for the cost of acquiring a greenfield site for the prison development. No details are provided in the report in relation to how this estimate was arrived at (e.g. size of site, cost per acre, location, etc).

The Department/Prison Service did not adopt a budget or affordability limit to guide its site procurement.

The Department has stated that, in the light of the number of variables involved, it was not considered to be of any significant benefit to try and set an artificially established budget for the site before the Committee had completed its work. Based on their extensive experience, the OPW and CBRE were able to advise on general market prices for different types of land which might be suitable for a prison development. The Committee also recognised that they might have to deal with an unwilling vendor because of the proposed end use for the land and that a premium might have to be paid to induce a vendor to sell. The cost of the site was seen as only one factor in the overall project of replacing Mountjoy (and the Central Mental Hospital) by new facilities on a new site. The purchase cost of the site would only have become a critical factor if it threatened the viability of the entire project.

# Disclosing the State's Interest

A prospective purchaser with a special interest in a landholding is faced with the choice of disclosing his interest to potential vendors, or arranging for agents to make discreet approaches on his behalf, without identifying the purchaser's identity or the reasons for the interest in the property.

Many developers of land choose to acquire property discreetly, even when the land may be openly for sale. The primary reason for not publicly disclosing an interest is that vendors may be able to identify why their land would be of special interest for the developer, thereby identifying him as a special purchaser who would be expected to pay a significant premium over the market price, particularly where the owner of the land may need to be induced to sell.

The OPW has stated that it advised the Department and the Prison Service that, to acquire the necessary land at the lowest possible price, it would be best to proceed confidentially, using a third party agent who would not publicise the fact that the State was the ultimate purchaser. This was on the grounds that any public announcement of the State's interest in acquiring land had the potential to drive up the asking price.

The Accounting Officer of the Department acknowledges that the confidential third party strategy might have resulted in a lower price, but rejected it for a number of reasons.

- The Prison Service was not convinced that this strategy would produce a broad enough range of sites that might be suitable. The Department considers that this view was confirmed by the fact that the advertisement resulted in a number of sites being offered that would not otherwise have been identified.
- The Prison Service was concerned that the third party approach did not comply with best practice for acquiring a site for a major prison development as it was not open and transparent, that it could give rise to allegations that political influence or corruption dictated the choice of site and that therefore it would be difficult to justify such a strategy to the Government or the Public Accounts Committee.
- Because of the size of the purchase and the need for in depth assessments and surveys prior to purchase, the Prison Service had real doubts as to whether it would be possible in practice to close a contract without the vendor becoming aware of the identity of the purchaser.

The Accounting Officer of the Department has stated that the cost of any premium paid above farmland prices should be weighed against the monetary and non-monetary benefits of inviting expressions of interest by public advertisement. He has also stated that the Department did not seek professional advice on the potential impact that advertising its interest in acquiring land would have on the price it would be likely to have to pay. He pointed out that the advertisement seeking offers of sites was intended also to provide some indication of the prices being sought for the type of land that might be suitable for a major prison development. However, these asking prices would be expected to already include a special purchaser premium, and so would be difficult to interpret without corresponding market value amounts.

The Accounting Officer of OPW has stated that he accepts that the approach taken by the Prison Service was reasonable. He has also pointed out that a Part 9 planning application following a confidential purchase would have the effect of conferring on the State, and on no one else, the ability to develop the land. He raised the question of whether the State should use this procedure to confer on itself planning gain and increased value after having paid a much lower price for land on the basis that it had no developmental potential.

# Hiring of Advisors

Central government departments and offices must comply with EU Procurement Directives in acquiring professional services, including those of consultants. The Directives require that, where proposed public sector contracts for services are expected to exceed certain threshold values, they must be advertised in the Official Journal of the EU. In 2004 and 2005, the relevant threshold for services procurement was €154,014 (excluding VAT).

In addition to the EU Directives, the Department of Finance publishes guidelines setting out best practice principles and guidance for engaging and managing consultants. These include requirements to seek competitive tenders from a number of service providers, to agree fixed fees for specified services, and to formally review the work done by consultants prior to final payment.

Based on the EU and Finance rules and guidelines, OPW has established a Consultants Selection Committee that considers requests for the appointment of consultants for construction projects. This Committee is also responsible for reviewing the terms of engagement of consultants and their fee levels.

OPW asked CBRE to become involved in the site search around the middle of 2003. There was no tendering for the service and no formal contract. Despite carrying out searches and producing two reports, it was only in May 2004 that CBRE formally wrote to OPW, setting out its fees for proposed professional services required to complete the site acquisition. This was prior to the decision of the Department to set up the Site Selection Committee.

CBRE's cost proposals included fees in respect of site selection study, site inspection and site acquisition negotiations; engineering studies of services, roads and site conditions; and studies of planning issues. CBRE indicated that they planned to sub-contract the engineering and planning studies to named firms of consulting engineers and consulting planners.

When CBRE made its fee proposal to OPW, it was envisaged that only three sites would be assessed as proposed. Consequently, the total fee proposal for the consultancy services was €184,500 (plus VAT and expenses).

By the time the process was completed, ten sites had been assessed by the consultant engineers and planners. As a result, the amount paid to CBRE in connection with the prison site acquisition was €256,506 (plus VAT of €53,866).

The manner in which OPW contracted with CBRE for the provision of professional services for the site selection and procurement did not comply with the rules for procurement of professional services in a number of respects.

- The requirement for professional services was not advertised in the Official Journal, even though the total amount paid exceeded the advertising threshold.
- There was no competitive tendering for the professional services' contract.
- OPW's Consultants Selection Committee was not asked to assist in selecting and engaging the service providers.
- OPW did not have a specific written contract with CBRE, which militates against the assessment of service delivery and the determination of the amount payable for those services.

In response to my enquiries relating to advertising and competitive tendering, the Accounting Officer informed me that judgments have to be made on a case-by-case basis on the known facts at the time. The Accounting Officer did not believe that it was necessary that the requirement for professional services should have been advertised in the Official Journal. He said the initial input by CBRE had been on the basis of their carrying out a confidential search for sites. CBRE had already done work for the Prison Service, had been aware of the issues involved and had recent relevant experience.

He also said that, in the case of the prison site, OPW's initial approach had been to acquire the site discreetly. The estimated cost of this service was below the EU advertising threshold. Furthermore, as it was at the time intended to keep confidential the ultimate use of any property acquired, it would not have made sense to have a public procurement for the appointment of professional advisors. When it was decided to adopt a more transparent process, OPW felt that tendering for a new agent at that point would have led to delays and given rise to an unnecessary duplication of effort and cost.

He said that a different approach is taken for property consultants and estate agents than for external consultants required for OPW building and engineering activities. While a list of suitable firms is drawn up on the basis of public advertisements for property consultancy services, OPW reserves the right in the public interest to make appointments from outside the list in specific instances or in circumstances when a special expertise is required or for reasons of confidentiality where the interest of the State should be kept confidential for a period.

He said that the initial approach of the OPW to this case — that the State's interest and purpose of the acquisition be kept secret — was, along with CBRE's relevant recent experience, one of the reasons why a confidential appointment had been made.

In the matter of a contract with CBRE, the Accounting Officer said that the contract was founded upon an exchange of emails between the two parties.

Finally, the Accounting Officer believed that the ongoing oversight and review of the firm's performance by both OPW and the Committee constituted normal and adequate oversight and monitoring.

# Evaluation of Site Options

The Prison Service's advertisement asked for offers of sites to be submitted by 23 February 2004. However, this wasn't treated as a fixed closing date (as would be the normal case in a competitive tendering process) and offers received after the specified date were not excluded from consideration. Land purchases are not covered by EU procurement rules, so it was appropriate for the Prison Service to consider offers as they arose, in the interests of maximising competition among potential vendors.

## Initial Evaluation

By the end of April 2004, the Prison Service had received a total of 28 offers in response to the advertisement. A further three potentially interesting sites were identified by OPW/CBRE through their search work. The OPW and CBRE assessed all the sites, and produced a short list of three, drawn from those sites which conformed in size and location to what was required. The basis on which the short list was arrived at is not clear. OPW reported to the Department on the short-listing on 20 May 2004.

Given the very significant financial and operational implications for the Prison Service of the site selection, the Department was strongly of the view that the site options needed to be rigorously evaluated in an objective way by people with expertise and experience in all the relevant areas. Because OPW and CBRE did not have the full range of necessary experience and expertise, the Department decided on 27 May 2004 to establish a Site Selection Committee to carry out the evaluation and to record the basis on which the site selection recommendations were made.

## Evaluation Criteria

The Site Selection Committee held its first meeting on 1 July 2004, and discussed a site evaluation scheme. Eight evaluation criteria were proposed including cost per acre, general location and accessibility of the site, and shape and size of site. With some minor amendments, the scheme was agreed at the Committee's second meeting on 9 July 2004.

After receiving a letter from the Director General of the Prison Service, the Site Selection Committee revisited the evaluation criteria on 16 September 2004. They decided to drop cost per acre from the evaluation scheme and reallocated the associated marks to the criteria relating to general location and shape/size. Evaluation of sites on and after that date was based on the revised scheme. Sites eliminated from consideration earlier on cost grounds were then reviewed, and some were evaluated against the revised evaluation scheme. Sites eliminated earlier on other grounds were not re-evaluated. Table 23 sets out the evaluation criteria, and indicates the weights assigned to each.

**Table 23 Evaluation criteria and weightings used in site selection process**

| Evaluation criterion | Original scheme (9 Jul to 31 Aug 2004) | | Revised scheme (16 Sep 2004 to 18 Jan 2005) | |
|---|---|---|---|---|
| | Maximum mark | Percentage weight | Maximum mark | Percentage weight |
| Cost per acre | 80 | 16% | — | — |
| General location /accessibility vis a vis Courts, other prisons, etc. | 60 | 12% | 100 | 20% |
| Proximity to public transport links | 80 | 16% | 80 | 16% |
| Availability of emergency services (Fire/Garda/ hospitals) | 15 | 3% | 15 | 3% |
| Access/egress options | 65 | 13% | 65 | 13% |
| Shape, size, topography of site | 100 | 20% | 140 | 28% |
| Availability of services, power, sewerage, etc. | 40 | 8% | 40 | 8% |
| Planning/community impact | 60 | 12% | 60 | 12% |
| **Total** | **500** | **100%** | **500** | **100%** |

## Consistency of Evaluation

The Site Selection Committee agreed that sites would have to score a minimum of 40% of the total available marks on all criteria to avoid elimination from consideration.

The Committee eliminated most of the site options on a consensus basis, without assigning evaluation scores, judging them to have failed on at least one of the evaluation criteria. It assigned scores for a total of 13 sites against the evaluation criteria at its meetings on 15 July 2004 (8 sites), 16 September 2004 (4 sites and revision of one site scored earlier) and 18 January 2005 (1 site — Thornton).

The Committee did not record the basis on which scores were awarded to individual sites under the various criteria, even though the criteria were generally amenable to technical analysis and quantification e.g. distance from the centre of Dublin, proximity of public transport services, call out time for availability of emergency services, aggregate estimated cost for provision of services and road improvements, etc. How the information provided by the engineering and planning consultants impacted on the decision making about site selection is also not clear.

Because the basis of the scoring is not recorded, it is difficult to establish whether or not the evaluation of the sites was consistent. For the purposes of this examination, the evaluation scores awarded by the Committee to four of the sites were compared to assess their consistency. To allow comparison between sites marked under the original and revised schemes, the marks awarded by the Committee under each criterion were expressed as percentages of the relevant maximum marks.

The four sites were selected because they were all located relatively near one another, and on or near the N2 national primary road. The sites were

- the Open Golf Centre, located between the M50 motorway and Dublin airport — this site received the highest score of all the sites evaluated by the Committee, but the site offer was withdrawn by the vendor in August 2004
- a site at Bullstown, just inside the County Meath border, and which was eliminated from further consideration by the Committee on 31 August 2004
- the site at Coolquay, which the State offered to buy in November 2004
- the Thornton site which the State ultimately bought.

It should be noted that the sites were not re-evaluated as part of this exercise. The objective was to establish whether or not the relative evaluation marks were consistent, not to identify what the 'correct' marks would have been.

There are a number of respects in which the marks awarded by the Site Selection Committee appear to be inconsistent. For example

- The respective distances by road from the sites to the junction of the M50/N2 (and to the centre of Dublin) do not appear to be reflected proportionately in the marks awarded under the general location/accessibility criterion.
- Sites served by the same public bus service got different marks in relation to proximity to public transport; and a site not served by any direct bus service got the same mark as a site that was served by a public bus service.
- One site got a significantly lower mark than two others in respect of availability of site services, even though the consultants estimated that the cost of provision of water, sewerage and energy services would be higher at the other sites.

The Accounting Officer of the Department has stated that he does not accept that the use of percentages makes for a valid comparison when different weightings were used and a completely new assessment has been carried out. He stated that the priority was to ensure that each assessment process was internally consistent to ensure a valid comparison could be made between the sites in contention.

## Evaluation of Cost

The original evaluation scheme drawn up by the Committee included cost per acre as a criterion, but with a low weighting (16% of the total available score). This created the risk that even very significant differences in cost per acre between site offers might be outweighed by relatively small differences in site characteristics.

The removal of the cost per acre criterion from the scoring system in September 2004 potentially allowed sites to be compared on their respective merits and a relative rank order of the sites on offer to be established. However, some test of the relationship between costs and benefits was then needed to bring cost back into consideration in the site selection process if good value was to be achieved.

The Committee recommended that price negotiations should commence with the vendors of three sites ranked highest in the evaluation carried out on 16 September 2004. Cost wasn't considered at that stage — the Department/Prison Service decided to postpone consideration of cost until actual land prices emerged in negotiations with vendors. However, this resulted in negotiations being opened only on sites where high prices had been sought initially by the vendors.

Better value for money might have been achieved if the Department/Prison Service had looked at all the sites that exceeded the specified minimum score levels during the full evaluation process, and weighed up whether or not the perceived extra benefits of more expensive sites were worth the additional costs. Options for improving the suitability of the less expensive sites should also have been considered e.g. securing small adjoining properties to regularise overall site configuration.

The OPW has stated that the Site Selection Committee felt strongly that the capital cost of the site was but one element in the overall value equation to be considered for the new prison. It said the Committee considered it vital to obtain the best-configured site so as not to compromise the form of what would be a major State institution with an operating life of probably 150 years. It was the Committee's strongly held view that any layout flaw in the new prison caused by a less than ideal site would cost multiples of the initial site price in lost operating efficiencies over the long life of the prison.

# Valuation of Sites

Having publicly advertised its interest, the State had declared its position as a purchaser with a 'special interest'. Negotiating a successful procurement in these circumstances demanded, at a minimum, that the State agencies maintain competition and equip themselves with key information in the form of a valuation report.

The Department and the OPW have stated that, while they did not seek valuation reports on the properties under negotiation, they comprehensively discussed with CBRE the likely market valuation range for the sites of interest. They recognised that the prices proposed by the vendors would be likely to exceed the respective market valuations by the 'special purchaser' premium that attached to the sale. The advice of CBRE on the likely valuation range for sites of interest to the Prison Service was not recorded at the time.

## Analysis of Land Values

The market value of land is the price it is likely to achieve in an open sale, where the vendor initiates the sale. In such circumstances, the price achieved will usually reflect the productive capacity of the land (and

of any associated buildings) and any generally perceived 'hope value' deriving from the development potential of the land e.g. related to proximity to towns or developing areas, infrastructure, zoning plans, etc.

At the time of its purchase, the main characteristics of the Thornton land relevant to its market value were

- it was a large landholding (150 acres)
- the land was zoned agricultural, but included a small element of 'RC' zoned land[27]
- it was situated in a mainly rural setting (the nearest urban centre — Swords — is about 5 kilometres away, via local roads)
- there was no access to mains drainage nearby
- the land was located 1.6 kilometres from the N2 and had direct access to regional and local roads only
- the site was not served by public transport.

A survey of auction results in 2004/2005 for large holdings of agricultural land in the north Dublin and east Meath areas indicates that the prices achieved were in the region of €20,000 to €30,000 per acre. Table 24 sets out a sample of these auction results.

**Table 24 Prices paid for agricultural land in north Dublin and east Meath, November 2004-October 2005**

| Address | Size (acres) | Price per acre | Total price |
|---|---|---|---|
| Ballyboughill, County Dublin | 86 | €29,766 | €2,560,000 |
| Garristown, County Dublin | 102 | €30,293 | €3,090,000 |
| The Naul, County Dublin | 109 | €19,265 | €2,100,000 |
| Ratoath, County Meath | 238 | €26,050 | €6,200,000 |

The degree of developmental potential that might attach to any particular parcel of land, like Thornton, is difficult to assess. Within the north County Dublin area, higher prices have been paid for large parcels of agricultural land, reflecting different degrees of development potential. For example, €68,000 per acre was paid for 73 acres of agricultural land at Turvey, County Dublin, adjacent to the M1 — this land was later zoned industrial.

In areas undergoing large scale urban development, unzoned land can attract much higher prices. For instance

- €191,000 per acre was paid for 115 acres of unzoned land at Adamstown, County Dublin, which is an area intended for significant new town expansion under agreed action area plans
- €400,000 per acre was paid for 96 acres of unzoned land at Tyrrellstown, County Dublin, which is an area undergoing significant residential development.

The Accounting Officer of the OPW has stated that knowledge of the demographic pressure on the greater Dublin area and a study of the map of north County Dublin and the relative positions of settlements and road networks would confirm that development is likely to reach the Thornton area in the future. His view is that, in assessing its value, a vendor would assign a 'hope value' to such a holding on the basis that it was only a matter of time before development would be permitted, particularly at a stage when development plans in the greater Dublin area were being revised. He stated that the Site Selection

[27] Land zoned RC in the Fingal Development Plan 2005-2011 is so designated to protect residential amenity and the character of settlement clusters and to provide for small scale infill development to serve local needs

Committee took the long view of the value issue into consideration in the context of the probable 150-year life of the proposed new prison and its place in an expanding city.

Subsequent to the agreement to purchase the land at Thornton, CBRE wrote to the Prison Service on 3 February 2005 stating that "*As (we) mentioned to you from the outset, the land being purchased in the Fingal county area by developers speculating on land with the hope of getting those lands rezoned in future development plans, trade at anything from €75,000 to €100,000 per acre.*"

CBRE attributed the balance of the cost to the fact that, because the public advertisement of the Prison Service requirements meant that potential vendors knew the identity of the purchaser, there was always going to be a premium price placed on properties being offered for sale by the vendors. This premium, in their opinion was *" … purely down to the 'fall-out' factor being identified by vendors for the stigma attached of being the vendor of the property for the prison in their locality.*"

Ultimately, the price paid by the Prison Service for the Thornton land — around €200,000 per acre — was at least twice the market price at the time for well-positioned agricultural land with development potential in the target area in north County Dublin. While it is acknowledged that the hope value attached to any particular holding may vary according to the subjective assessments of the parties on the prospect and nature of future development, it is likely that the main factor giving rise to the differential between the price paid for the Thornton land and the going rate for similar land in the area was public knowledge of the State as the purchaser and the premium associated with that status.

# Negotiation of Purchase

Negotiations with the prospective vendors were conducted on behalf of the State by CBRE, with some involvement of officials of the Prison Service.

There is no official record indicating that the Department/Prison Service and/or the OPW clearly specified to CBRE what the negotiation strategy should be, what the spending limit was or what conditions were to be applied to protect the State's interest. The only evidence of a negotiating mandate is contained in two letters from CBRE to the OPW and the Prison Service on 11 and 22 November 2004, putting on the record the main elements of the proposed State offer to buy the land at Coolquay.

No similar record exists in relation to the State's offer to buy the land at Thornton. However, the cost limit set for the Coolquay offer (i.e. up to €31.5m, as noted by CBRE in their letter of 22 November 2004) may have been treated by the Prison Service as setting the limit of what could be spent in relation to Thornton.

It is noted that the initial approach from the Thornton vendor's agent proposed a price of €210,000 per acre, implying a total asking price of €31.5m for the 150 acres on offer.

## Level of Competition

In late September 2004, negotiations commenced with the vendors of three shortlisted sites. These were located at

- Coolquay, County Dublin
- Sillogue, County Dublin, and
- Clonee, County Meath.

However, when the Committee met on 29 November 2004, it was told that the cost of one site had escalated to circa €500,000 per acre, and that the owner of another site was "not open to realistic discussions in relation to cost". Therefore, it had become apparent to CBRE, the Department/Prison

Service and OPW that only the remaining option (Coolquay) was a realistic prospect. By the time the Thornton land came into play, that was also the only realistic prospect.

In effect, the State twice ended up negotiating a sale with single vendors, with no effective degree of competition. While the vendors may or may not have been aware of this, the lack of competition weakened the State's negotiating position. The lack of apparent alternative deals on offer may have created a fear on the part of the State agencies that other, better offers were unlikely to emerge.

## Disclosure of Connection

On 10 January 2005, the OPW was informed in a telephone conversation with the CBRE representative that he had discovered that he had a distant connection through marriage to the vendor of the Thornton site. Prison Service officials state they were also informed on that date.

The OPW record includes a copy of a CBRE file note written by CBRE's representative dated 12 January 2005. The note states that

- The CBRE representative had only become aware of the connection to the vendor on 10 January 2005.
- On 12 January 2005, OPW gave him approval to negotiate to purchase the property subject to title, contract, Ministerial approval and Cabinet approval on the basis that the approval should be forthcoming given the comparisons with the Coolquay property.
- The CBRE representative, along with two officials from the Prison Service met the Thornton vendor on 12 January 2005 to discuss the possible sale of the land to the State.

The OPW stated that, following the disclosure of the connection, it invoked its internal procedures in relation to declarations of interest or connection in this case. The CBRE representative offered to withdraw from negotiations but the OPW declined the offer, judging that the connection was at a sufficient remove and the process would be damaged more by the withdrawal of the CBRE representative.

# Pre-acquisition Procedures

At the time of its offers to buy land at Coolquay and Thornton, the State had not completed certain procedures.

- Comprehensive site surveys, which would have taken some months to complete, had not been carried out on either property prior to the purchase offers. In these circumstances, offers to buy are normally made conditional on comprehensive site surveys being carried out.
- There was no comprehensive costing in either case of the work that would be necessary after acquisition to enable the site to be used for a secure prison. For example the cost of road widening to serve the Thornton land was not assessed and, in the case of the Coolquay land, the cost of dealing with a recognised site flooding problem was not assessed.

The OPW Accounting Officer has stated that the professional advisors supplied surveys which included all the relevant information and costings required to make a decision on acquisition, and that the successful completion of the Thornton sale demonstrated that no deal breaking issue emerged. He also stated that risks associated with sites and post-acquisition costs were discussed by the Committee prior to offers to vendors being made.

The Accounting Officer of the Department informed me that, although not ruling out the option that the road might be widened in the future, the existing width of the R130 road from the N2 to the Thornton site was assessed as being perfectly adequate.

# Completion of Purchase

Following the recommendation of the Thornton site by the Site Selection Committee on 18 January 2005, the Prison Service and the Chief State Solicitor's Office examined title, clarified with the vendor the exact boundaries of the site and prepared a contract for signature. A memorandum for information was prepared for the Government meeting on 26 January 2005, at which the proposed purchase was noted. Department of Finance sanction for the purchase was issued on the same day and the contract for the purchase was signed that afternoon. Ten per cent of the purchase price of €29.9m was payable on signing the contract, with the balance due on closing on 1 October 2005.

# Conclusions

The evaluation criteria adopted by the Site Selection Committee, set up to carry out an objective assessment of the sites on offer and to record the basis on which site selection recommendations were made, were relevant to the site selection. However, the available records do not provide sufficient information about the basis for the Committee's assessments, and there are some apparent inconsistencies in its evaluations.

The overarching factor in the high cost of the purchase was the decision to disclose the State's interest in acquiring a site for a prison. This identified the State as a special purchaser with the attendant financial implications for the Exchequer. The fact that the target location was land to the north/north-west of Dublin City, within a reasonable distance of the M50, meant that the asking price for the land would also include an element of hope value, regardless of its current zoning for planning purposes.

OPW initially favoured a confidential approach. The Department, while recognising that a third party strategy might have resulted in a lower site cost, considered that, in principle, the purchase should be open and transparent and that, by publicly disclosing its interest, it would attract a wide range of potentially suitable sites, especially lands not even contemplated for sale by their owners hitherto. The Department also considered that, on a pragmatic level, it might be difficult to close a sale without the vendor becoming aware of the identity of the prospective purchaser in light of the in-depth assessments and surveys that would be needed prior to purchase.

OPW accepted the reasonableness of the Department's decision to disclose its interest and the proposed end-use. It was conscious of the possible implications of the State using a special procedure in the planning law to confer a monetary gain on itself.

Considerable effort was expended in trying to identify and evaluate sites for the new prison. However, identification rounds by the OPW and the invitation of expressions of interest by way of public advertisement did not directly contribute to making available a property that was suitable in all respects for the stated purpose at an acceptable price. One consequence of the process undertaken was the determination of a price, €31.5m, that the Department was willing to pay for the Coolquay site – a purchase which fell through. Subsequently, as a result of a third party contact, the site at Thornton became available for sale at the same price. Ultimately, the Department purchased this site for €29.9m.

The procurement arrangements and, in particular, the use of a public advertisement did not position the State to acquire the land at the lowest cost economically achievable. However, once that approach had been adopted, it was important to have an element of competition in order to try to mitigate upward cost drift. In the event, no real competition on price materialised. Twice during the acquisition process, the State was left negotiating a price with only one potential vendor. This weak negotiating position was not conducive to achieving value for money.

The Prison Service had the freedom under planning law to use agricultural land for development of the prison facilities. The price paid for the site at Thornton is likely to have been at least twice the market price at the time for well-positioned agricultural land with development potential in the target area in

north county Dublin. In the circumstances, a well-managed, confidential, third party approach might have allowed the Prison Service to procure suitable land at a much lower price than was paid for the land at Thornton.

The area of land acquired was also greater than that sought by the Prison Service to meet its needs and those of a relocated Central Mental Hospital. While the larger site affords the opportunity for future expansion without further land acquisition, the fact that the land was purchased at a price substantially more than the market price of similar lands calls into question the value obtained from the enlarged acreage.

The purchase of this site raises the question as to whether there is a need for greater consistency in the land acquisition procedures employed by the State for public good projects. In this respect, it is worth noting that under Compulsory Purchase Order mechanisms, prices paid for land required for public infrastructure development are based on market value, while under the mechanism employed in acquiring land for an essential structure like a prison, a considerable premium was paid by the State.

# General Views of the Department

The Accounting Officer of the Department, while accepting that in many cases a third party approach may result in the best value for money, has pointed out that the moral and strategic imperatives in the purchase of a site for the most significant prison development in the history of the State imposed special and unique demands. A deliberate and principled decision was taken not to use a third party approach for the purchase of the site both for the practical reasons already outlined but also for ethical reasons particularly where local opposition might be aggravated and the vendor forced to leave the area. He is satisfied that in the particular circumstances, it would not have been possible to obtain a site as suitable as Thornton for any less than was paid. This view is reinforced by the fact that to the best of the Accounting Officer's knowledge no comparable sites closer to Dublin have been sold in the recent past for an amount per acre less than was paid for Thornton.

# Chapter 5

# Department of Environment, Heritage and Local Government

# 5.1 Landfill Targets

Biodegradable municipal waste (BMW) is waste that is capable of undergoing decomposition over time through natural processes. It comprises household waste as well as commercial and other waste which, because of its nature or composition, is similar to waste from households. It is typically made up of organic waste such as food and garden material, together with other biodegradable materials such as paper and cardboard, wood and textiles.

## State Obligations

The 1999 EU Landfill Directive[28] imposed obligations on Member States in relation to Waste Management. The principal obligations imposed by the Directive include the requirement to

- progressively reduce the level of BMW disposed of by landfill in stages up to 2016
- publish a national strategy on waste management.

Ireland was required to bring into force, by July 2001, laws, regulations and administrative acts to give effect to the Directive. The Waste Management (Amendment) Act, 2001 was passed on foot of this obligation. Over the years the Department of Environment, Heritage and Local Government introduced a number of regulations to deal with aspects of the Directive – these were consolidated in 2004.

## National Policy

The Department has issued a number of policy documents in recent years to address the waste issue, the first being *Waste Management-Changing Our Ways* published in 1998. This document set out national targets for municipal waste recycling and biological treatment, to be achieved over a fifteen year time period. These are the targets that are used by the Department when benchmarking progress.

The 1999 Directive required the submission of a national strategy on BMW to the EU by July 2003. The National Strategy on Biodegradable Waste was published by the Department in April 2006. The Strategy describes a range of measures designed to enable the State to meet the landfill diversion targets as set out in the 1999 Directive.

## Implementation of Measures

The Waste Framework Directive of 1975 established the requirement for waste planning, licences for carriers and the polluter pays principle. On foot of obligations deriving from the Directive, waste management plans were prepared by each of the local authorities. The Waste Management Act, 1996 required local authorities to produce waste management plans either individually or jointly with other authorities. Subsequently, seven regions evolved, each representing a number of local authorities. Each of the seven regions produced a waste management plan for their areas, apart from three local authorities which prepared individual plans. In 2005 the regions published their second round of plans, generally for a five-year period up to 2009 or 2010. A Policy Statement produced by the Department in 1998 was based on an internationally adopted hierarchy of options for dealing with waste management. These options were, in order, prevention, minimisation, reuse, recycling, energy recovery and disposal. According to the Department's Overview Report on Waste Management Plans, published in 2004, the options chosen by local authorities in their waste management plans were recycling, thermal treatment and landfill, with recycling being the most favoured option.

[28] Council Directive 1999/31/EC

Recycling is facilitated by segregated household collection, bring banks, civic amenity sites, materials recovery facilities or transfer stations and biological treatment facilities. The provision of biological treatment facilities, which would deal with organic waste, is only at proposal stage in local authorities in all but two of the regions. However, increasing numbers of private sector facilities are coming on stream with others at the planning and development stages.

Although progress is evident in recycling some items of municipal waste such as glass and ferrous metals there is not the same success with BMW. A high proportion of organic materials and textiles are still being sent to landfill.

# Reporting Progress

An EU Waste Statistics Regulation came into force in December 2002, with an obligation on the State to report on the 2004 data by June 2006. This will require greater harmonisation of waste statistics. The State has an option to apply for a derogation from this 2006 reporting date in relation to certain waste categories.

At national level the Environmental Protection Agency (EPA) is responsible for the collection and reporting of national statistics on the generation and management of waste. Since 2001 it has published information in relation to BMW. The information is based on an annual collection of data from local authorities and waste licence permit holders, using questionnaires.

A report by the Department[29] noted that local authority waste management plans highlighted the lack of consistent, reliable information on waste generation within the regions and that different approaches to data and statistics have been taken in the plans with the use of a variety of data estimation and presentation practices. Some plans used target rates or quantities, others expressed targets in terms of increases in the rates or quantities recovered or recycled, while targets were expressed in other plans in terms of decreases in the rates or amounts of waste to be managed in other ways (e.g. landfill). It also noted that the target achievement dates varied between plans and ranged from 2004 up to 2013.

A report published by Forfás[30] advocated greater co-ordination in the implementation of waste management plans and more effective national and regional co-operation in order to achieve an integrated network of waste management facilities.

The EPA recommended in its 2004 report that waste data should be supported by audits and other verification exercises by local authorities in order to enhance the credibility of the data, and that the development of waste information management systems at local and national levels should be actively supported.

# Targets for Reducing Landfilled Biodegradable Municipal Waste

The reduction in the amount that could be sent to landfill under the 1999 Directive was set by reference to the total amount by weight of BMW generated in 1995. The maximum amount that could be sent to landfill was to be no higher than the following percentages of the 1995 level

- 75% by July 2006
- 50% by July 2009
- 35% by July 2016

[29] Waste Management; Taking Stock and Moving Forward, April 2004
[30] Key Waste Management Issues in Ireland, July 2003

The 1995 baseline figure for BMW generated was agreed between the EPA and the Department at just under 1.3m tonnes. This figure was arrived at after taking account of information and knowledge accumulated by the Agency since original 1995 data was compiled and was included in the Agency's National Waste Report 2004 which was published in 2006.

The 1999 Directive allows Member States which consigned more than 80% of collected municipal waste to landfill to postpone achievement of these targets by a period not exceeding four years. According to the *National Waste Database Report 1995* Ireland consigned some 92% of municipal waste to landfill in that year. The European Commission was formally notified by letter of 22 December 2005 that the National Strategy on Biodegradable Waste will be based on a first phase target date of 2010 (deferred from 2006) and a second phase target date of 2013 (deferred from 2009), with the stated intention that the Irish authorities are strongly committed to achieving the targets at the earliest possible dates and that efforts will focus on achieving the necessary BMW diversion from landfill in advance of these revised target dates.

The National Strategy also states that Ireland will review the position in relation to the available four-year derogation from 2016 to 2020 and will come to an informed decision on the prospects for achievement of the third phase diversion targets as soon as practicable.

# Current Performance on Diversion from Landfill

The biodegradable element of municipal waste was first itemised separately in the EPA's 2001 National Database Report. BMW is categorised under the headings of wood, paper and cardboard, organics and textiles.

In 2004, the latest year for which statistics are available, some 1.3m tonnes of BMW was still being disposed of by landfill. The total amount of BMW being produced was over 1.9m tonnes.

When this production is broken down by category the position is set out in Table 25.

**Table 25 Biodegradable Municipal Waste Managed in 2004[31]**

| Category of Waste | Tonnes Managed | Tonnes Landfilled | Tonnes Recovered | % Landfilled |
|---|---|---|---|---|
| Wood | 175,330 | 14,180 | 161,150 | 8.1 |
| Paper and Cardboard | 821,903 | 446,306 | 375,597 | 54.3 |
| Organics | 780,460 | 696,955 | 83,505 | 89.3 |
| Textiles | 157,521 | 146,986 | 10,535 | 93.3 |
| **Total** | **1,935,214** | **1,304,427** | **630,787** | **67.4** |

Waste recovered in 2004 was diverted from landfill mainly through recycling and other recovery operations. This was implemented through separate collections of mixed dry recyclables via kerbside schemes and organic waste, together with dry recyclables collected through bring facilities.

[31] Source: EPA National Waste Report 2004

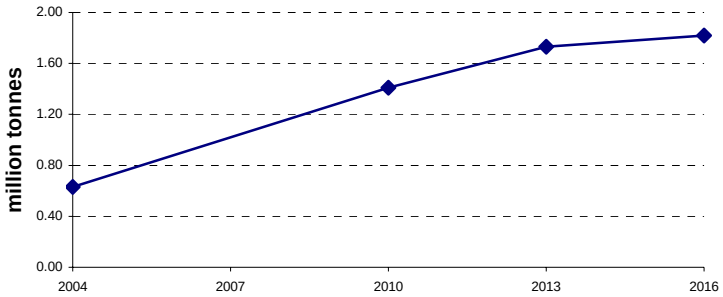
Two major trends are apparent in the management of BMW in recent years

- The overall amount produced has grown significantly since 1995 and is continuing to grow – up from 1.5m tonnes in 2001 to 1.9m tonnes in 2004. This upward trend over the period has been ascribed to population growth and increased economic activity.
- There have been some inroads into reducing the proportion sent to landfill. By 2004, 67% was going to landfill compared with 85% in 2001. However, in absolute terms slightly more was being landfilled in 2004 than in 1995.

# Diversion Required to Meet Targets

Notwithstanding the reduction in the percentage of BMW going to landfill it has been estimated that, taking account of the expected growth in the BMW production, the amount diverted from landfill would need to increase as set out in Figure 3

**Figure 3 Diversion necessary to meet targets[32/33]**




# Audit Concerns

While the overall percentage of BMW going to landfill has been reducing the volume going to landfill has continued to increase in the period 1995 to 2004. It would appear, therefore, that there is a significant risk that Ireland will fail to meet the targets set down in the Landfill Directive. In the light of the possibility of EU financial penalties arising from any such failure, I sought the views of the Accounting Officer on the effectiveness of the measures taken to date and on the action proposed to meet the specified targets.

# Accounting Officer's Response

The Accounting Officer informed me that he is confident that the National Strategy on Biodegradable Waste forms a credible basis for the achievement of the landfill diversion targets. The Draft National Strategy on Biodegradable Waste was subjected to a public consultation process under which submissions were received from many key stakeholders. These submissions facilitated the preparation of a more informed, robust and coherent Strategy, which should have high levels of support from stakeholders. The published strategy forms a comprehensive programme of measures and actions which is designed to comply with the Landfill Diversion targets as contained in the Landfill Directive.

[32] Source: National Strategy on Biodegradable Waste.
[33] These projections are based on a derogation of four years for the 2006 and 2009 targets.

He pointed out that considerable progress had already been made on the management of BMW between 1995 and 2004. Almost 33% of waste was recycled in 2004 compared with 11% in 1995. This is shown in Table 26

**Table 26– Biodegradable Municipal Waste Recycled 1995, 2001 - 2004**

| Year | Gross Quantity Available Tonnes | Landfill Tonnes | Recycled Tonnes | % Rate |
|---|---|---|---|---|
| 1995 | 1,289,911 | 1,147,320 | 142,591 | 11.1 |
| 2001 | 1,525,315 | 1,291,464 | 233,852 | 15.3 |
| 2002 | 1,727,490 | 1,365,628 | 361,862 | 20.9 |
| 2003 | 1,855,505 | 1,317,560 | 537,944 | 29.0 |
| 2004 | 1,935,214 | 1,304,426 | 630,788 | 32.6 |

He also outlined the measures which are proposed within the Strategy, in addition to those in operation in 2004, in order to facilitate achievement of the landfill diversion targets in the areas of prevention, recycling and biological treatment, and residual waste treatment.

## Prevention

- National Waste Prevention Programme – a module to deal specifically with BMW is to be developed following publication of the Strategy.
- The introduction of a "Pay-by-Use" system of waste management on 1 January 2005.
- The continuation of the "Race against Waste" campaign with the objective of improving environmental behaviour.

## Recycling and Biological Treatment

- A Market Development Group of key stakeholders was established in late 2004 with the objective of driving forward the development of existing markets for recyclables and identifying new applications and markets for recyclables and secondary recycled products. Separate Working Groups were established for the priority BMW streams of paper/ cardboard and organics.
- Local Authorities will use the Waste Collection Permitting system to introduce a requirement for separate collection policies in a uniform manner across their functional area.
- Bye-laws governing the presentation and collection of waste will be adopted by local authorities to support the implementation of separate collection systems.
- Regulations will be reviewed on a regular basis to ensure that the legislative provisions for waste collection and waste treatment facilities support the objectives of the Strategy to the greatest extent practicable.
- The provision of pre-treatment (e.g. Material Recovery Facilities) and biological treatment facilities by local authorities will be supported by capital grant assistance.

## Residual Waste Treatment

- Residual waste treatment will be required to at least cater for the proportion of BMW which cannot be prevented or recycled (including either material recycling or biological treatment) and which is not allowed to be landfilled under the provisions of the 1999 Directive.

- Thermal Treatment with energy recovery is seen as a robust residual waste treatment technology which can also cater for non-BMW and industrial wastes. The 10 Waste Management Plans for the regions/ counties of Ireland recognise this integrated policy role of thermal treatment and facilities have been proposed by local authorities for the treatment of residual waste within 6 of the regions.
- Mechanical-Biological Treatment (MBT) – generally followed by thermal treatment or landfill - can also play a role in the pre-treatment of residual waste, particularly in the short-to-medium term when thermal treatment capacity is being developed. MBT capacity developed should be compatible with the treatment of source-separated organics in the future.

The Accounting Officer stated that the National Strategy on Biodegradable Waste sets out the total annual tonnage which must be diverted from landfill at a national level each year to meet Irish landfill diversion targets. These diversion requirements correspond to the available capacity which will be needed for alternative treatment methods to process the BMW diverted from landfill. The capacity will include appropriate waste collection infrastructure, pre-treatment infrastructure (such as Material Recovery Facilities) and final processing capacity for the prepared recyclable materials.

In order to optimise flexibility for the Strategy to achieve national targets, latitude was devolved to individual waste planning regions/ counties to decide how their Waste Management Plans could best address the landfill diversion requirements within the overall framework of the national targets. Each region/ county would be required to either provide the required capacity directly or alternatively to source the necessary capacity outside the region/county. These projected figures for alternative treatment requirements are to be kept under continuous review and updated regularly by each region/ county in order to ensure that sufficient capacity is available to facilitate the achievement of the required BMW diversion targets.

# Evaluating Performance

In terms of the performance evaluation of local authorities by the Department, the Accounting Officer stated that the success of implementation of the management measures for the BMW stream will be measured against the level of waste generation, the rates of recycling and recovery for various materials, and ultimately the amount of BMW sent to landfill. The Strategy will be reviewed at regular intervals and will be subject to further development which will be designed to deliver the principal objectives and targets which have been established.

The Accounting Officer acknowledged that monitoring and review of strategy implementation will be crucial if the challenging targets are to be achieved. The following monitoring measures are proposed

- Simple performance indicators outlining current performance and future targets in terms of BMW generation, paper/ cardboard recycling rates, textile recycling rates, wood recycling rates, biological treatment rates for organic waste, residual waste treatment rates and the level of landfill of BMW (See Table 27).
- The EPA will issue regular reports on these performance indicators in its National Waste Report publications.
- Each Annual Implementation Report to be prepared by local authorities on the implementation of the Waste Management Plan will record progress made in relation to the National Strategy on Biodegradable Waste over the previous year.
- The Strategy Implementation Group will provide qualitative information in relation to the particulars of Strategy implementation and will make recommendations on the manner in which improved performance can be achieved.

In terms of the individual materials within the BMW stream, the following target levels are proposed.

**Table 27 Proposed Target Levels**

| **Material Recycling** | **Targets** |
|---|---|
| Paper/ Cardboard | 55% in 2010, 65% in 2013 and 67% in 2016 |
| Wood | 90% to 95% between 2010 and 2016 |
| Textiles | 15% in 2010, 20% in 2013 and 25% in 2016 |
| **Biological Treatment** | **Targets** |
| Overall Diversion of food and garden waste | 35% in 2010 and 48% in 2016 |
| Home Composting | 13.5% in 2010 and 2013, 16% in 2016 |
| Separate Collection and Centralised Biological Treatment | 25% in 2010, 33% in 2013 and 36% in 2016 |

# Chapter 6

# Department of Education and Science

# 6.1 Payment of Salary in Lieu of Untaken Annual Leave

## Annual Leave Regulations

Rules for the regulation and control of annual leave allowances for civil servants are set out in Department of Finance Circular 27/03.

These rules allow payment to be made to civil servants for untaken annual leave accrued at the date of cessation of employment *i.e.* resignation, retirement or death. Payment in respect of each day of untaken annual leave should be calculated on the basis of one fifth of the normal weekly salary, irrespective of whether staff are paid on a weekly, fortnightly or monthly basis.

The Circular sets out rules to be applied where it is not possible because of work requirements to allow staff to avail of annual leave in excess of the statutory minimum. Any such untaken leave may be carried over to the following year on the basis of a three-year cycle. However, leave carried over at the end of year two of the cycle is forfeit if not taken during the third year. Under the provisions of the Organisation of Working Time Act 1997, Departments are obliged to ensure that an officer takes his/her full statutory minimum annual leave entitlement within the year in which it is accrued or, with the employee's consent, within six months of the start of the next leave year. This allows for limited carryover of the untaken statutory balance into the new leave year.

## Audit Findings

In the course of a payroll audit of the Department of Education and Science it was noted that the Department made payment for untaken leave of 120 days to a senior official who had recently retired. The gross amount of the payment made was €77,586.

As I was concerned that some of the untaken leave for which payment was made in this instance breached the regulations on carryover set by the Department of Finance, I asked the Accounting Officer for details of the untaken leave for which payment was made in this instance, the circumstances which gave rise to the payment, the extent of payments made by the Department for untaken leave in the past five years and the number of instances where the regulations regarding carryover of leave had been breached by the Department.

## Accounting Officer's Response

### Specific Case

The Accounting Officer stated that in this case, the untaken leave had accumulated over the period since 1994. She informed me that the official was unaware that this payment was not consistent with the Department of Finance Circulars. He had been informed by the Department's Personnel section at the time of his retirement that he was entitled to be paid for any untaken leave and had been requested to forward details of leave taken so that Personnel section could make the necessary calculations and arrange payment. When the matter was brought to his attention recently, he immediately indicated that he wished to repay to the Department the amount inadvertently received in respect of days in excess of those allowable had the Department implemented the provisions of Finance Circular 27/03 (and its predecessor 26/99) in relation to carryover of annual leave. If the circular provisions had been implemented he would have been paid for 37 days not 120. The gross overpayment was €53,664: the net amount worked out at €29,570 and arrangements are in train to repay this amount to the Department.

### Department's Practice

The Accounting Officer informed me that it had been the practice in the Department to allow staff to carry over annual leave in excess of that allowed under Department of Finance Circular 27/03 and pay staff upon retirement for untaken leave. While the Department informed staff of the terms of the Circulars, in practice it had allowed the carryover of leave in excess of that allowed under these Circulars due to various pressures over a number of years.

She stated that in the late 1990s, the Department had serious concerns as to its capacity to deliver the range of educational services required of it in an increasingly demanding environment. A major programme of structural reform was recommended by a Task Force chaired by a former Secretary General of the Department of Finance. This led to internal reorganisation of the Department, the creation of a network of Regional Offices and the establishment of the State Examinations Commission and the National Council for Special Education. All of these reforms contributed to a significant turnover of staff in 2003. This was followed by Ireland's Presidency of the EU from January to June 2004, which also gave rise to additional pressures. As a result of these pressures, the Department took the position that staff should not suffer loss of untaken leave.

She confirmed that the Department had not sought the approval of the Department of Finance to set aside the provisions of Circular 27/03.

### Extent of Payments for Untaken Leave

The Accounting Officer informed me that approximately €392,000 had been paid to 64 officials in the last five years on foot of untaken leave on cessation of employment. In respect of 16 of these (excluding the payment in the specific case), approximately €69,000 was paid in respect of untaken leave estimated to be in excess of that which would have been payable if the Circulars had been implemented by the Department over the period concerned. Payment for untaken leave ranged from as little as a half day to 151 days, with 22 payments in the period exceeding €5,000.

She also informed me that over the same five-year period the Department had permitted staff to exceed the maximum allowable carryover of annual leave in 137 separate instances.

### Recovery of Amounts Overpaid

The Accounting Officer informed me that the Department had not sought repayment of any amounts paid in respect of untaken leave in excess of that which would have been allowed had the Department implemented the provisions of Circular 27/03 and its predecessor in relation to carryover of annual leave.

However, she stated that she was considering the position regarding the approach to be adopted in the cases where overpayments had been made.

### Revised Procedures

The Accounting Officer stated that, following an analysis of the position, the Department intends to put in place a range of measures designed to bring about compliance with Circular 27/03 for all staff on a phased basis and at the same time minimise the circumstances in which individuals receive payment in lieu of untaken leave.

## Views of the Department of Finance

As the issues arising in the Department of Education and Science also have relevance for all other Departments and Offices, I sought the observations of the Accounting Officer of the Department of Finance on the matter.

He informed me that the day-to-day implementation of the Circular was a matter for Departments and Offices. He confirmed, however, that under the rules any untaken leave in excess of that allowed to be carried over by serving staff under a three year cycle provided for in the Circular was lost and that there was no provision for payment to be made in such circumstances. He informed me that separate arrangements under the Circular allow for payments to be made in respect of untaken leave accrued at the date of cessation of employment within the context of the three year cycle and, where appropriate, the provisions of the Organisation of Working Time Act 1997.

It was his view that Departments and Offices should as a matter of course consider recovering any overpayments that arise. He also indicated that it was a matter for Departments and Offices to consider whether it is possible or appropriate to pursue repayment in light of the circumstances of each individual case.

He also informed me that the Department of Finance was not immediately aware of other Departments or Offices where the provisions of the Circulars were not applied in recent years. He added that, in the light of my enquiries and the response of the Department of Education and Science, his Department had recently asked Departments and Offices to review their files to identify any cases where the annual leave carryover rules had not been properly applied and to rectify the matter. The Department of Finance had also advised all Departments and Offices of the need to apply the rules and procedures in the relevant Circulars and instructed them not to make any payments in respect of accumulated leave other than those set out in the Circular to cover the arrangements which apply on the cessation of employment.

# 6.2 Institiúd Teangeolaíochta Éireann

Institiúd Teangeolaíochta Éireann (ITÉ) was established in 1972 as a company limited by guarantee without share capital. Its primary objective as set out in its Memorandum of Association was: *"to initiate, promote, commission and carry out studies, research and experiments on language, language behaviour, language acquisition and the teaching of languages, such work to be primarily concerned with the Irish language, with promoting its development and extending its use".*

In recent years a value for money report and an independent consultant's report made recommendations in relation to the reorganisation of ITÉ. However, no progress was made in implementing these recommendations.

Due to some internal difficulties in the company the Director agreed to stand aside from his duties as Director in the first half of 2002. An Acting Director subsequently resigned in November 2002, citing personal reasons. The then Chairman of the company resigned his position in January 2003. At this stage the company was without a Director or Chairman. In January 2003, two members of staff served legal proceedings against the company.

The Department met a delegation of members of the Executive Committee of ITÉ in May 2003 and, having considered the history of discord in the company and the difficulties that members would have in trying to run the company, agreed that the prudent course would be to wind up the company. The Department's desire was that the winding up process would be orderly and achieved without undue delay.

An Extraordinary General Meeting of ITÉ, held on 18 July 2003, agreed to initiate a process of voluntary liquidation. At a meeting of the Executive Committee of ITÉ on 5 December 2003 a timetable for appointment of a liquidator was agreed. The liquidator was subsequently appointed on 9 January 2004. The company agreed to issue redundancy notices to staff in advance of the liquidator's appointment.

I have certified final accounts of the company to 9 January 2004. At that date ITÉ had total assets of €395,000, of which €393,000 was cash.

I noted that funding continued to be provided from the Vote for Education and Science during the liquidation process – €1.480 and €1.304 in 2004 and 2005 respectively (this compares with funding of €1.764 and €1.985 provided in the previous two years). I also noted that after two years the liquidation had not been completed and a further €889,000 has been provided for 2006 to meet expenditure on payroll, office expenses and liquidation fees. I asked the Accounting Officer to outline the reasons for the delay in finalising the affairs of the company.

The Accounting Officer informed me that the Department gave a commitment to provide every assistance to the company in giving effect to its decision and had been working closely with the liquidator since his appointment in this regard. This included exploring possible arrangements for the continuation of certain research activities previously carried out by ITÉ and, in the interest of assisting with an orderly wind-up, facilitating appropriate re-deployment or other appropriate arrangements for staff in line with public service policy in these matters.

The period of notice of redundancy for staff at ITÉ had been periodically extended by the liquidator to take account of the ongoing process of pursuing re-deployment options and of the interim operational needs of the company during the wind-up period. The entitlements of those employees for whom appropriate re-deployment arrangements were not made would be determined in accordance with the terms of their contracts. She stated that by the end of December 2005 seven of the original 26 staff remained in the employment of ITÉ; three of these left early in 2006. It was anticipated that by August/September 2006 all of the four remaining staff would either be redeployed or have been given their statutory notice to leave ITÉ.

She provided me with examples of the type of work carried out by ITÉ during the liquidation period. These included projects in the areas of Sociology of Language, Psycholinguistics, Modern Languages and Structural Linguistics.

Another factor in the delay was the need to surrender leases on property occupied by ITÉ. ITÉ's interest in a property owned by the Office of Public Works would soon be transferred to the Dublin Institute for Advanced Studies; the Liquidator handed back another premises in April 2005, taking advantage of a break clause in the lease; while following lengthy negotiations, two further leases on a subdivided property were to be surrendered under a Deed of Surrender awaiting the landlord's signature. The need to deal with two separate legal actions taken against ITÉ also contributed to the delay.

The Accounting Officer provided details of the costs incurred since the start of the liquidation process in January 2004 as shown in Table 28.

**Table 28**

| | **To end 2005** | **Jan - May 2006** |
|---|---|---|
| | € | € |
| Pay | 2,152,115 | 170,821 |
| Rent | 479,800 | - |
| Other Non-Pay | 409,257 | 34,754 |
| Liquidator Fees | 80,504 | - |
| Liquidator Expenses | 167,645 | - |
| **Total** | **3,289,321** | **205,575** |

The Accounting Officer also informed me that when the remaining staff have left ITÉ a number of relatively minor items would remain to be finalised (mainly by the Department rather than the Liquidator), principally

- Future publication of ITÉ reports
- Relocation of ITÉ archives,
- Settlement of Litigation
- Transfer of ITÉ copyright.

She expected the liquidation would be completed in 2006.

# 6.3 Superannuation Schemes

In my 1995 and 2004 Annual Reports I drew attention to the failure of the Department of Education and Science to ensure that there was up to date legislative authority for amendments to superannuation schemes of teachers.

In the course of the 2005 audit, I noted that the Pensions Section of the Department had discovered, in April 2004 while reviewing another matter, that the terms of an agreement between the Department and teachers representatives contained in Agreed Report 4/87 had not been implemented. The intention was to bring certain provisions of the teachers' superannuation schemes affecting teachers who retired on ill health grounds or who died in service, into line with other public service schemes, but this had not occurred. As a result, these pensioners and their spouses were paid less than their full retirement benefits.

I asked the Accounting Officer to outline the circumstances that gave rise to this failure to pay the proper benefits to the pensioners concerned.

The Accounting Officer informed me that the Agreed Report was worded in such a way as to be open to misinterpretation and that the difficulties of interpretation were the subject of correspondence between the Pensions Section and the Conciliation and Mediation Section of the Department from October 1988. However, the matter had not been clarified at the time of transfer of the Pensions Section from Dublin to Athlone in 1991 and appeared to have been overlooked following the extensive staffing changes that occurred at that time.

The matter rested so until April 2004 when, in examining the file of Agreed Reports, the Pensions Unit identified a parallel between the intent of the Agreed Report in regard to primary and secondary teachers and the corresponding Local Government provisions in another scheme applicable to vocational teachers.

The Accounting Officer assured me that the terms of the Agreed Report have been correctly applied on an ongoing basis to primary and secondary teachers who have retired on ill health grounds or died in service since May 2004. A review of ill-health retirement cases and cases where teachers had died in service since the beginning of the 1986/87 school year had also been undertaken. A total of 655 awards had to be revised. In 428 cases arrears payments totalling €1.65m were made in 2005, a further 85 payments amounting to €98,000 have been made to date in 2006 while work is ongoing in the remaining 142 cases. It was expected that the total cost would be somewhat less than the €2.2m originally estimated. The payments include a cost of living compensation payment where, through no fault of the beneficiary, a delay of more than a year has arisen in paying superannuation benefits. The payments were in accordance with procedures sanctioned by the Department of Finance.

The Department was satisfied, as a result of the checks it had carried out, that the provisions of other agreed reports and approved changes are being correctly implemented for schemes for which it has operational control.

The Accounting Officer was of the view that the problem in this instance did not arise from the failure to update the statutory schemes but was due to the combination of circumstances outlined. In this regard she informed me that she had assigned an officer of the Department to the Pensions Unit on a full-time basis with the sole task of updating the statutory pension schemes, commencing with the Secondary Teachers' Pension Scheme. Updated drafts of three Spouses' and Children's Schemes for Secondary Teachers have already been forwarded to the Department of Finance for consent and to the Parliamentary Counsel. Work is continuing on the drafting of the updated main Secondary Teachers' Superannuation Scheme.

# Chapter 7

# Community, Rural and Gaeltacht Affairs/Justice, Equality and Law Reform

# 7.1 Agency Services – Control of Advances to Pobal

## Pobal

Pobal (formerly Area Development Management Ltd.) is a not-for-profit company with charitable status initially set up in the early 1990s to manage programmes on behalf of the Irish Government and the EU. Following a consultancy review in 2003, the Government agreed to a fundamental reform of the company to address accountability issues, to define its role as a delivery agent for Government programmes and to provide for the appointment by the Government of the Board and Chair. Pobal operates within the ambit of the Department of Community, Rural and Gaeltacht Affairs and its annual accounts are subject to audit by me.

Pobal has no independent source of funding. Contractual arrangements, negotiated with the Departments and Agencies for which it delivers a service, provide that it receives advances to enable it meet the cash requirements of the programmes it manages. The financial statements of Pobal for 2005 show that it had received cash advances of some €174m in the year. €10.5m of this went to meet its administration costs, agreed as part of these arrangements.

### Year-end Departmental Balances in Pobal's 2005 Financial Statements

The financial statements for Pobal for 2005 indicate that at 31 December 2005, the company held balances on behalf of Departments and the Dormant Accounts Fund Disbursements Board amounting to approximately €34.5m. It had cash balances of some €37m at that time (an increase of some €12m on 31 December 2004) and earned some €700,000 in bank interest on foot of these cash balances. Table 29 shows the balances Pobal held on behalf of its main clients, the Departments of Justice, Equality and Law Reform and Community, Rural and Gaeltacht Affairs at the beginning of 2005, how much was paid to it by way of advances, the administration costs it was entitled to, the payments made by it under each programme and the amount still on hands at the year-end.

**Table 29**

| | Balance 1 January 2005 | Advances Received | Less Administ-ration Costs | Less Programme Payments | Balance 31 December 2005 |
|---|---|---|---|---|---|
| | €'000 | €'000 | €'000 | €'000 | €'000 |
| **Department of Community, Rural and Gaeltacht Affairs** | | | | | |
| Grants for Community and Voluntary Service | 0 | 6,142 | 183 | 0 | 5,959 |
| Local Development/Social Inclusion (LDSIP) | 497 | 47,697 | 2,112 | 44,760 | 1,322 |
| RAPID | 462 | 1,333 | 783 | 679 | 333 |
| Rural Social Scheme | 172 | 24,287 | 360 | 23,036 | 1,063 |
| Other | 181 | 0 | 0 | 126 | 55 |

| **Department of Justice, Equality and Law Reform** | | | | | |
|---|---|---|---|---|---|
| Equal Opportunities Childcare Programme | 12,047 | 72,549 | 3,207 | 64,417 | 16,972 |
| Equality for Women Measure | 32 | 3,490 | 315 | 1,555 | 1,652 |
| Enhancing Disability Services Programme | 0 | 3,000 | 146 | 3 | 2,851 |
| Other | 3 | 345 | 75 | 2 | 271 |
| **Total** | **13,394** | **158,843** | **7,181** | **134,578** | **30,478** |

As the amount of interest earned by Pobal in the year suggested that it had a daily average of the order of €20m on deposit throughout the year, I sought the observations of the Accounting Officers of both Departments.

## Department of Community, Rural and Gaeltacht Affairs Response

The Accounting Officer pointed out in his response that Pobal is a private company limited by guarantee without access to funding in its own right. It was therefore necessary for it to be put in funds by his Department to enable it to discharge the obligations placed on it in terms of the delivery and administration of programmes on behalf of his Department. Oversight and control procedures varied according to the requirements of each programme. Budgets for each programme and associated administrative costs were agreed with Pobal annually.

He stated that funding was provided to Pobal on the basis of advances, drawn down in accordance with the contractual arrangements particular to individual programmes, to meet commitments and forthcoming expenditure. Expenditure incurred by Pobal in previous periods was taken into account in deciding the amount to be advanced on foot of each drawdown request. Funds were only advanced where they were considered warranted to meet commitments on hand or demands likely to arise within the subsequent operating period.

He informed me that an independent review of the drawdown procedures and the funding arrangements in place between his Department and Pobal for the delivery of Departmental programmes was currently being undertaken by the Internal Audit Unit of his Department.

In subsequent correspondence the Accounting Officer informed me that following recent meetings with Pobal, the Company would, for the larger Programmes (e.g. LDSIP, Rural Social Scheme and the Community Services Programme),

- Receive two months' funds at the commencement of the financial year and
- Not make an application to draw down the next tranche of funding until it has a month's or less funding remaining.

In effect, bearing in mind that it took 15 days to process payments at Departmental level, this meant that the operating cash for programmes could run as low as a fortnight's advance payments. Such an arrangement was intended to ensure that Pobal was not at any time holding more than two months' funds, and would generally hold substantially less. These revised payment procedures would be subject to the verification checks already carried out by his Department on all requests for funding received from Pobal.

In regard to smaller Programmes, such as the Annual Community Grants Scheme, it was proposed to make payments to Pobal only in respect of actual commitments under the Scheme and based on careful ongoing appraisal of actual expenditure.

He stated that with all programmes, the final payments each year would be calculated to ensure that there was no significant carryover of funds from year to year. In the case of larger Programmes, however, it would be necessary to pay an advance of 2 weeks' funding to ensure that projects were kept in funds until the first draw-down of the following year's funding could be processed.

In regard to the level of interest earned by Pobal, he informed me that, in light of the increasing value of the programmes being delivered by Pobal on behalf of the Department, the question of interest earned was now being addressed in the ongoing review of the apportionment of administration costs associated with those programmes.

In his subsequent communication, he stated that it had recently been agreed with Pobal that his Department's approval would be sought before any surplus on the Company's accounts was distributed in future years. It was anticipated, given the revised cash-flow management procedures being implemented, that the surplus accruing from interest would, in any event, be significantly reduced.

## Department of Justice, Equality and Law Reform Response

The Accounting Officer of the Department of Justice, Equality and Law Reform informed me that the drawdown of advances by Pobal was fully supported and evaluated by his Department and took account of the need to ensure that payments would not lead to an excessive cash reserve in the accounts of Pobal relative to its requirements to spend drawdown funds and to make a prudent provision for expenditure by it in the subsequent operating period.

In respect of his Department's funding of the Childcare Programme capital expenditure he pointed out that by December 2005, his Department considered it prudent, given the level of outstanding capital commitments, to increase its funding of Pobal by approximately 10% of these commitments. This was considered essential to avoid unnecessary delays within Pobal in processing applications for payment. He said that even allowing for stringent evaluation of drawdown requests, unanticipated delays outside the control of both Pobal and lead Departments could arise.

However, the Accounting Officer suggested there was a need to review the way in which Pobal interacts with all Government Departments. He considered that the role of the Department of Finance in any cross departmental review would be crucial both in terms of the way Pobal operated, and as regards the impact of any changes on the annual estimates process. The way funding was allocated on a year on year basis for schemes operated by Pobal on behalf of Government Departments would also have to be examined.

He stated that there was no provision in terms of engagements or contracts for Pobal to retain interest earned on any balances provided by his Department under the Equality for Women Measures, Enhancing Disability Services or Community Based CCTV programmes. This matter would be clarified with Pobal in due course. The issue of interest earned on the funding provided under the Childcare Programme had been the subject of ongoing discussion between Pobal and the Childcare Directorate but had yet to be fully resolved.

In subsequent correspondence, following a meeting of the key parties, the Department informed me that new accounting procedures would be implemented in the very near future to ensure that Exchequer funding provided to Pobal would be based on documentary evidence of corresponding expenditure by Pobal via standing imprest arrangements for rolling grant-aided programmes such as Childcare, Equality Measures and Disability Projects. These procedures would minimise bank account balances held by Pobal and thereby its potential to accumulate bank interest.

# Chapter 8

# International Co-operation

# 8.1 Overseas Development Aid

## Background

Irish Aid, formerly Development Co-operation Ireland, which is a directorate of the Department of Foreign Affairs (the Department) is responsible for the administration of Ireland's programme of assistance to developing countries. The largest proportion of assistance is provided for in Subhead B - Bilateral and Other Co-operation. Expenditure from this subhead in 2005 amounted to almost €340m.

Irish Aid programme expenditure comprises grants to third parties such as partner governments, non-governmental organisations (NGOs), United Nations agencies, other multilateral bodies and aid partners. It also involves an element of direct expenditure. Funding may be disbursed from Departmental Headquarters or through Overseas Offices in the developing world. Table 30 shows the make up of expenditure for the years 2003 – 2005.

**Table 30**

| | 2003<br>€ m | 2004<br>€ m | 2005<br>€ m |
|---|---|---|---|
| Grants to Countries having Irish Aid Overseas Offices[34] | 130 | 143 | 145 |
| Other Grants (e.g. to NGOs, Multilateral agencies) | 110 | 146 | [35]189 |
| Direct Expenditure | 14 | 6 | 6 |
| **Total Charge to Subhead B** | **254** | **295** | **340** |

Additional direct expenditure of €11m (2003), €9m (2004) and €11m (2005) is included in Subhead A – Salaries, Wages and Allowances.

## Bilateral Assistance

Bilateral Assistance comprises support for eight specific programme countries and certain other regions and countries, assistance through non-governmental organisations (NGOs), support for the fight against HIV/AIDS and rehabilitation assistance.

Since 2005 eight countries - Ethiopia, Lesotho, Mozambique, Tanzania, Uganda, Zambia, Timor Leste and Vietnam – have been designated as programme countries by Irish Aid. These countries have a very low ranking in terms of human development indicators such as the percentage living in absolute poverty, life expectancy, adult literacy, infant mortality, access to safe water, sanitation and health services. In addition, assistance is provided for specific projects in a number of other regions and countries for example the western Balkans, Eastern Europe, Zimbabwe, South Africa and Palestine.

The bilateral relationship between Irish Aid and programme countries is governed by individual country strategy plans. These are negotiated between Irish Aid, and the relevant national government. Other donors and a number of the larger international organisations are consulted as appropriate. The plans are focused round the achievement of sustainable poverty reduction targets and are typically reviewed every three years. The percentage of aid channelled through government institutions at national and local government level was 68% in 2003, 74% in 2004 and 72% in 2005. Details of 2003 and 2004 expenditure,

[34] Includes Republic of South Africa and Zimbabwe that do not have programme country status.
[35] Includes Vietnam, which came on stream in 2005.

which can be directly related to the Department's most recent Annual Consolidated Audit Reports for those years, are shown in Table 31.

**Table 31 - Support Managed by Overseas Offices**

| Country | Through National Government Systems € m | | Through Local Government Systems € m | | Other € m | | Total Support Managed by Overseas Offices € m | |
|---|---|---|---|---|---|---|---|---|
| | 2003 | 2004 | 2003 | 2004 | 2003 | 2004 | 2003 | 2004 |
| Ethiopia | 1.5 | 8.2 | 15.2 | 12.8 | 9.1 | 8.3 | 25.8 | 29.3 |
| Uganda | 25.8 | 27.2 | 0.6 | .5 | 7.9 | 4.6 | 34.4 | 32.3 |
| Mozambique | 15.6 | 14.7 | 5.8 | 8.1 | 11.5 | 7.5 | 32.9 | 30.3 |
| Tanzania | 14.4 | 15.2 | 1.9 | 3.4 | 4.4 | 4.6 | 20.7 | 23.2 |
| Zambia | 4.9 | 5.9 | 2.4 | 4.0 | 7.3 | 7.8 | 14.6 | 17.7 |
| Lesotho | 8.2 | 9.1 | 0.0 | 0.0 | 2.6 | 2.3 | 10.7 | 11.4 |
| Timor Leste | 1.5 | 2.0 | 0.0 | 0.0 | 1.4 | 2.0 | 2.9 | 4.0 |
| South Africa | 5.3 | 3.4 | 1.6 | 2.5 | 4.8 | 4.1 | 11.7 | 10.0 |
| Zimbabwe | 0.0 | 0.0 | 0.0 | 0.0 | 0.8 | 0.8 | 0.8 | 0.8 |
| **Total** | **77.2** | **85.7** | **27.5** | **31.3** | **49.8** | **42** | **154.5** | **[36]159** |

The aid delivered through national government involves a range of aid instruments the majority of which relate to moneys that are clearly earmarked for specific purposes e.g. health, education, agriculture, water and sanitation, or specific projects. In Tanzania and Mozambique some of this funding is delivered as general budget support to the Treasury.

The balance of Irish Aid programme money, not delivered via national or local government, includes administration, support to NGOs, UN and other multilateral agencies and moneys spent directly by Irish Aid on behalf of various programmes and partners.

I undertook an examination of Irish Aid audit and evaluation procedures with particular emphasis on projects funded through bilateral assistance in the programme and other countries in 2003 and 2004 as these are the most recent years for which consolidated results of the evaluation procedures used are available.

# Examination Findings

## Financial Control and Accountability

All assistance budgets are submitted annually, in advance, for approval by an interdepartmental committee, set up by Government decision, on which the Department of Finance and other Departments with an involvement in development co-operation are represented.

[36] This figure includes the Subhead A costs of Overseas Offices, which exceeded €9m in 2004.

This interdepartmental committee, acting as the Programme Appraisal and Evaluation Group (PAEG) under the authority of the same Government decision, approves all new expenditure proposals. The group is assisted by external consultants who evaluate the proposals before submission for consideration.

Both direct and indirect aid expenditure are extensively audited. The audit of indirect expenditure relies increasingly on the work of auditors external to the Department. The Auditors General of partner governments account for the largest proportion of other auditors on whom Irish Aid relies, with the larger audit firms contributing most of the remainder. Irish Aid works closely with the Auditors General to strengthen their capacity (e.g. funding of training initiatives, development of IT audit and equipment purchases).

In the eight programme countries in receipt of bilateral assistance, Ireland's aid programmes, are subject to annual external audit by

- The Department's Evaluation and Audit Unit (EAU) or
- Professional auditors commissioned by Irish Aid, or jointly with other aid donors or independently by development partners or
- Other countries' Auditors General.

Area-based programmes (programmes which operate in specific local authority districts) and sector support programmes (which cover specific sectors such as health or education) in these programme countries are also subject to annual audit.

There are accounting staff in all of the Overseas Offices in the African programme countries.

## Evaluation and Audit Unit

The EAU is an independent unit within the Department. Its mission is to provide an efficient, effective, relevant and independent evaluation and audit function and to contribute to policy development within the overall assistance programme. The unit is currently staffed by a head of unit, three auditors[37] two evaluators and three support staff based in headquarters and six auditors based locally in the Department's Overseas Offices in programme countries.

The work of the EAU is carried out in accordance with an annual work plan and the Strategic and Multi-annual Work Plan 2006 to 2008. The plan notes that progress has been achieved recently in strengthening evaluation and audit in Irish Aid but does, however, state that staff shortages limit the unit's ability to deliver adequate coverage across the whole programme.

I enquired as to the EAU's ability to deliver adequate audit coverage across the whole aid programme in light of the staff shortages and the implications of these shortages for the unit's stated mission.

In reply, the Accounting Officer stated that Irish Aid recognises that, as the aid programme grows, the capacity of the EAU will need to be enhanced in order to ensure effective audit and evaluation. He stated that Irish Aid recognises that the EAU has experienced some limitations due to staffing, particularly in developing a programme of value for money audits, and on providing audit support to other sections of Irish Aid. The EAU had at all times aimed to deploy available resources efficiently and effectively with a particular focus on the overseas offices and to maximise assurance by reliance on the work of others and through the use of consultants.

[37] Two additional posts have been sanctioned.

In relation to staff numbers, he stated that identifying and retaining staff for this highly skilled area presented a challenge to Irish Aid. In the programme countries 3 additional local staff have been recruited since 2003 bringing the total to 6 local audit staff.

He further stated that the implication of staff shortages had been delays in feeding back to and supporting line management in the interpretation of partners' audit reports. However, this had to be considered in the context that support is available immediately from the 6 internal auditors in the programme countries and via the in-country management structures in Irish Aid and other donors in the field.

The Accounting Officer also stated that the EAU utilises audits commissioned by various partners, where these audits include Irish funds. The largest proportion of these audits consists of audits carried out by national Auditors General and audits carried out by recognised audit firms. This practice of reliance on the audit work of others in relation to grants to development partners assisted Irish Aid to fulfil its requirements under the Rome Declaration on Harmonisation.

## Annual Consolidated Audit Report

The EAU produces an annual Consolidated Audit Report, which covers direct expenditure by Irish Aid and the disbursement of grants to development partners. The reports for 2003 and 2004 summarise all the audit activity completed in respect of expenditure in those years. They are intended to inform line management, support the Audit Committee in its oversight of the audit and evaluation function and assist the annual audit by my Office.

The objectives of the Consolidated Audit Report are to

- Identify gaps in audit assurance by detailing what expenditure has not been audited or for which audit reports have not been received
- Summarise the findings of the large number of audits and management letters to identify key deficiencies in accounting procedures and internal control
- Show the status of recommendations arising from previous years' audits
- Highlight whether financial statements give a true and fair view of the financial position of the entity or programme being audited.

### Overall Audit Coverage 2003 and 2004

The 2004 Consolidated Audit Report, which was completed in March 2006, included an update of the original 2003 report completed in October 2005. This showed that the audit coverage of expenditure had increased from 78% to 85% (this had increased again to 89% by mid-July 2006) for 2003. The audit coverage for 2004, as at April 2006, was 63%. This had increased to 84% by mid-July 2006. The Department's policy is that the level of audit coverage should aim to be greater than 85% each year. The audit coverage of 2003 and 2004 expenditure as at mid-July 2006 is outlined Table 32.

**Table 32 Audit Coverage**

| | 2003 | | | 2004 | | |
|---|---|---|---|---|---|---|
| **Country** | **Amount Audited €** | **Amount Unaudited €** | **% Unaudited** | **Amount Audited €** | **Amount Unaudited €** | **% Unaudited** |
| Ethiopia | 18,994,084 | 6,785,836 | 26 | 23,775,744 | 5,533,305 | 19 |
| Lesotho | 10,573,256 | 109,525 | 1 | 11,474,867 | - | 0 |
| Mozambique | 28,583,553 | 4,351,987 | 13 | 20,278,900 | 10,005,227 | 33 |
| South Africa | 9,782,614 | 1,961,627 | 17 | 9,186,856 | 886,920 | 9 |
| Tanzania | 20,359,075 | 357,025 | 2 | 19,283,474 | 3,940,000 | 17 |
| Timor Leste | 2,485,743 | 450,420 | 15 | 3,915,727 | 9,900 | 0 |
| Uganda | 33,448,892 | 878,779 | 3 | 30,424,011 | 1,848,152 | 6 |
| Zambia | 12,188,710 | 2,460,231 | 17 | 14,941,533 | 2,712,642 | 15 |
| Zimbabwe | 368,195 | 394,313 | 52 | 275,704 | 482,475 | 64 |
| **Total** | **136,784,122** | **17,749,743** | **11** | **133,556,816** | **25,418,621** | **16** |
| **Total for Year** | **€154,533,865** | | | **€158,975,437** | | |

As audit reports had not been received at the time of my examination in respect of 37% (this had improved to 16% at 30 June 2006) of 2004 expenditure, I enquired as to the total number of reports receivable for 2003 and 2004 and how many of these were currently outstanding. I also enquired as to the limitations on the Department's scope to take effective action in respect of material adverse findings or significant audit recommendations as a result of delayed receipt of audit reports. I further enquired as to how the Department ensured that the stated mission of EAU to maintain an efficient, effective, and relevant evaluation and audit function is achieved and how the risks to public funds from irregularities or misappropriations remaining undetected, due to delays in receiving reports, are minimised.

The Accounting Officer stated that Irish Aid's overseas office audit policy emphasises that audit coverage is a tool and does not, in itself, give complete assurance. The policy outlines 85% as a guide figure only and the specific circumstances in each country must also be taken into account. There are many additional processes and tools in place that inform Irish Aid's assurance. These include partner Governments' own public expenditure reviews, tracking studies, work by other donors, internationally conducted national assessments (typically led by IMF/World Bank), day to day monitoring and discussions by line management based in the overseas offices.

## Audit Reports and Opinions Received

Over 450 audit reports were received in respect of 2003 and 2004 expenditure. The Accounting Officer pointed out that these fell into two distinct categories: internal audits relating to Irish Aid and audits relating to the use of grants by the Department's development partners. The 355 audit reports relating to the use of grants by development partners are analysed in Table 33, which shows, by country, the percentage of reports, which contained a qualification or disclaimer. The Accounting Officer said that it was important to note that none of the qualified reports related to Irish Aid's direct expenditure.

**Table 33 Analysis of Audit Opinions received in 2003 and 2004**

| | 2003[38] Audit reports | | | 2004 Audit reports | | |
|---|---|---|---|---|---|---|
| | **Received** | **Qualified or Disclaimer Opinions** | **% Qualified or Disclaimer** | **Received** | **Qualified or Disclaimer Opinions** | **% Qualified or Disclaimer** |
| Ethiopia | 13 | 2 | 15 | 31 | 2 | 6 |
| Lesotho | 25 | 5 | 20 | 20 | 4 | 20 |
| Mozambique | 33 | 12 | 36 | 29 | 13 | 45 |
| South Africa[39] | 22 | 12 | 55 | 12 | 9 | 75 |
| Tanzania | 25 | 10 | 40 | 20 | 14 | 70 |
| Timor Leste | 2 | 0 | 0 | 2 | 0 | 0 |
| Uganda | 11 | 3 | 27 | 24 | 1 | 4 |
| Zambia | 33 | 2 | 6 | 43 | 3 | 7 |
| Zimbabwe[40] | 6 | 5 | 83 | 4 | 3 | 75 |
| **Total** | **170** | **51** | **30** | **185** | **49** | **26** |

Regarding 2003, the Accounting Officer stated that two audit reports were outstanding at 1 June 2006. These reports were due from an Auditor General and the delay was due to local factors. The office of the Auditor General concerned had not yet completed all audits in relation to the financial year ended 7 July 2004, which includes Irish Aid grants issued after 7 July 2003. The outstanding audits were currently in progress.

In regard to the risk to public funds, he informed me that development activities by their nature take place in a high-risk environment. There are delays in receiving certain types of partners' audit reports, but the effect of timing on the risk of misappropriation or irregularities is lower than might initially appear. Irish Aid line management is usually aware of the issues raised by an audit before the field work is fully completed.

He also stated that risk is minimised by the extensive management systems in place in Irish Aid to manage the aid programme. However, he stated that it must be acknowledged that on occasion delay does affect Irish Aid's reaction to audit issues and the ability to follow-up. Irish Aid responds in a number of ways

- Working with partners' line management to agree a programme of remedial action
- Withdrawing funding or temporarily withholding funding or part funding pending the implementation of reforms, including staff changes
- Working with partners to conduct detailed investigations.

**38** The source of these figures is the 2003 report. The 2004 report updated this coverage. Disclaimers are generally issued in situations where the auditee has failed to keep full and complete books of account.

39 Most qualifications in South Africa reports (9 in 2003, 8 in 2004) are in respect of income. As the organisations derive their income from voluntary donations, the income cannot be verified before it is entered in the accounting records. As this is the nature of the operation of such organisations, this qualification is not, in itself, a major concern to Irish Aid.

40 A number of auditors issued disclaimer opinions due to the hyperinflationary situation in Zimbabwe. These fully account for two of the adverse opinions in 2003 and for all three in 2004

## Consolidated Audit Report - Audit Findings

Audit findings are classified by EAU according to the level of seriousness

- Category A findings relate to major weaknesses in financial controls or a recurring issue that it is considered must be urgently addressed.
- Category B findings are important matters that will significantly improve the control environment, the accounting system or the operations of the entity but are not so serious or prevalent as to be considered major weaknesses.
- Category C are minor or isolated weaknesses that should nevertheless be addressed to improve the control environment, the accounting system or the operations of the entity.

Many findings are in respect of projects/programmes that are co-funded by Ireland with other donors.

Table 34 analyses the number of audit reports received and the related number of Category A findings by each aid supported country.

**Table 34 Analysis of Audit findings as classified within management letters (including internal audit reports and VFM studies)**

| Country | 2003 | | 2004 | |
|---|---|---|---|---|
| | No. of Reports Received | No. of Category A Findings | No. of Reports Received | No. of Category A Findings |
| Ethiopia | 12 | 16 | 28 | 7 |
| Lesotho | 37 | 32 | 23 | 36 |
| Mozambique | 30 | 46 | 36 | 51 |
| Tanzania | 28 | 62 | 34 | 64 |
| Timor Leste | 2 | 4 | 2 | 1 |
| Uganda | 9 | 16 | 27 | 16 |
| Zambia | 53 | 24 | 74 | 38 |
| South Africa | 24 | 9 | 14 | 2 |
| Zimbabwe | 6 | 2 | 5 | 3 |
| **Total**[41] | **201** | **211** | **243** | **218** |

In regard to the nature of the Category A findings, the following are examples of some of the more common themes noted

- Lack of supporting documentation for expenditure
- No tendering for contracts or comparative quotations for purchases

[41] These overall totals are greater than those shown in Table 4 because they include Internal Audit Reports and VFM Studies in addition to audit opinions.

- Expenditure not always authorised
- Use of funds for other than intended purposes
- Weak internal controls
- Long outstanding unsettled advances
- Stores discrepancies.

I enquired what the Department's approach was to the management of Category A findings disclosed in the audit reports and as to how the Department can ensure that the appropriate action in these cases is timely and relevant given the delays in the Department becoming aware of them.

In reply, the Accounting Officer stated that the follow-up to partners' audit reports is about addressing issues arising in third parties that have received Irish funding and funds from other donors, and this affects the nature of that follow-up. He stated that all of the programmes are implemented in partnership with developing countries and other donor countries and follow-up is conducted in this context. Follow-up with partners is aimed at the strategic level, with the intention of improving the overall financial management and accountability of the partners.

He also stated that working with other donors to support the implementation of ongoing public sector financial management and administrative reform processes is the key to rectifying many of the issues identified in audit reports. In addition, the joint donor/government coordination committees that exist in programme countries are also a platform for follow-up actions to audit and other programme issues. In non-governmental partners, the follow-up is usually via discussion between Irish Aid and the partners' senior management. All audit reports on partners commissioned by Irish Aid and the reports of most Auditors General include follow-up on the issues raised in the previous year's audits.

He informed me that Irish Aid's approach to the Category A issues arising in the programme varies depending on the particular structure and type of programme and the level of influence Irish Aid can bring to bear. The ranking system was introduced so that Category A issues could be clearly identified and could be emphasised by line management in follow-up. This is particularly important when the line managers do not have a financial background. The intention of the ranking is to assist them to identify the key areas to focus their follow-up efforts. The ranking should assist line managers to check that they have already identified the key issues arising from the underlying individual audit reports that would have been available to line management for some time.

He further stated that, in many cases, Ireland is a contributor to programmes along with many other donors who share information and work closely together. In such programmes, each donor does not conduct individual follow-up, but rather a lead donor is designated to take primary responsibility for the programme. In such cases, it is the lead donor who is responsible for following up on audits on behalf of all donors and sharing information on actions taken.

In this context, the follow-up to each partner's qualified audit reports is different, but influenced by

- The nature of the aid in question and the corresponding donor/government management structures
- The amount of expenditure in the programme from all donors and government
- The strategic importance of the programme/project
- The timeframe of the programme
- The partner's line management's ability to implement a programme of action.

## Risk Assessment and Value for Money

I enquired if a risk assessment of overseas projects had been carried out and, if so, what was the outcome in terms of risk identification and management. In reply, the Accounting Officer stated that the PAEG approval process is a comprehensive appraisal system to which all country aid programmes are subjected to test for quality, poverty focus, sustainability and adherence to policy priorities. In addition to the PAEG system, a specific example of the outcome of the introduction of risk assessment methodology in Irish Aid is the inclusion of a section on risks in the quarterly reports submitted by the programme countries to Departmental headquarters.

He also stated that the wider international donor community carries out a wide range of assessments, which include risk analyses, and these studies are utilised by Irish Aid. At a national partner Government level, these assessments are usually led by the IMF/World Bank using formal tools that have gained international acceptance. Most developing country partners do not yet have sophisticated and effective risk management and mitigation systems integrated into their own internal management systems. An important objective of the donor community (including Ireland) in working together with partner Governments through national plans is to develop all aspects of public sector performance, including risk management. He added that progress varies from country to country and significant challenges remain.

Finally, I asked how many value for money reports had been completed or planned since 2003. In reply, the Accounting Officer stated that Irish Aid has completed six value for money studies since 2003, two were currently in progress and at least one is planned for 2007. He also stated that Irish Aid is engaged in value for money studies via the Expenditure Review Initiative of the Department of Finance.

# Chapter 9

# Department of Communications, Marine and Natural Resources

# 9.1 Irish National Seabed Survey

## Background

A number of limited seabed studies have been carried out over the years including a survey commissioned by the Petroleum Affairs Division (PAD) of the Department of Communications, Marine and Natural Resources (DCMNR) in 1995/6. The PAD survey covered an area of 231,000 sq km. These studies produced fragmented information on the Irish seabed area.

In April 1999 the Government approved a proposal to undertake a complete survey of the entire Irish seabed at a cost of €26.3m over a period of 7 years. The memorandum submitted stated that Ireland claimed an area of greater than 850,000 sq km. Overall responsibility for the management and direction of the survey, named the Irish National Seabed Survey (INSS), was assigned to the Geological Survey of Ireland (GSI). The INSS project ceased at the end of 2005. As the survey work completed did not cover the whole of the Irish seabed area, the Government, in November 2005, adopted as national policy, a new programme entitled Integrated Mapping for the Sustainable Development of Ireland's Marine Resource (INFOMAR), designed to complete the seabed survey. INFOMAR is expected to take a further 20 years and the cost was estimated in 2005 by DCMNR to be €80m.

## Cost

The revised approved INSS budget was set at €33m. Total expenditure on the project amounted to €34.4m as detailed in Table 35.

**Table 35 INSS Expenditure 1999-2005 (€,000)**

| | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | Total |
|---|---|---|---|---|---|---|---|---|
| GSI | 74 | 5,547 | 9,581 | 2,572 | 2,013 | 835 | 835 | 21,457 |
| Marine Institute | nil | nil | nil | 2,390 | 3,429 | 3,679 | 3,405 | 12,903 |
| **Total** | **74** | **5,547** | **9,581** | **4,962** | **5,442** | **4,514** | **4,240** | **34,360** |

The main components of GSI expenditure were survey work contract payments, consultancy and IT equipment while Marine Institute (MI) expenditure mainly comprised operating costs of 2 research vessels and equipment.

## Project Monitoring

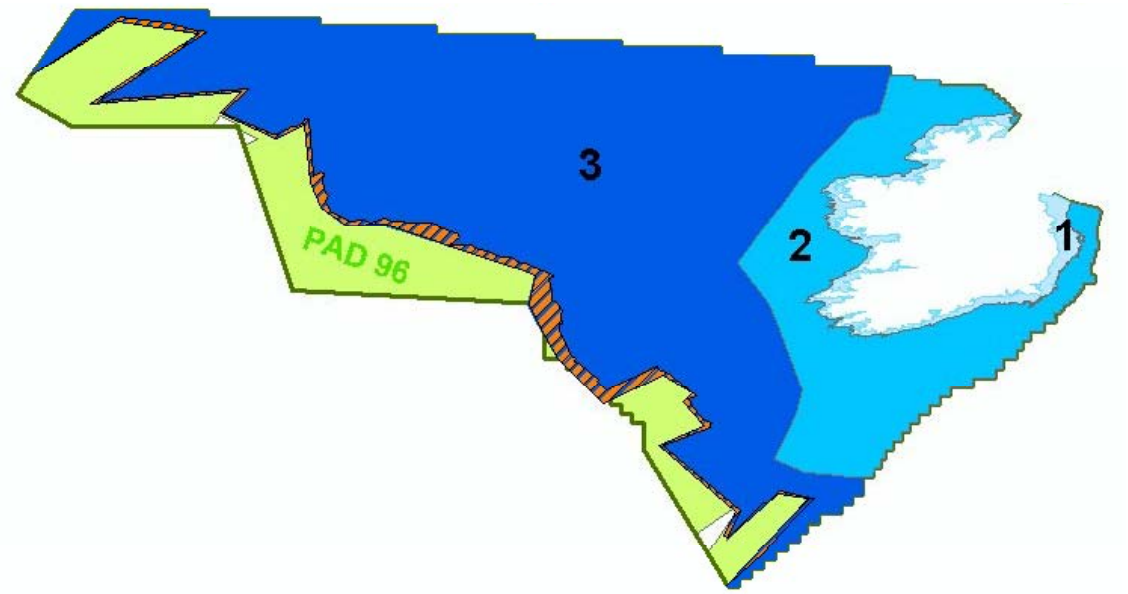
A Steering Group had responsibility for the direction and monitoring of the project. It comprised representatives of the Departments of Public Enterprise (DPE), Marine and Natural Resources, Finance, GSI and the MI. It met regularly and considered project progress reports and financial updates. In September 2003, some time after the transfer of DPE functions to DCMNR and internal re-organisation within DCMNR, meetings of the Steering Group ceased. Subsequently, the project and future strategy, as outlined in INFOMAR, were handled by a committee consisting of representatives of DCMNR, GSI and MI.

A Seabed Advisory Committee comprising representatives of various Government Departments together with representatives of MI, GSI, National University of Ireland (Galway) and University College Dublin was also established in June 1999 to provide technical advice.

A memorandum of understanding, signed in 2000, confirmed GSI's responsibility for achieving the deliverables of the project while MI was to play a key role in supporting the sustainable development of Ireland's marine resources.

Following Government approval, scientific and management consultants were engaged in 1999.

## Map of Zones[42]




- Zone 1 – water depths are less than 50 metres
- Zone 2 – water depths range between 50 and 200 metres
- Zone 3 – water depths greater than 200 metres

## Project Revision

Soon after the project started the Steering Group decided to postpone for at least a year any decision to undertake surveying in Zone 1.

GSI records of August 2001, while acknowledging that the memorandum to Government envisaged the survey covering the entire Irish seabed, state that it soon became obvious that this was not feasible. The major reason given was that shipboard surveying in shallow waters would be prohibitively expensive.

The scientific consultants also warned that the cost of surveying Zone 2 would be considerably higher than had been originally envisaged in the submission to Government. They advised in December 1999 that a total survey of the Irish seabed, on which the original Government decision was based, could not be achieved within the allocated funding. It therefore became necessary to prioritise survey work within Zone 2 as work on all of the Zone could not be completed. The Steering Group did not revert to Government with this new information despite its consequences for the scope of the project.

[42] Not to scale

Ultimately, 12.6% of Zone 1, 22% of Zone 2 and 96% of Zone 3 were surveyed under INSS.

The Accounting Officer informed me that the area surveyed totalled 453,046 sq. kms. This figure includes a 10% overlap within the originally surveyed PAD area for harmonisation purposes.

In relation to the decisions to exclude most of Zone 1 and some of Zone 2 from the survey, he stated that the key issue was whether or not the inshore area (Zone 1) was an integral part of INSS. If it was, then the cost and timescale of the project were seriously underestimated. He stated that it is the GSI view that Zone 1 was never intended to be surveyed as part of INSS. He did however, state that the 1999 Government memorandum and supporting documents were not explicit on this and that there had evidently been a lack of clarity in the language used to describe the area to be surveyed. However, the 2005 Government memorandum states that the Government agreed in 1999 that the State should undertake a comprehensive survey of the Irish seabed from the shore out.

He stated that the Steering Group met both sets of consultants in November 1999 and, *inter alia*, concluded that the inclusion of the nearshore area in INSS would be considered at a later stage. A few days later the Steering Group decided that the extent of surveying in 0-50 metres water depths would be determined after the end of year 1. In his view the straightforward conclusion from this was that the inshore Zone 1 was excluded from INSS until it was decided to the contrary.

He stated that the underestimation of costs in Zone 2 was another factor in the change in direction of the project. The Government memorandum itself had specified the need to undertake a detailed design and planning exercise and it was precisely this exercise that highlighted the need for significantly greater line density in Zone 2 – the major factor in increasing costs over those estimated in the memorandum. The lack of experience of this pioneering survey technology was fully anticipated and acknowledged in the memorandum. It was, of course, realised that surveying costs per unit area would increase with decreasing water depth. But the relationship between cost and water depth was not a simple linear one. The scientific consultants could not resolve the large difference between their relatively high costs of surveying in Zone 2 and those estimated for the original memorandum to Government. The Accounting Officer also informed me that some coverage of Zone 1 did occur (i.e Shannon, Cork, Dublin, Clew, Killala, Mulroy Bays, Dun Laoghaire and Killary Harbours as well as inshore areas in the Irish Sea) that reduced coverage in Zone 2.

He felt it was unfair to criticise the project management for responsibly reacting to the best available international design advice and taking the opportunistic course of action, through the Steering Group, to cut its cloth according to measure. While the Steering Group did not revert to Government with these significant changes to INSS, GSI understood that reports were tabled at Cabinet along with a briefing outlining the main strategic changes. He stated that it was not seen as prudent to seek additional funding in advance of demonstrating some real success in managing the available resources.

He was of the opinion that the planning of the project was comprehensive and properly conducted. A seabed mapping project on this scale had not previously been attempted anywhere worldwide.

He stated that current thinking was that it would be preferable to complete INFOMAR by the end of 2013, which would correspond with the end of the forthcoming National Development Plan. As a result, the period for completing the overall seabed work would be considerably shortened. The final decision will be one for Government.

# Procurement

GSI awarded a contract for survey work in Zone 3 for an amount of €10.3m in June 2000.

In September 2001, GSI agreed to retrospectively pay the company an amount of €635,000 in respect of additional survey work carried out in 2000 and 2001, but not previously notified. This work was carried out in Zones 1 and 2 en route to Zone 3, in which location the company's work under the contract was exclusively based. No details of the basis for the computation of the amount were retained.

I queried the basis on which this payment was made. In reply the Accounting Officer informed me that an amendment to the contract provided for additional payment in respect of surveying in parts of Zone 3 and the adjacent areas of Zones 1 and 2. The invoiced cost was calculated using the rates and prices set out in the contract. He acknowledged that the results of the work had not been initially notified. However, GSI had assured him that the work was properly authorised, that it was satisfied payment was justified and that comprehensive and satisfactory work results were subsequently lodged.

# Project Management

The Department noted a deteriorating relationship between GSI and MI, evident at strategy, policy and operational levels in the course of the INSS project. It was of the opinion that both project credibility and value for money was at risk. Such was the extent of the difficulties that the Department engaged a mediator to advise on a resolution. As a result, a revised memorandum of understanding was agreed between the bodies in 2004 and new administrative arrangements were put in place. These included a new joint working group with a Departmental official acting as observer.

Internal audit reported that project management controls were not in place or were not applied in relation to INSS and also concluded that the suggested governance structure for INFOMAR fell short of best practice for such projects. It recommended that strict budgetary and project management controls be put in place to prevent overruns such as occurred on the INSS project.

The Accounting Officer informed me that GSI INFOMAR expenditures are being managed through the Departmental financial management system which tracks all transactions against assigned budget subheads. Once budgets are set in the system, cost overruns are not permitted. The GSI project manager reviews outturns monthly. There is close coordination with the MI project manager on all operational matters. He also stated that a Steering Committee under the chairmanship of a senior Departmental official, to which the joint MI/GSI project management team reports, will monitor progress on INFOMAR and the achievement of its deliverables to specification and on time.

# Conclusion

The INSS project did not succeed in covering a substantial part of the area envisaged and there will be a significant cost to the State to complete a survey of the claimed Irish seabed area. Despite the fact that there was a major change in the scope of the project this was never formally communicated to the Government.

# 9.2 Payments to the Broadcasting Commission of Ireland

## Background

In December 2002 the Minister for Communications, Marine and Natural Resources (the Minister) announced that the Government had approved a new framework for public service broadcasting including an increase in the television licence fee from €107 to €150. He indicated that 5% of the net proceeds of the new fee was to be ring fenced as a special broadcasting fund for new, additional, innovative content, from which all free-to-air broadcasters could draw. The Minister said he expected the fund to amount to €8m annually and that legislation would be necessary to give effect to the changes.

The Broadcasting (Funding) Act, 2003, (the Act), was signed into law on 23 December 2003. The Act requires the Broadcasting Commission of Ireland (BCI) to

- prepare a scheme or schemes for the funding of grants to support certain television and radio programmes and projects, for example, to improve adult literacy
- to submit a scheme or schemes to the Minister for approval
- carry out the terms of the scheme.

Section 4(2) of the Act states that

*The Minister, with the approval of the Minister for Finance, may pay to the Commission out of moneys provided by the Oireachtas for the purposes of grants under a scheme and any administration of or reasonable expenses relating to a scheme, in respect of each financial year, after the financial year ending on 31 December 2002, an amount being equal to 5 per cent of net receipts in that year in respect of broadcasting licence fees.*

It is noteworthy that the Act provides for the preparation and approval of a scheme or schemes to allow BCI to finance particular types of programmes as distinct from the establishment of a fund for the receipt and accumulation of resources from which programmes of the kind specified in the Act might be financed.

The BCI submitted a draft Broadcasting Funding Scheme to the Minister on 8 December 2004 for his approval. In accordance with the provisions of EU Regulations 659/1999 and 794/2004, Ireland notified the European Commission of the draft Scheme on 28 April 2005 to ensure that the Scheme was compatible with the relevant provisions of the EU treaty. The European Commission replied on 5 October 2005 indicating that it had decided not to raise any objections to the Scheme. The Minister approved the Scheme on 13 October 2005.

Payments totalling €25,858,395 were made to BCI up to 31 December 2005 on foot of Section 4(2) of the Act as follows: 2003 - €8,342,727, 2004 - €8,451,025, 2005 - €9,064,643.

Prior to 13 October 2005, the date on which the Minister formally approved the Scheme, a total of €23,366,806 was paid by the Department to BCI relying on Section 4(2) of the Act for authority to make payment.

No payments were made by BCI to programme makers under the terms of the Scheme by 31 December 2005.

# Audit Concerns

I was concerned that there was no legal basis for payments made from the Vote to BCI prior to the formal approval of a scheme by the Minister on 13 October 2005. I was also concerned as to why payments continued to be made to BCI subsequent to the Minister's approval of a scheme in view of the accumulated surplus on hands and available to BCI. I sought the views of the Accounting Officer on these matters.

# Accounting Officer's Response

The Accounting Officer informed me that the Department had interpreted the Broadcasting Funding Act, 2003 on the basis that, on its enactment, it provided for the immediate establishment of a Broadcasting Fund to which 5 per cent of net receipts from television licence fees would be paid each year. He stated that the Department was of the opinion that the intent of the Bill, introduced to give effect to the Government decision to establish the Fund, was for the immediate establishment of a Fund while a scheme or schemes were being developed. He also stated that, if the Department had not paid these amounts to the BCI in respect of the Fund, the Department would have been required by law to pay these moneys to RTÉ in accordance with Section 8(a) of the Broadcasting Authority (Amendment) Act 1976. In arriving at this opinion, the Department considered the Broadcasting (Funding) Act 2003 and associated papers that were prepared in advance of the drafting of the Bill.

He also felt that the fact that the legislation, which was only enacted in late December 2003, provided that 5 per cent of the net proceeds of television licence fees for 2003 could be paid into the Fund underpinned the Department's interpretation of the legislation. He felt it was evident that a scheme could not have been developed by BCI, cleared with the EU Commission and approved by the Minister in the remaining days of 2003.

In summary, he stated that the Department was of the view that the Broadcasting (Funding) Act 2003 established a Broadcasting Fund to which 5 per cent of the licence fee would be allocated year on year from 2003 onwards and that this Fund would be accessed by a scheme or schemes to be developed by BCI. The Department had interpreted the legislation as providing that payments should be made to the Fund in the period leading up to the approval of the first scheme and that payments would also continue in any future period where a scheme had been withdrawn and a new scheme was being developed.

He informed me that, following initial queries raised by my Office in relation to this interpretation of the Act earlier in the year, legal advice was sought. The advice received appeared to cast doubt on the Department's interpretation of the Act and also suggested that the provisions of the Act dealing with the payment of moneys were not as detailed as they might have been. The Accounting Officer concluded by saying that the matter was being reconsidered in consultation with the Department of Finance.

# Chapter 10

# Department of Agriculture and Food

# 10.1 Single Payment System

## Background

The Single Payment System (SPS) was introduced in 2005 as part of the new measures agreed to reform the Common Agricultural Policy. It changed radically the basis on which payments are made to farmers by decoupling payment and production and consolidating a range of scheme-based payments into one single payment. It also required the development of a range of new business processes by the Department of Agriculture and Food (the Department) and significant personnel and organisational changes.

With effect from 1 January 2005 the SPS replaced various cattle, sheep and arable aid support schemes. Most schemes were fully decoupled from production with effect from 1 January 2005. The exceptions were dairy premium introduced in 2004 and fully decoupled since 31 March 2005, and the dried fodder scheme, which has been partially decoupled (50%) to date.

In view of the radical changes involved in the introduction of the SPS my staff undertook a high level review of the processes and procedures adopted by the Department to manage the new environment.

## Implementation of the SPS

The regulatory framework governing the SPS is EU Regulation 1782/2003. In addition EU Regulation 795/2004 lays down the detailed rules for the implementation of 1782/2003 while EU Regulation 796/2004 details the rules for the implementation of cross compliance, modulation and the integrated administration and control system provided for in 1782/2003.

There is no national legislation implementing the SPS. It has been implemented by way of Ministerial Decision, as were the schemes it has replaced.

The EU regulations gave countries a choice of implementing the new system between 2005 and 2007 and of initially opting for full or partial decoupling. Ireland was the first country to opt for full decoupling and opted, per Government decision, to begin issuing SPS payments from 1 December 2005, the earliest date allowed.

The SPS is applicable to farmers who actively farmed during all or any of the three reference years – 2000 to 2002 - and who were paid livestock premium and/or arable aid in one or more of those years and who will farm, or whose successors will farm, in 2005.

The Department, in its role as Paying Agency on behalf of the EU, has the same responsibilities for administration and for exercising financial control, in regard to the SPS, as it had for the previous schemes.

The Department had developed and managed a sophisticated information and communications technology (ICT) environment over many years. The SPS required the calculation of each farmer's entitlement, based on the unique history of the farm over the reference period 2000-2002, and the processing of over 140,000 SPS applications for payment by December 2005. The Department had a relatively short period of time from the Government announcement in October 2003 in which to acquire the necessary ICT systems. It approached the task in a pragmatic way by the extension of some relevant existing IT contracts and by open tendering for other elements of the system. Total development costs to end 2005 were almost €5m with additional costs of approximately €2.7m expected in 2006 for support, maintenance and change requests.

# National Reserve

A National Reserve was established in accordance with EU Regulation 1782/2003. This is a fund created to compensate farmers, by way of new entitlements or a top-up on existing entitlements, for disadvantages arising in their specific circumstances from the introduction of the SPS. The National Reserve can be financed by a deduction from entitlements of up to 3%. The actual deduction was applied at a rate of 1.82% and so a National Reserve of €22.7m was created. An amount equal to the value of unclaimed entitlements is also transferable to the Reserve. The Department estimates that some €5m will be credited to the National Reserve from entitlements that were not activated in 2005.

Defined categories of farmers are automatically entitled to apply for an allocation of entitlements from the Reserve. To date some €12.4m has been allocated to successful applicants under the 2005 National Reserve. Farmers who receive new entitlements from the Reserve may not sell, lease out or otherwise transfer (except in cases of inheritance or gift), any of the entitlements that they receive from the Reserve for a period of 5 years starting from the year of allocation.

# Deductions and National Ceiling

Under the EU legislation governing the SPS, there is a national ceiling for the total value of entitlements for each of the years to 2012. Ireland's national payments ceiling for 2005 was initially €1,136m but was subsequently increased to €1,260m by Commission Regulation 118/2005 to take account of the deferred inclusion of the Dairy Premium scheme in the SPS in 2005. Under the regulation, this ceiling cannot be exceeded and, if necessary, a linear reduction must be applied to entitlements to ensure compliance. In the event the sum of entitlements established for farmers exceeded the ceiling by some 1.18% and it was necessary to apply a linear reduction amounting to some €15.1m.

Entitlements are also reduced for modulation – a process whereby funds are diverted from the SPS to rural development measures. The modulation reduction in 2005 was 3% and this will be increased to 4% in 2006 and 5% from 2007 onwards. A refund of the modulation reduction applied to the first €5,000 of each farmer's entitlement will be issued in 2006 as provided for in the regulation. In practice this will amount to a maximum of €150 per farmer payable in 2006.

I asked the Accounting Officer how the Department would ensure that the National Ceiling for 2005 was not exceeded in light of the payments made to date, the deductions made for the National Reserve and modulation payments yet to be made in respect of applications not yet processed.

In reply he informed me that, as the National Ceiling is €1,260m and the reduction for the National Reserve was €22.7m, the amount available for payments in respect of 2005 was therefore €1,237.3m. The total amount paid to June 2006 (excluding payments from the National Reserve) was €1,160.3m, net of modulation at 3%. The total spend to date (including modulation payments of €34.7m) is therefore €1,195m.

He stated that the Department was satisfied that the payments made under the 2005 SPS would not exceed the National Ceiling because of the preventative action taken and various controls implemented as part of the payment process.

# 2005 SPS Payments

The SPS entitlement is calculated using the average number of livestock (hectares in the case of arable aid schemes) on which payment was made under each scheme in the reference years 2000 to 2002, multiplied by the 2002 payment rate for that scheme.

In the course of my examination of the new system I carried out a test check of the calculation of entitlements and their payment. This proved satisfactory.

Some 118,000 payments were made in December 2005 totalling approximately €1,058.6m (net of 3% National Reserve and 3% modulation reductions). All applications processed for payment in December 2005 were paid. However, approximately 10,000 farmers received no payment then as their applications had not been finalised. At the time of audit examination this number had been reduced to approximately 3,000.

The Accounting Officer informed me that 8,565 payments amounting to €85.7m in respect of 2005, excluding payments out of the National Reserve, were made in the period January to June 2006. A further €27.4m of supplementary payments, including National Reserve payments, was paid to 10,396 farmers in the same period. He also informed me that, at the end of June 2006, there were approximately 900 applicants, under the 2005 SPS, who had not been paid. A small number of other applicants would also become eligible following the processing of their application to transfer entitlements to them.

In the course of my examination I noted that a reconciliation had not been carried out between the total payments recorded on the SPS system in December 2005 and the SPS payments shown in the SAP accounting system. The Accounting Officer has informed me that the reconciliation has since been completed.

# Force Majeure

Farmers who felt that their production was adversely affected by exceptional circumstances during some or all of the reference period (2000-2002) could claim force majeure. If the claim was accepted, the years in which production was adversely affected were excluded from the reference years in calculating entitlements. Where it was accepted that such circumstances arose during all of the reference years, the Department could use the period 1997-1999 as an alternative reference period. Examples of force majeure would be death or long-term incapacity of a farmer.

The European Commission conducted an examination in 2005 of force majeure claims and in their findings commented that the Irish authorities, in examining such cases, did not fix clear percentages to measure dips in production and recommended the introduction of a coherence test to ensure that all claimants were treated in the same way. The Commission's opinion resulting from their examination was that the Department might not have fully complied with the regulations.

In response, the Department stated that the objectives of article 40 of 1782/2003, the article dealing with force majeure, would not have been met if it were decided to fix clear percentages to measure reduction in production. It also stated that in every single application the circumstances put forward by the applicant were carefully examined to determine whether or not such circumstances satisfied the criteria for force majeure/exceptional circumstances. This was done by insisting on full documentary evidence such as death certificates or medical evidence. Having satisfied itself that the circumstances put forward, whether occurring during or before the reference period, could give rise to a dip in production, the Department examined each case to determine if, in fact, a dip in production actually occurred in one or more of the reference years. Departmental databases allowed for the examination of the patterns of production. In conclusion, it was stated that the Department was satisfied that its implementation of the article was in accordance with the provisions of that article and was the most equitable way of dealing with applications.

In 2005 the overall number of force majeure applications was 17,592. Of these 4,266 (including those allowed at appeal, etc) were accepted for payment and the number rejected was 13,326. The total paid on the 4,266 cases was €51.9m and the force majeure element of this sum was €8.5m.

# Appeals Committee

An Appeals Committee was established by the Minister for Agriculture and Food in February 2004 to review the cases of farmers who were not satisfied with the Department's decisions in relation to their SPS entitlements.

Up to June 2006, a total of 4,943 appeals were considered. 509 appeals were upheld, 4,287 were not, 44 were deemed to be invalid and 103 had not been finalised. Applicants in 64 cases not upheld have complained to the Office of the Ombudsman. Following review, the Department has changed decisions in eight of these cases, often in light of further information.

Since March 2006, the Appeals Committee is also considering appeals in relation to the allocation of entitlements from the National Reserve. Some 900 such appeals have been lodged with the Appeals Committee but, as at the end of June 2006, no decisions have yet been made by the Committee.

# Cross Compliance

Under cross compliance requirements, a farmer receiving a SPS payment must implement the various Statutory Management Requirements (SMRs) set down in EU legislation on the environment, food safety, animal health and welfare and plant health and must maintain the farm in good agricultural and environmental condition (GAEC). Seven cross compliance SMRs were introduced in 2005 together with the GAEC requirements for Ireland. A further eight SMRs, including the Nitrates Directive, were implemented in Ireland in 2006 while a further three are to be introduced with effect from 1 January 2007.

For farmers selected for inspection, there are two types of checks carried out for the purpose of implementing the SPS - eligibility checks and cross compliance checks. Eligibility checks verify the accuracy of areas being farmed and claimed for. It is a requirement that all eligibility checks are completed prior to payment. There are two types of inspections – ground (on-site) and remote sensing by satellite. It is an EU requirement that eligibility checks be carried out on 5% of farmers applying for the SPS.

A Commission audit of cross compliance was carried out during 2005 which raised a number of issues on the method used to select farms for inspections and the level of sanctions imposed on non-compliant farmers. The Commission auditors had further comments on weightings applied to the cases of non-compliance, application of sanctions and tables and instructions used for inspecting various SMRs.

A number of the audit comments were accepted by the Department in January 2006 and, as a consequence, some changes have been made. I enquired what implications these had for the number of cross compliance inspections required to be carried out and the number of inspection staff. The Accounting Officer informed me that the inspection visits are integrated with eligibility inspections with a view to ensuring, as far as possible, that only one visit was made to each farm. In this context, inspections under the Disadvantaged Areas' Compensatory Allowance scheme were also integrated with the eligibility and cross-compliance inspections under the SPS. The consequence of the introduction of the revised risk analysis model was that, while the number of farm visits will be reduced by 2,000 visits, the time spent on each farm will be significantly increased as inspection report forms will have to be completed in respect of each SMR necessitating an inspection of the total farm by the inspection staff.

# Conclusions

The introduction of the SPS marks the single biggest change in the operation of the Common Agricultural Policy since its inception over 30 years ago. The Department faced major challenges in determining farmers' entitlements under the new system and making, what are in effect, key income support payments to the individuals concerned by the December 2005 deadline. This had to be done in accordance with complex EU regulations and subject to rigorous EU scrutiny. The evidence available so far suggests that the Department planned its approach to these tasks in a strategic manner and implemented them in a pragmatic and generally satisfactory way.

# 10.2 Staff Savings

It was anticipated at an early stage that the introduction of the SPS would lead to significant staff savings in the Department. The savings were expected to arise, as the full decoupling of farm support payments from production and the associated rationalisation of farm income support schemes would require less administrative effort. It was also anticipated that the staff savings would be partly offset by an increased level of controls linked to the introduction of cross compliance under the SPS.

Correspondence with the Department of Finance in April 2005 indicated that the Department felt it would be able to operate with some 400 less staff. The breakdown of the 400 was

- 250 local office staff
- 100 staff from the Department's office in Castlebar
- 50 staff from the area aid division in Dublin.

It was noted that, as of April 2006, local office staff numbers had been reduced by 152. This was achieved through 35 internal transfers within the Department and the departure of 117 staff from the Department - mainly through transfer to other Government departments, retirements and career breaks. It was also noted that 56 staff from the Castlebar office had transferred to the Department of Justice (Garda Information Services Centre). As it was expected that area aid staff would be required to administer SPS for the remainder of 2006, no reductions had been made in this area.

In September 2005 the Department commenced a review of District Veterinary Office (DVO) staffing levels. The review was carried out in the context of falling disease levels and efficiencies arising from the introduction of the new Animal Health Computer System (AHCS). The review report, issued in March 2006, found that some 115 less staff would be required in the local DVOs.

It was therefore estimated that the Department could make total staff savings of 515 in the relevant areas. As actual transfers out of the Department to April 2006 were 173, savings yet to be made at that stage amounted to 342.

I asked the Accounting Officer

- How many staff had worked on schemes replaced by the SPS?
- What measures were taken by the Department to ensure that these staff were redeployed as quickly as possible? In the meantime what measures had the Department taken to ensure that all of these staff were gainfully employed?
- What difficulties had been experienced by the Department in relocating staff where alternative local relocation opportunities were not available and how had these been overcome?
- Had the Department experienced particular difficulties in relocating or redeploying technical staff such as veterinary staff and, if so, how did the Department propose to address the difficulties?
- When was it expected that the anticipated staff savings of 115 in the DVOs would be achieved?

The Accounting Officer informed me that, in all, some 400 administrative, 185 technical agricultural and 12 inspectorate staff worked on schemes replaced by the SPS. He stated that the Department had worked closely with the Department of Finance, other Departments and also with staff associations with a view to redeploying surplus staff. Apart from the 50 administrative staff in the Area Aid unit, who were still an integral part of the SPS operation and not yet available for redeployment, approximately 250 of the balance of the 350 administrative staff had been accounted for, by the end of June 2006, through redeployment, natural wastage, promotion etc.

He further stated that his Department, with the assistance of the Department of Finance, had facilitated the possibility of temporary blocks of work being transferred from other Departments to Departmental locations where alternative local relocation opportunities were not available. The Department of the Environment, for example, had availed of the surplus Departmental staff in Ballybay. In other offices, surplus staff, because of their experience with the previous schemes, were working on certain measures relating to the continuing implementation of the SPS.

He informed me that it was not yet clear how many technical/inspectorate staff would be surplus, if any. While the number of annual inspections had decreased, the complexity had increased, particularly with the introduction of a range of cross compliance and environmental measures. To date, the Department had concentrated on the redeployment of surplus administrative staff but intended to review the situation regarding technical/inspectorate staff in the near future.

Finally he stated that the rate at which staff could be redeployed from DVOs was dependent on the number of vacancies arising in other Departments or offices in the same geographical location.

# Conclusions

Issues associated with re-organisation and re-deployment of staff affected by the introduction of the SPS might fairly be described as work in progress. The Accounting Officer makes it clear that these issues must be advanced in conjunction with the Department of Finance, staff representatives and indeed other Departments and agencies who may have a need for staff in locations where Department of Agriculture and Food staff are no longer required as a result of the introduction of the SPS. While this is no doubt the case, there remains a pressing need to ensure that professional, technical and administrative staff formerly working on schemes now replaced by the SPS are deployed in the most efficient and effective way possible in the new environment.

# Chapter 11

# Department of Transport

# 11.1 Integrated Ticketing System

## Background

The Transport (Railway Infrastructure) Act, 2001 provided for the establishment of the Railway Procurement Agency (RPA). This agency's original remit was to secure the provision of, or to provide, such light railway and metro infrastructure as might be determined from time to time by the Minister for Transport. In March 2002 its remit was extended, by Statutory Instrument 84/2002, to give it a mandate for the delivery of a multi-operator system of integrated public transport ticketing using smart card technology, with initial deployment in the Dublin area. Pending the establishment of a transport regulatory body, the RPA was given responsibility for procuring the integrated ticketing system as, in the view of the Department of Transport (the Department), it had no direct responsibility for providing transport services and, thus, any concerns about the project being captured by an existing operator and causing difficulties as regards competition issues would be avoided.

## Project Outline and Budget

In 2002, the RPA prepared a budget and a four year plan – 2002 to 2005 – with 4 distinct phases for delivery of the project. The original budget was set at €29.6m. In late 2004, the RPA indicated that the delivery date had been revised to 2006 and that costs could still be met from the agreed budget of €29.6m. In January 2006, the RPA submitted proposals for a revised budget with an upper limit of €42.7m, the final amount to be determined on the basis of the amount of Exchequer contributions to be made towards operators' capital costs. The key reasons given for the increase in the budget were the longer implementation period, the consequential need for retention of the project team and management for an additional two years, along with the proposals in relation to the amount of the capital contributions to be paid to operators. A revised budget has yet to be agreed and in this regard the Minister awaits the forthcoming report of the integrated ticketing project board on the agreed scope, timelines and budget for the phased completion of the integrated ticketing project.

The 4 phases of the plan were

- Establishment including appraisal
- Design/specification including public consultation
- Procurement
- Implementation augmented at strategic intervals by a number of important processes - public awareness campaign and proof of concept.

The RPA put together a dedicated expert in-house team for the delivery of the project.

## Overseeing the Project

Two committees were established to oversee its implementation. A monitoring committee, led by the Department, consisted of Department and RPA officials and a steering committee, led by the RPA and including representatives of transport organisations, the Department and other interested State agencies.

## Implementing the Project

Phases 1 and 2 were completed broadly in line with the original timeframe and budget. The proof of concept was also undertaken. However, there were problems with phase 3 – procurement - which commenced in April 2004 but was subsequently terminated in May 2005. The procurement process itself

was carried out in line with national and EU rules but no tenderer ultimately met the selection criteria. The complexity of the project, together with another State transport agency also seeking a similar system in the marketplace at that particular time, appears to have undermined the procurement process. The RPA subsequently informed the Department that the net additional cost of this unsuccessful procurement was €860,000 and had the effect of delaying the project by approximately a year.

## Suspension of Project

In light of the difficulties experienced with the project, the Department commissioned a consultancy report

- to review the approach to procurement
- to benchmark the costs of the system against other major smart card integrated ticketing systems
- to consider the deliverability of the benefits

prior to committing any further expenditure which, at 31 December 2005, had amounted to approximately €9.5m . This report was presented to the Department in April 2006.

The conclusions reached were that there was general agreement among the stakeholders that integrated ticketing was required in Dublin and that the procurement process should be continued. The report, however, stated that there was a general feeling of uncertainty over the future regulatory and institutional structure for transport in Dublin and this had had two significant impacts. Operators were unsure of the size and/or nature of their role in the public transport network of the future and were, therefore, unwilling to commit to a particular ticketing direction and the institutions to progress integrated ticketing were lacking. It stated that these uncertainties had led to two fundamental problems – private operators had largely withdrawn from the process and Dublin Bus and, to a lesser extent, Iarnrod Eireann were continuing to develop their own ticketing systems in parallel to maintain flexibility in the event of regulatory review requiring them to stand alone.

The report considered a number of options but firmly recommended proceeding with the project and stated that, with firmer governance, the project could be kept on time and budget.

The Department also commissioned a peer review of the project in line with the Government decision on the management of major ICT projects. This report noted a lack of unity of vision and purpose among the participating parties. It stated that discontinuing the project would incur further costs bringing total expenditure to approximately €13.5m. It also recommended that the project, as currently envisaged, should proceed and stressed that successful completion would depend on

- full agreement by all parties to the concept of integrated ticketing
- unity of vision and purpose in achieving this
- a willingness to forgo partisanship in favour of the project
- more effective project governance and management.

Both reviews looked at the options of abandoning the project, mothballing it, or continuing with it and both the resultant reports strongly recommended the continuance of the project, subject to new and enhanced governance arrangements being put in place. The Department considered these reports, in addition to taking account of its own analysis, and recommended to the Minister that the broad thrust of the recommendations be accepted.

In July 2006, the Minister formally advised the Government of his intention to proceed with the integrated ticketing project on the basis of the establishment of enhanced governance arrangements for the completion of the project. The Minister's intentions were noted by Government..

Details of the expenditure of €9.5m to the end of December 2005 are set out in Table 36.

**Table 36**

| | **€ m** |
|---|---|
| RPA | 4.7 |
| Systems design and development | 3.0 |
| Operator equipment contribution | 0.9 |
| Third party professional Fees | 0.7 |
| Marketing and branding | 0.1 |
| Market Research | 0.1 |
| **Total** | **9.5** |

Expenditure in the four years 2002 to 2005 was €0.3m, €1.9m, €4.9m and €2.4m respectively.

## Audit Concerns

As I was concerned that the way in which the project had been managed had led to the lack of progress and the incurring of substantial nugatory expenditure, I put a series of questions to the Accounting Officer.

## Governance

**To what extent was the unsatisfactory rate of progress attributable to the governance system employed?**

The Accounting Officer informed me that, until the initial public procurement process failed in May 2005, the project was reported by the RPA as within budget and it was not evident up to that point that the existing governance structure was incapable of delivering the project. There were a number of factors which contributed to the inconclusive procurement process. These included the relatively small scale of the system being procured by international standards, confusion over the role of the RPA and the other agencies within the system and the specialised nature of the services being sought. A further contributory factor appeared to be underlying tensions between RPA and the CIE companies, particularly Dublin Bus, which were becoming increasingly evident at that time. Department records showed that the process of seeking agreement with, and involving stakeholders in, the decision making process had become protracted. However, delivery of such a project in a multi-operator and multi-agency environment would always depend to a material extent on the co-operation of these agencies no matter what the governance arrangements or the available statutory powers.

She stated that the conclusion that enhanced governance structures were required arose directly from the Departmental review of the project following the failed procurement process in May 2005, protracted tripartite discussions between the Department and the chief executives of the RPA and Dublin Bus which took place between July 2005 and January 2006, the consultancy undertaken to review the project and the peer review undertaken in accordance with a Government Decision on the management of major ICT

projects. The governance system relied on agreement between the RPA, Dublin Bus, Bus Eireann, Iarnrod Eireann, the Department of Social and Family Affairs (DFSA) as well as the private bus operators and Luas. Revised governance arrangements for the project were introduced in July 2006 in the form of a new high level project board charged with the successful delivery of the smartcard technology required to deliver an integrated ticketing system within an agreed specification, timeline and budget.

The board would also consider such other technical scope and design issues as may be necessary to complete delivery of the smart card technology (e.g. technical design issues in relation to possible fare structures and levels, ticket products, revenue collection strategies, data requirements etc). Before a public transport operator could proceed with any of its own ticketing investment proposals, the operator would be required to satisfy the board that the proposed equipment was consistent with the integrated ticketing requirements.

The board comprises an independent chairperson, the chief executives of the RPA, Dublin Bus, Iarnrod Eireann, Bus Eireann, senior officials from the Department and, as appropriate, the DSFA and a representative of the private bus operators. The Minister has appointed a former Secretary-General as independent chairperson of the project board. The first meeting of the new Board took place in July 2006.

The board will be accountable to the Minister for Transport. It has been asked to formally report on progress to the Minister in September 2006 and every 3 months thereafter.

A project implementation team will be established, led by the RPA, to include the current RPA ticketing team and relevant personnel from Dublin Bus, Iarnrod Eireann, and Bus Eireann, private operators and, as appropriate, the DSFA. It will report to the project board and will be responsible for the day-to-day development and implementation of the project. Members of the project implementation team will, however, remain as employees of their own organisations throughout the duration of the project.

The Accounting Officer also informed me that the Department is reviewing the current mandate of the RPA and will amend the underlying Statutory Instrument, if appropriate, in order to give effect to the new arrangements.

She stated that the enhanced governance structure for the integrated ticketing project is designed to recognise the independent statutory role of the various stakeholders while ensuring a single focal point for all key decisions in relation to the integrated ticketing project.

She pointed out that the governance structure employed was intended to be interim in nature pending changes in public transport institutional arrangements. It was always recognised by the Department that the most appropriate locus for the project was in an independent transport regulatory body with statutory powers to govern the public transport market. This is being addressed by the Minister for Transport in the context of his proposals to establish the Dublin Transport Authority.

In the interim, the Minister wants to ensure that the project progresses as expeditiously as possible and that the benefits of expenditure to date are realised.

## Action Taken to Address Shortcomings

**What specific action was taken by the Department to address shortcomings in the interaction between the RPA and the CIE group of companies up to the end of 2005?**

The Accounting Officer stated that, from the outset of the project in 2002, the Department had monitored progress on the project between RPA and CIE. It hosted many meetings between the CIE subsidiaries and the RPA with a view to resolving specific issues on integrated ticketing as they arose. In addition to other correspondence from the Department, she had written to the Chairman of CIE in June

2004 seeking assurances that Dublin Bus, Bus Eireann and Iarnrod Eireann would be full participants in the integrated ticketing system under development by the RPA. The Minister also wrote to the Chairman of Dublin Bus in November 2004 regarding Dublin Bus's interim ticketing arrangements and again in March 2005 to clearly articulate public policy on integrated ticketing.

Following the abandonment of the procurement strategy in May 2005, the RPA presented a revised strategy to the Department in July 2005. The Department was reluctant to agree to the revised strategy until it was assured on the costings and the time frame for the project and until agreement had been reached between RPA and Dublin Bus on the way forward. The Department considered it essential that Dublin Bus, as the biggest public transport operator in Dublin, would be a fully committed participant to ensure the success of the integrated ticketing scheme.

To that end, tripartite talks were arranged in an attempt to resolve differences. In December 2005 agreement was reached on a way forward and formally signed off by the chairmen of CIE and the RPA in January 2006. The agreement covered a number of central issues including the development of a disposable smartcard for operation on Dublin Bus services as an interim step, the RPA to be the issuer of the disposable card with the agreement of Dublin Bus, the withdrawal of the disposable card within 12 months of the introduction of the integrated system, the testing of the software interface on a number of buses and the next steps to be taken by both parties.

Financial provisions were also included in the Memoranda of Understanding (MOU) agreed between the Department and the three CIE subsidiaries in 2005 and 2006.

## Imposition of Financial Sanctions

**Was any consideration given to the imposition of financial sanctions on the CIE group of companies in light of their perceived lack of commitment to the project?**

The Accounting Officer informed me that this was considered. She stated that the MOU on service levels and targets agreed between the Department and the CIE companies provide for subvention payments to be made to the companies. In relation to the integrated ticketing project, the MOU provide for a proportion of the payment to be contingent on cooperation with the integrated ticketing project.

The agreements for 2006 provide that payment be linked to satisfactory participation in the development of the multi–operator system of integrated ticketing. Payment would only be released if, in the opinion of the Department, the companies complied with the relevant conditions of the MOU.

The MOU for 2005 also made provision for the withholding of funds on the basis of compliance with the integrated ticketing project. The Department had written to CIE in December 2005 warning that certain payments associated with progress under this project would be recouped during 2006 if significant progress was not made during 2006. The Department would be making an assessment in due course whether there was sufficient evidence of commitment by the CIE companies to warrant not recouping these payments.

She stated that the CIE companies did not accept that there was or is a lack of commitment on their part to the integrated ticketing project.

## Financial Leverage

**Had the Department exercised the appropriate financial leverage to progress the project considering the substantial subsidies paid to State transport agencies?**

The Accounting Officer informed me that the peer review report, in its concluding remarks, noted inter alia that "a compelling case could be made to make the very substantial Exchequer investment in the

various modes of transport contingent on transport operators introducing the integrated ticketing project."

She stated that the Department acknowledged and accepted the point made by the report. However, the Department had to balance this with the impact on the travelling public and society generally of the withdrawal or deferral of public funds on the provision of public transport services provided by the State transport agencies. Any financial intervention of this kind which might be considered would, while clearly reflecting a lack of satisfaction with the commitment of the relevant CIE companies to the project, also have to be proportionate, have regard to the overall financial position of the relevant company and the CIE group and not result in a significant curtailment of services provided under public service obligations.

While the Department had made it very clear to the CIE companies that it would exercise the sanctions in the MOU in the event of default of their obligations under the MOU, the Department's main focus was to ensure that the integrated ticketing project was implemented as speedily as possible and to address the legitimate concerns of transport operators in that context. The new governance arrangements being put in place were designed to achieve this.

Nevertheless, the Department, in November 2005 and again in early 2006, had asked RPA to defer two payments claimed by Dublin Bus in relation to expenditure incurred by the company in procuring electronic ticketing machines. The claim arose from an agreement by the Department (and included in the project budget) to pay a grant towards the partial funding of the cost to Dublin Bus of electronic ticketing machines pending developments on integrated ticketing.

While the Department had initially agreed to the payment of the funds to Dublin Bus, in both cases the agreements were subsequently rescinded. Firstly in November 2005, the Department advised RPA to defer payment pending agreement being reached in the tripartite discussions. Secondly, in February 2006, the Department initially agreed to a payment by RPA claimed by Dublin Bus. However, before payment was made, the Accounting Officer had reviewed the project and, in light of the difficulties and delays experienced, initiated the immediate undertaking of the consultancy review and the peer review. She did not consider it appropriate to make the payments in question to Dublin Bus pending the outcome of both reviews and clarity regarding the future approach to the project.

She stated that these payments are still outstanding and she would be considering whether to release them in light of the decision to proceed with the project and progress under the new arrangements now being put in place.

## Nugatory Expenditure

**To what extent had nugatory expenditure been incurred on the project to date, and specifically, on the procurement process discontinued in 2005?**

The Accounting Officer stated that the RPA informed the Department in June 2005 that the consequential net additional cost resulting from the inconclusive procurement process was approximately € 860,000.

From July 2005 to end December 2005, approximately €700,000 was incurred on the RPA's project team and on associated expertise. During this time, the RPA's project team participated in the tripartite talks and supporting technical dialogue which contributed to the resulting agreement with Dublin Bus in December 2005. In the first half of 2006, a further €690,000 was paid to meet the costs of the RPA on integrated ticketing. The funding also contributed to some limited detailed design work and development of the smartcard interface module. While some of the ongoing costs incurred over the past year could be regarded as nugatory expenditure, the Accounting Officer was not in a position to be definitive on the proportion.

The Accounting Officer informed me that the Department moved to address the underlying issues before allowing the project to proceed, while recognising that some nugatory expenditure could be incurred by not giving an immediate go ahead to the revised procurement process proposed by the RPA. She stated that she recognised that there would be ongoing costs associated with the project pending the completion of the two reviews. She took the view, subsequently endorsed by both review reports, that if the project team and associated expertise were to be lost, it would have resulted in significant nugatory expenditure and it would have been difficult to resurrect the project in its current form. In all probability it would have required additional expenditure very substantially in excess of that incurred over the review period to resurrect the project. Therefore, she believed that the continued incurring of these costs was warranted pending a final decision on the project.

## DFSA Requirements

**Was she satisfied that the requirements of the DSFA's free travel schemes were being fully catered for in the proposed system?**

The Accounting Officer stated that it was the Department's expectation from the outset that the technical specifications of the integrated ticketing system would address the requirements of the DSFA. That Department had had an involvement with the project at various stages since its inception. It had participated in the project as members of the Steering Committee and had communicated, on a number of occasions, its support for the project. DSFA recognised the benefits of the project and had stated that it was in full agreement on the need to ensure compatibility between the integrated ticketing project and the free travel scheme. The Department was in discussions with DSFA to finalise how it would be involved in the new project board in a manner that recognised the role of that Department as a transport user.

## Implementation Timetable

**What was the current best estimate of the cost and time required for the successful and full implementation of the system?**

The Accounting Officer stated that the Minister had set a number of immediate tasks for the project board, including

- to review and settle by way of agreement the scope, timetable and budget for the phased completion of the integrated ticketing project, having regard to the work undertaken by the RPA to date, the agreement signed off by the chairmen of the RPA and CIE in January 2006, the overall target budget of €42.7m proposed by the RPA in January 2006 and the recommendations of both reviews.
- to review the ticketing plans and associated timetable of the transport agencies to satisfy itself on their compatibility with the integrated ticketing project;
- to agree a procurement plan for the project taking on board lessons learned from the experience to date.

The Minister had asked the chairman to report back to him on these issues by September 2006. The cost and timetable for the project would be clearer at that time.

## Accounting Officer's Conclusion

The Accounting Officer concluded that projects of this nature were inherently complex and difficult particularly in a multi-operator environment. They also tended to be more costly and to take longer to deliver than initially anticipated. Experience in other countries, such as Australia and the Netherlands, supported this point. The steps taken by the Department were intended to mitigate the difficulties that had arisen in rolling out integrated ticketing with a view to getting best value for money for the taxpayer for expenditure that had already been incurred and to ensure successful implementation of a project that had an important contribution to make to the delivery of integrated public transport.

# 11.2 Dundalk Port Company – Corporate Governance Issues

The Harbours Act 1996 provides for the management, control, operation and development of certain harbours. It enabled the Minister, (the Minister for Transport since 1 January 2006, formerly the Minister for Communications, Marine and Natural Resources) with the consent of the Minister for Finance, to establish companies in respect of certain harbours for that purpose and to define the functions of those companies. Among the companies so established is Dundalk Port Company, which on incorporation took over the functions, previously carried out by Dundalk Harbour Commissioners. The Minister and the Minister for Finance or their nominees are the sole shareholders in the company.

In October 2004, in my capacity as Comptroller, I received a request from the Department of Finance on the recommendation of the Department of Communications, Marine and Natural Resources to release €119,000 from the account of the Exchequer at the Central Bank to enable the Department to provide funding to Dundalk Port Company under the National Development Plan 2000-2006.

On examining the requisition and associated papers, my staff noted references to the propriety of earlier borrowings by the company and the setting up of a subsidiary company. In the light of my misgivings the requisition was not pursued. These matters were followed up during the course of my 2005 audit.

## Unauthorised borrowings

The consent of the Minister and the Minister for Finance is necessary for all borrowings by the company under Section 23(1)(a) of the Harbours Act 1996. However, three instances of unauthorised borrowings by the company were noted as follows

- An unauthorised loan of €371,960, for the purchase of a dredger, was drawn down by the company in October 2003.
- An unauthorised loan of €161,834 for the purchase of a pilot boat was drawn down by the company in August 2004. This loan was drawn down by the company despite the fact that the previous instance of unauthorised borrowing had come to light and had been raised with the company.
- In August 2005, despite correspondence from the Department that it was gravely concerned at persistent breaches by the company of the requirements of the Harbours Act, 1996 and the Code of Practice for the Governance of State Bodies, the Department became aware of a further unauthorised borrowing – a short term overdraft of €280,000 that had been drawn down in February 2005.

The balances outstanding on these facilities as at 1 April 2006 were €103,584, €161,869 and €761,923 respectively. The borrowings have since been repaid using the proceeds of a land sale.

## Unauthorised subsidiary

The consent of the Minister, given with the consent of the Minister for Finance, is necessary for the establishment of a subsidiary company under section 6.1 of the Code of Practice for the Governance of State Bodies. However, the Department had noted on receipt of the company's annual accounts for 2003 that an unauthorised subsidiary company, Dealgan Shipping Ltd (Dealgan) had been incorporated in July 2003.

Dealgan was the registered owner of the dredger and operated it in 2003. Ownership was later transferred to the port company. In June 2004 the port company informed the Department that an employee was allowed a monthly management fee to operate the dredger outside of his normal duties. However, while the management fee was invoiced, no payment was ever made and the company has confirmed to the

Department that no fee will be paid. The company informed the Department by letter in December 2004 that Dealgan had ceased trading with effect from 1 September 2004.

# Audit Concerns

In view of the foregoing I asked the Accounting Officer if she was satisfied with the monitoring by the Department of the activities of the company and whether, in view of the level of unauthorised activity in the company, she was satisfied that corporate governance in this and other State port companies was in line with best practice.

I also asked her to comment specifically on

- Measures taken to ensure that unauthorised borrowings are not drawn down by the company or any other state port company
- The delay in striking off Dealgan
- The conduct of the sale of the land.

# Accounting Officer's Response

The Accounting Officer informed me by way of background that her Department had assumed responsibility for maritime transport functions on 1 January 2006. Dundalk Port Company is required to take all proper measures for the management, control, operation and development of its harbour. Operational decisions relating to the port are primarily a matter for the port company and its board.

On becoming aware of the existence of the subsidiary when considering the company's accounts for 2003, which were signed off by the company on 25 March 2004, the Department launched an immediate investigation into the reason for the establishment of an unauthorised subsidiary, and led to a temporary postponement of the company's AGM. The company was instructed that it must produce a comprehensive business plan for the subsidiary in order for the matter to be considered further.

In giving guidance to the company on the production of a business plan, it became apparent to the Department that a primary driver for the establishment of the subsidiary was an erroneous perception on the part of the company that such an arrangement was necessary in order to draw down National Development Plan funding. When the Department clarified to it that this was not the case, the company undertook that Dealgan would cease trading and be wound up.

In consultation with the Chairman of the company the Department engaged the services of a firm of accountants and business advisors in September 2005 to provide a report on the state of affairs of the company. The key recommendations received were

- To consolidate all unauthorised loans and facilities into one authorised bridging facility of €700,000 to be repaid as soon as possible using the proceeds of a proposed sale of property
- To train company staff in corporate governance procedures
- To monitor quarterly the implementation of these recommendations and the ongoing performance of the company and its management.

In this way the Department sought to get assurance that proper procedures would be implemented and maintained.

The firm of accountants and business advisers were re-engaged in December 2005 to provide the necessary training and oversight. In a progress report dated 10 May 2006 they confirmed that all

recommendations were being implemented. In the light of these developments the Accounting Officer stated that she was satisfied with the monitoring by the Department of the activities of the company.

In relation to the particular audit concerns the Accounting Officer informed me that

- The requirement to obtain the consent of the Minister before arranging to borrow finance is clearly laid out in the Harbours Act 1996. The Department had written on 10 March 2005 to the CEO of each port company, including Dundalk, to outline what procedures must be followed when submitting a borrowing application. In the specific case of the company, the Department has confirmed that unauthorised borrowings have been repaid by the company from the disposal of a non-core asset, that appropriate commitments to future compliance have been obtained and that appropriate monitoring and training arrangements have been put in place. Similar breaches had not come to light in any of the other port companies.
- The consultants had informed the Department that Dealgan could not be struck off the register of companies until 2005 accounts had been prepared. All requirements for strike off had now been carried out and the Department understood that strike-off would be completed shortly.
- The consultants had monitored the closing stages of the sale of land on behalf of the Department. The property was sold on the open market and the Department understood that the process was carried out under the relevant Government guidelines.

The Accounting Officer confirmed the validity of the commercial decision to purchase the dredger, thus avoiding the expense of renting a vessel on a temporary basis. In fact, the company could not have afforded to have the dredging work carried out at the rates quoted by international companies. Failure to carry out the dredging would have ultimately led to the closure of the port.

She added that Dundalk Port is seeing the benefit of the dredging work carried out. It permits access to larger vessels and has led to a significant expansion of the port's customer base and throughput. As a result, the port company has indicated that it hopes to return an operating profit in the current year.

# 11.3 Performance Audit of State Port Companies

The Harbours Act 1996 also provides that the Minister may appoint a suitably qualified person to carry out an examination as to the efficiency and cost-effectiveness of the performance by a state port company of its functions and to report in writing to the Minister the results of the examination. The Minister shall submit a copy of such a report to the Government and the company or companies to which the report relates.

In the course of my review I noted that in September 2000 the Department commissioned a performance audit of the State's port companies under the provisions of Section 29 of the Harbours Act, 1996. The consultants recruited examined the efficiency and cost effectiveness of the performance of the following port companies

- Dublin Port Company
- Port of Cork Company
- Dun Laoghaire Harbour Company
- Shannon Estuary Port Company/Foynes Port Company (merged December 2000)
- New Ross Port Company
- Galway Port Company
- Drogheda Port Company.

The consultants' report was received in Spring 2001 but I noted that it had not yet been presented to Government as required by Section 29(2) of the Act. I asked the Accounting Officer why, what action the Department had taken as a result of the report and whether, in light of the content of the report, it was proposed to commission any further performance audits.

## Accounting Officer's Response

The Accounting Officer informed me that submission of the audit findings to Government had been delayed on foot of legal advice, dated April 2002, regarding a judicial review sought by former board members and employees of one port company. This advice stated that if the Department wished to present the report to Government then any mention in it of that particular port company should be deleted. The cases were struck out in March 2004 as part of an agreed settlement. The report was eventually presented to Government on 12 July 2006.

She stated that, in summary, the performance audit found that the eight State port companies operating in 2001 managed very different ports, that the companies had successfully accommodated rapid traffic growth, were generally adapting to a more commercial mindset and were becoming cost efficient and customer focused. In January 2005, the Minister for the Marine had launched the Government's ports policy statement. This aimed to better equip the port sector and its stakeholders to meet national and regional capacity and service needs through clearer commercial mandates for the ports and their boards, encouragement of private sector investment and mergers, better dispute resolution and better transport policy coordination. These issues were consistent with a number of the performance audit findings.

She also informed me that the Department did not propose to commission any further composite performance audits of all the State port companies. The Department believed that, having regard to the number and diversity of the State port companies, individual monitoring and targeted intervention where necessary was more efficient and cost effective. The Department also considered that the mandatory annual reporting requirements that apply to the port companies, together with regular meetings and other contacts, was the appropriate mechanism for monitoring the performance of the port companies. The focus of current Government policy was on sectoral ports policy and, in that context, an extensive study has just been completed in the area of port capacity.

# Chapter 12

# Department of Social and Family Affairs

# 12.1 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 €6.30bn and €5.46bn respectively in 2005.

Table 37, Table 38, Table 39, and Table 40 outline overall expenditure on various schemes over the period 2001 to 2005, 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 2001.

**Table 37 - Scheme Expenditure**

| | 2001 €m | 2002 €m | 2003 €m | 2004 €m | 2005 €m |
|---|---|---|---|---|---|
| Social Insurance | 3,517 | 4,198 | 4,649 | 5,081 | 5,460 |
| Social Assistance | 3,983 | 4,940 | 5,460 | 5,821 | 6,296 |
| **Total** | **7,500** | **9,138** | **10,109** | **10,902** | **11,756** |

**Table 38 - Number and Amount of overpayments recorded for recovery (Numbers shown in brackets)**

| | 2001 €m | 2002 €m | 2003 €m | 2004 €m | 2005 €m |
|---|---|---|---|---|---|
| Social Insurance | 6.79 | 9.72 | 10.60 | 12.12 | 11.02 |
| | (15,786) | (23,723) | (26,174) | (26,131) | (22,420) |
| Social Assistance | 19.26 | 19.41 | 28.77 | 44.85 | 36.24 |
| | (14,274) | (15,084) | (17,459) | (20,000) | (17,126) |
| **Total** | **26.05** | **29.13** | **39.37** | **56.97** | **47.26** |
| | **(30,060)** | **(38,807)** | **(43,633)** | **(46,131)** | **(39,546)** |

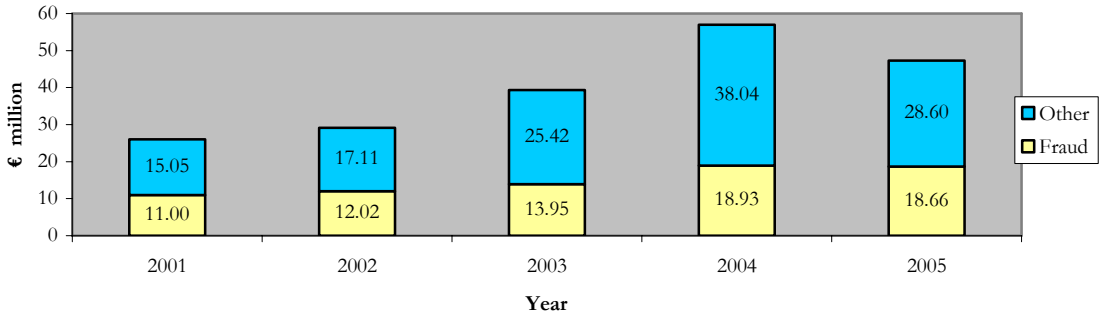
**Table 39 Number and Amount of overpayments attributed to fraud[43] or suspected fraud (Numbers shown in brackets)**

| | 2001 €m | 2002 €m | 2003 €m | 2004 €m | 2005 €m |
|---|---|---|---|---|---|
| Social Insurance | 3.27 | 4.59 | 5.07 | 6.24 | 5.53 |
| | (5,321) | (8,121) | (9,606) | (10,771) | (8,587) |
| Social Assistance | 7.73 | 7.43 | 8.88 | 12.69 | 13.13 |
| | (5,350) | (5,728) | (7,148) | (8,483) | (7,758) |
| **Total** | **11.00** | **12.02** | **13.95** | **18.93** | **18.66** |
| | **(10,671)** | **(13,849)** | **(16,754)** | **(19,254)** | **(16,345)** |

The amount of overpayments attributed to fraud or suspected fraud compared to total overpayments since 2001 is summarised in Figure 4.

[43] Estate cases where undisclosed means come to light are not classified as fraud/suspected fraud. The amount of overpayments recorded in respect of estate cases in 2005 was €6.2 .

**Figure 4**




The Department's record of recovery of overpayments during the period 2001 - 2005 is shown in Table 40.

**Table 40 - Departments record of recovery of overpayments 2001 to 2005**

| | 2001 €'000 | 2002 €'000 | 2003 €'000 | 2004 €'000 | 2005 €'000 |
|---|---|---|---|---|---|
| Overpayments not disposed of at 1 January | 64,374 | 65,452 | 70,621 | 85,953 | 115,993 |
| Overpayments recorded for recovery | 26,049 | 29,130 | 39,367 | 56,967[1] | 47,261 |
| **less** | | | | | |
| overpayments recorded in prior years cancelled | (668) | (394) | (381) | (693) | (1,826) |
| sums recovered in cash | (9,873) | (8,892) | (10,397) | (11,506) | (11,246) |
| sums withheld from current entitlements | (5,185) | (6,734) | (6,521) | (8,332) | (8,715) |
| net amounts written off as irrecoverable | (9,245) | (7,941) | (6,736) | (6,396) | (10,217) |
| **Overpayments not disposed of at 31 December** | 65,452 | 70,621 | 85,953 | 115,993[1] | 131,250 |

[1.] Revised

Of the €131,250,158 overpayments outstanding at 31 December 2005 - €34,295,696 dates from 2005; €38,787,682 from 2004; €22,834,566 from 2003 and €35,332,214 from earlier years.

The Accounting Officer attributed the fall in the number and value of overpayments in 2005 to initiatives taken by his Department to deal with overpayments and combat fraud.

Specific control initiatives undertaken by the Department in 2005, which led to the identification of significant levels of overpayment included

- The Lower Back Pain Project
- A Disability Allowance mail shot where payments are made using electronic funds transfer
- Data-matching exercises involving
  - Special Investigations Unit in unemployment cases;
  - And in One -Parent Family (OPF) cases
  - student unemployment cases
  - Child Benefit in OPF cases
  - The General Register's Office data-matching (Marriages and Deaths)

# 12.2 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 2005, 412 criminal cases (2004 - 476 cases) were forwarded to the Chief State Solicitor's Office for prosecution as shown in Table 41.

**Table 41 - Criminal cases forwarded to the Chief State Solicitor**

| | 2005 | 2004 |
|---|---|---|
| Unemployment Assistance | 197 | 191 |
| Unemployment Benefit | 153 | 226 |
| Disability Benefit | 19 | 9 |
| One Parent Family Payments | 19 | 23 |
| Other Schemes | 10 | 10 |
| Offences Committed by Employers | 14 | 17 |
| **Total** | **412** | **476** |

A total of 256 criminal prosecutions (2004 – 259 prosecutions) involving social welfare recipients were finalised in court in 2005. The total amount of overpayments assessed in these cases of persons who attempted to or obtained benefits/assistance fraudulently was €1,346,770 (2004 - €1,116,492). The results of these 256 court cases and the penalties imposed are given in Table 42.

**Table 42 - Results of Criminal Cases finalised in Court in 2005**

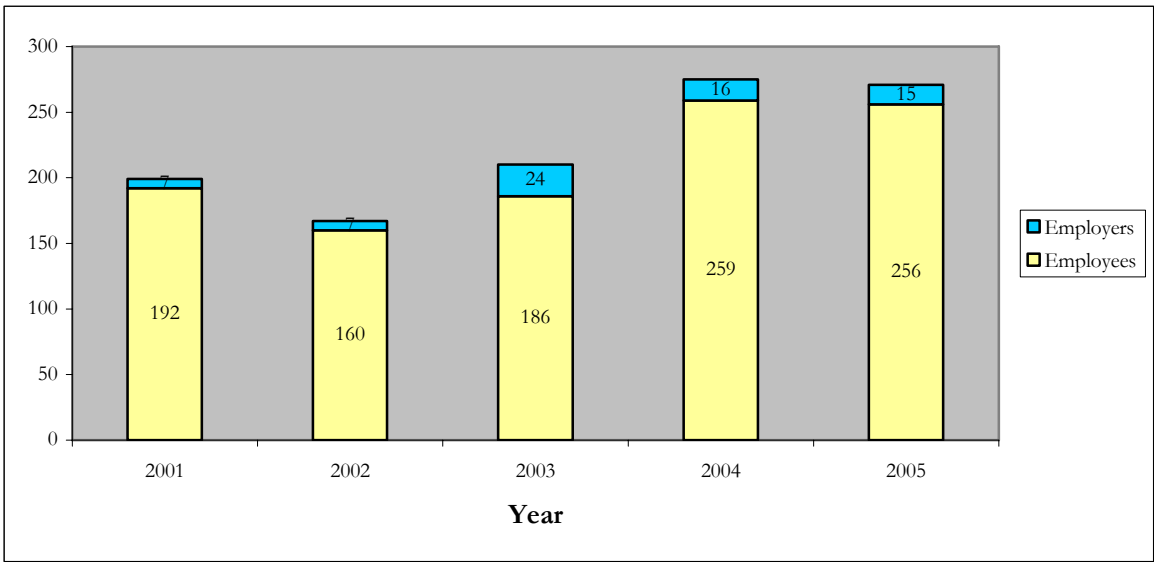
| | Unemployment Assistance | Unemployment Benefit | Disability Benefit | One Parent Family Payments | Other [44] | Total |
|---|---|---|---|---|---|---|
| Fined[45] | 46 | 56 | 4 | 6 | 4 | 116 |
| Community Service | 3 | 3 | 0 | 0 | 0 | 6 |
| Imprisoned | 3 | 1 | 0 | 0 | 0 | 4 |
| Probation Act | 33 | 41 | 5 | 5 | 1 | 85 |
| Suspended Sentence | 17 | 5 | 1 | 1 | 0 | 24 |
| Struck-out | 4 | 2 | 1 | 0 | 1 | 8 |
| Dismissed | 2 | 0 | 0 | 0 | 0 | 2 |
| Bound to the Peace | 2 | 0 | 0 | 0 | 0 | 2 |
| Liberty to re-enter | 4 | 2 | 1 | 0 | 0 | 7 |
| Decree Obtained | 1 | 0 | 0 | 0 | 1 | 2 |
| **Total** | **115** | **110** | **12** | **12** | **7** | **256** |

[44]Other 7: Disability Allowance 2, Invalidity Pension 1, Old Age Pension 2, Liable Relative 1 and Carers 1
[45] Fines to a value of €56,525 were imposed by the courts (€68,886 in 2004 in 144 cases)

Prosecutions of 15 cases involving employers (2004 – 16 employers) were also finalised with 14 being fined[46] and 1 receiving a suspended sentence.

The number of prosecutions finalised in the courts since 2001 is summarised in Figure 5.

**Figure 5**




Between 2001 and 2005, a total of 76 cases were sent to the Chief State Solicitor's Office (CSSO) for the pursuit of civil proceedings. In this period, 66 cases (including 49 pre-2001cases) have been finalised. The breakdown per year is set out in Table 43

**Table 43**

| | 2001 | 2002 | 2003 | 2004 | 2005 | Total |
|---|---|---|---|---|---|---|
| Sent to CSSO in the year | 14 | 11 | 21 | 17 | 13 | **76** |
| Finalised in the year | 8 | 11 | 14 | 12 | 21 | **66** |

Of the 66 finalised, settlement was reached in 8 cases without going to court (this involved recovery of €92,868), 2 were finalised in court (decrees awarded), 12 cases were not pursued due to the circumstances of the debtor, 10 cases were statute barred, 34 made arrangements to repay the debts in instalments. There are 78 cases that have yet to be finalised.

[46] Fines to a value of €8,370 were imposed by the courts (€7,039 in 2004 in 14 cases).

# Chapter 13

# Department of Health and Children

# 13.1 The Post-Mortem Inquiry

## Background to the Inquiry

In 1999 parents of children who had died at Our Lady's Hospital for Sick Children, Crumlin began to query the hospital's practice in the area of removal and retention of organs. By late March 2000, approximately 1,700 enquiries had been received from parents by the major hospitals. Concerns were expressed that the removal and retention of organs was not covered by informed consent. A particular concern related to the extraction of pituitary glands from deceased children. Our Lady's Hospital for Sick Children, Crumlin, confirmed that correspondence on its files indicated that its laboratory had participated in extracting pituitary glands from deceased children which were then supplied to a pharmaceutical company to manufacture a human growth hormone for the treatment of children.

In December 1999, parents of children whose organs had been retained by Our Lady's Hospital and by Cork University Hospital formed a support group called Parents for Justice (PFJ).

In April 2000 the Government decided to establish a non-statutory inquiry which would review post-mortem policy, practice and procedure in the State since 1970 particularly relating to organ removal, retention and disposal by reference to prevailing standards both within the State and in other jurisdictions. An inquiry was established with the intention that work would be completed in two phases

- The first phase of the Inquiry would culminate in a report which was to be available within six months.
- On receipt of this report, the Minister for Health and Children (the Minister) would table a motion that the second phase of the Inquiry would be undertaken by the Oireachtas Joint Committee on Health and Children. The Committee has powers to discover documents and compel witnesses under the Committees of the Houses of the Oireachtas (Compellability, Privileges and Immunities of Witnesses) Act 1997.

A chairman was appointed by the Minister on 11 April 2000 subject to approval of the terms and conditions of employment by the Minister for Finance.

## The Form of the Inquiry

Detailed discussions took place with PFJ and its legal advisors in a bid to agree an appropriate format for the inquiry. PFJ lobbied for the establishment of a statutory inquiry with full powers of compellability, privileges and immunities of witnesses. However, the Minister favoured a non-statutory format for the following reasons

- The needs and concerns of PFJ could be met by this route
- It could be speedily established
- It could be flexible in its approach and less rigid in its implementation
- It would be relatively informal and less adversarial
- It would not be as debilitating on the provision of vital hospital services
- It could deal with these painful issues over a shorter period of time.

Additionally, the Minister expressed concerns that many parents might not be open to the prospect of going before an open and public tribunal to talk about the traumatic event of the loss of a child. While some parents would want to participate in such a forum there might be many others who might not wish to do so. At that stage, PFJ went along with this proposal on the basis that the Minister gave a written

commitment that there would be a second phase – the Oireachtas Joint Committee on Health and Children which would constitute the statutory phase. The Committee could decide whether to conduct hearings in relation to the report and, if it considered it appropriate to do so, to avail of powers to call witnesses as appropriate. Ultimately, however, it was not possible to conduct the second phase through an Oireachtas committee in the manner originally envisaged.[47]

# Objectives of the Inquiry

Although pressure groups, such as PFJ, lobbied to make the Inquiry as extensive as possible the Government proposed to confine the remit of the Inquiry in order to ensure timely completion. At the time the Government decided to establish the Inquiry in April 2000 its objectives were set out as follows

- To independently establish the full facts in regard to past practice relating to post-mortem examinations and to address the issues (removal, retention, disposal, storage and consent) raised by parents and by the PFJ group.
- To restore full public confidence in hospitals and in the necessity for post-mortem examinations including organ and tissue retention for such purposes as further diagnosis, teaching and research.
- To provide public assurance that any previous practice which might be judged unacceptable will not recur. An inquiry would provide for publicly acceptable protocols to apply to all hospitals where post-mortem examinations are carried out.
- To establish the full facts relating to some hospitals' confirmed participation in the extraction of pituitary glands from deceased children and the supply of these glands to a pharmaceutical company to produce a growth hormone for the treatment of children.

# Inquiry Resources and Timing

In a letter to the Minister in February 2001 the chairman set out the terms under which the Inquiry team and the chairman were embarking on the Inquiry. The chairman indicated that

- She no longer thought it possible to complete the task within the six months originally agreed and asserted that it would take far longer because the Inquiry had become much more extensive, complex, and comprehensive than originally envisaged.
- She required the services of at least one Senior Counsel on a full time basis rather than on an ad hoc basis alone.
- She and two members of the legal team would be operating with flexibility. This would allow them to attend to legal work other than that of the Inquiry which she felt was necessary, in order to maintain connection with the Law Library and with their respective practices.
- She wished to be able to review these terms every six months.

# Terms of Reference

The Terms of Reference were set out in a Public Notice issued on 23 March 2001 by the chairman together with her Interpretation of the Terms of Reference. The published Terms of Reference are set out in Figure 6.

[47] The Minister had stated that if it transpired that it was not possible to submit the final report to the Oireachtas Committee (whether as a result of the Abbeylara judgment or otherwise) he was committed to submitting it to another appropriate forum with statutory powers. When the final Madden report was published it was submitted to the Oireachtas Committee.

**Figure 6 Terms of Reference of the Inquiry**

To review all post-mortem examination policy, practice and procedure in the State since 1970, and in particular as it relates to organ removal, retention, storage and disposal by reference to prevailing standards both in and outside of the State. To examine the application of these policies, practices and procedures in hospitals, generally and in particular their application in the 11 named hospitals[48].

The Inquiry will address the hospitals' policies, practices and procedures in this area of organ removal, retention, storage and disposal, the necessity for such practices and the manner in which they were carried out. The Inquiry will take account of best practice regarding post-mortem examinations in and outside of the State together with the reasonable expectations of parents of deceased children and next of kin in such circumstances. In particular, the Inquiry will:

- Examine the hospitals' policies and practices relating to obtaining consent from parents and next of kin for post-mortem examinations, organ removal, retention, storage and disposal.
- Examine the hospitals' procedures and practices relating to retained organs, including the reasons for such retention, the hospitals' management of such retention and storage of organs (including record keeping) and of any other arrangements relating to such organs and the practices adopted for ultimately dealing with retained organs including any arrangements with pharmaceutical companies in relation to those retained organs.
- Review the nature and appropriateness of the hospitals' overall response to parents of children and next of kin of persons on whom a post-mortem examination was performed.
- Examine any specific cases in any hospital as it deems appropriate in relation to post-mortem examinations and post-mortem examination related matters.

However, it will be at the discretion of the Inquiry to examine any other relevant matters which arise in the course of the Inquiry in relation to post-mortem examination policy, practice and procedure in the State since 1970.

The inquiry will make its final report, including its findings, to the Minister for Health and Children within six months unless otherwise determined by the Minister. It will make recommendations to the Minister on foot of its findings.

The report will include confirmation that the Inquiry received all the information and co-operation from health agencies, persons employed therein and any other persons, which it considered necessary to form its opinions and to arrive at its conclusions. In the event of deficiencies arising in these areas, which the Inquiry considers materially limits the scope of its investigations the report will identify same.

The chairman's Interpretation of the Terms of Reference stated that she considered that the work of the Inquiry would extend to all post-mortem examinations wherever carried out. This set the scope of the Inquiry which would extend to an examination of the specifics of individual post-mortem examinations. The scope in the Interpretation also extended to all hospitals within the State in which post-mortem examinations were carried out and/or hospitals which requested, directed or authorised post-mortem examinations to be carried out at another location. The Interpretation stated that the Minister for Health and Children had determined that the time limit of six months for the final report no longer applied and that the inquiry would report to him within a period of 18 months unless otherwise determined by him.

[48] Temple St Children's Hospital, Coombe Women's Hospital, Our Lady's Hospital for Sick Children (Crumlin), National Maternity Hospital (Holles St), Rotunda Hospital, and the Major Academic Teaching Hospitals.

On 22 October 2002 the Minister, in Dáil Éireann, expressed some reservations about the scope of the terms of reference. He noted that to move to a statutory phase at that stage would not be achieved within the existing terms of reference, as these were too wide. He also noted that the problem which had by then arisen with the timeframe was related to the terms of reference.

# Provisions in Regard to Procedures

By reason of the fact that the Inquiry was established on a non-statutory basis it had no powers of compellability, either in relation to the production of documents or information, or in respect of the attendance of witnesses before it. Consequently, it depended upon the voluntary co-operation of the many potential participants in its work. For this reason it was deemed necessary to obtain a consensus between all potential participants as to the procedures to be adopted. To this end a document entitled 'Memorandum on Procedures' was drawn up, in consultation with relevant parties, and issued on 3 August 2002 to all participants for signature and return. The memorandum outlined how the Inquiry proposed to conduct its work. Specifically it set out three stages to be completed.

- The first stage involved conducting research as well as obtaining information from all relevant individuals. This included taking submissions both oral and written, obtaining a sample of post-mortem examination records and records of consent.
- The second stage aimed to consider all the evidence and identify matters which might be in dispute.
- In the third stage it was planned to resolve these disputed matters of fact.

The Memorandum guaranteed the constitutional right to fair procedures to all those affected by its work. Moreover, the Inquiry stated that it would inform all affected persons of proposed criticisms contained in its report and would afford them a right of reply.

It is unclear how many hospitals agreed to be bound by these procedures but by 2 October 2002 only 62 of the 201 hospitals identified in the report had signed the Memorandum. Furthermore, only 65 of 402 parents and next of kin who had made written submissions to the Inquiry had signed as at that date. However, having regard to the level of co-operation obtained to that date the chairman did not regard the failure of participants to sign the memorandum as impeding the ability of the Inquiry to continue its work. A number of participants who had not signed the Memorandum provided full cooperation to the Inquiry.

# Conduct of the Inquiry

The first phase of the Inquiry began on 5 March 2001. No provisions had been put in place for interim reporting as the report was expected to be delivered by September 2002. However, in August 2002 the chairman informed the Minister that the Inquiry was a long way from reaching the stage at which a report would be available having regard to the extensive scope of the terms of reference and the nature of the Inquiry. The Minister requested a progress report from the chairman. In response, the chairman submitted a Progress Report on 2 October 2002 which outlined the work already completed by the Inquiry team and set out the work that had yet to be completed. The Report also noted the response rate obtained from hospitals, individual parents and next of kin, and other relevant parties. However, the chairman was unable to give an estimate of the timescale required for the completion of the work of the Inquiry and the making of its report.

In October 2002 the PFJ expressed their dissatisfaction with the process in a meeting with the Minister and decided to withdraw. At the time, there were also concerns about the implications of the Abbeylara judgment. The Minister assured the PFJ, following legal advice, that the Abbeylara judgment should not affect phase one and that it could continue. In respect of phase two, his advice was that much would depend on the content of the report that would be presented to the Oireachtas Committee. Upon their withdrawal from participation in the Inquiry the PFJ also withdrew any submissions made to it by their

members. The Chairman informed the Minister, in November 2002, that she had sufficient involvement of parents and the Inquiry was continuing with its work.

In December 2002, the chairman indicated to the Minister that an interim report on paediatric hospitals would be provided by December 2003 which would be followed by reports on maternity hospitals and on general hospitals. Subsequently, in October 2003, the chairman, in a further progress report, informed the Minister that she would not be in a position to provide the interim report on paediatric hospitals by the end of the year.

During a review of all ongoing Tribunals and Inquiries the Attorney General wrote to the chairman on 16 July 2004 requesting an estimated date of completion. The chairman's response to this request did not give a definite timeframe for completion. Subsequently, it was agreed by Government on 1 September 2004 that the chairman should be requested to furnish the Minister with a final report not later than 31 March 2005 and that the Inquiry should then cease.

# Output of Phase One of the Inquiry

On 31 March 2005, 54 bankers boxes of material were furnished to the Department of Health and Children. This material comprised a report running to 3,500 pages accompanied by 51 boxes of appendices including submissions from parents, next of kin, hospitals, health boards and professional bodies. The report dealt with the three Dublin paediatric hospitals and did not report on the other 198 hospitals identified in the progress report. However, evidence collected on these other hospitals was contained in the appendices. It was acknowledged in the report that it was not complete due to time constraints.

Counsel from the Attorney General's Office were retained to read and analyse the report at a total cost of €21,800. Arising out of this review certain legal issues were identified. In a letter written to the Tánaiste and Minister for Health and Children in April 2005 the Attorney General stated that the report could not be published for legal reasons due to issues relating to natural justice.

# Cost of Phase One

At the outset the costs had been estimated to be of the order of €1.9m. However, by 31 March 2005 when the report was submitted the total cost of the Inquiry had risen to over €13m. Table 44 outlines the costs of the Inquiry.

**Table 44 Costs incurred by Inquiry**

| Cost Category | €m |
|---|---|
| Office Fit out costs | 1.19 |
| Rent of Premises | 1.10 |
| Legal costs (Inquiry Team) | 7.70 |
| Administrative Costs[49] | 3.80 |
| **Total** | **13.79** |

A total of €7.7m was incurred on legal costs. These fees were incurred as set out in Table 45.

[49] These included salaries, office administration, heat power, light, maintenance, cleaning, security etc.

**Table 45 Legal Costs**

| Recipients | Number | Cost €m |
|---|---|---|
| Chairman | 1 | 2.5 |
| Full-time Barristers | 2 | 3.1 |
| Part-time Barristers | 3 | 1.1 |
| Solicitor | 1 | 1.0 |
| **Total** | **7** | **7.7** |

# UK Inquiries

No inquiries of this scale have previously been undertaken on organ retention issues in Ireland or the UK. The two inquiries which were undertaken in the UK dealt with single hospitals and are therefore not directly comparable in terms of timescale and cost.

- An inquiry into the management of the care of children receiving complex surgical services at the Bristol Royal Infirmary was established in June 1998 and disclosed that following post-mortem examinations, the organs of children who had died were removed and retained by the hospital. The Inquiry was conducted by a Chairman who was a Professor of Health Law, Ethics and Policy, and assisted by a Professor of Medicine, a Director of Nursing, and a Director of a Centre for Family Law. An interim report of the Inquiry investigating the removal and retention of organs was published in May 2000.
- An inquiry into Alder Hey Children's Hospital in Liverpool, which was established in December 1999, found that the organs of a large number of children were retained without the consent of parents or next of kin. The Alder Hey Inquiry was conducted by a Chairman who was a Queen's Counsel, and assisted by a Consultant Paediatric Pathologist, and a Chief Officer of a Community Health Council. This Inquiry extended only to one hospital and reported in nine months.

In contrast to the UK inquiries, the Irish Inquiry relied heavily on legal expertise. Two full-time barristers, three part-time barristers and a solicitor made up the bulk of the Inquiry's resources. No other area of expertise was represented on the team. However, the advice of several experts was sought throughout the life of the Inquiry. The advice of a statistician was sought but does not appear to have been used.

# Appointment of Legal Expert to prepare Report

In May 2005, following the advice of the Attorney General, the Government approved the appointment of a legal expert to prepare a report on key issues relating to post-mortem practice and procedures by 21 December 2005. The final report was completed and presented to the Minister by the reporting deadline and at the total cost of €436,000.

The specific terms of reference for this work were

- To inquire into policies and practices relating to the removal, retention and disposal of organs from children who had undergone post-mortem examination in the State since 1970.
- To inquire into allegations that pituitary glands were removed from children undergoing post-mortem examination for sale to pharmaceutical companies within and outside the State.
- To examine professional practice in relation to the information given to children's parents in respect of the removal, retention and disposal of tissue and organs and the appropriateness of practices of obtaining consent.

- To review the manner in which hospitals responded to concerns raised by bereaved families relating to post-mortem practices carried out on children.
- To make recommendations for any legislative and/or policy change as deemed appropriate in relation to post-mortems on children.

For the purpose of her report 'child' or 'children' refers to those born alive and less than twelve years of age at the date of death.

In conducting this work, the objective pursued by the expert was to make findings on facts about post-mortem procedure in the hospital system. The expert's report found that post-mortem examinations were carried out in Ireland according to best professional and international standards and that no intentional disrespect was shown to the child's body. In relation to the extraction of pituitary glands the expert concluded that there was no known commercial motive on the part of any hospital or its staff. The root causes of the controversy had been a lack of communication with parents as to why organs were retained, the difference in perspective as to their symbolic significance and the legislative vacuum on the role of consent in post-mortem examinations. The report recommended the enactment of clear and unambiguous legislation to ensure that such practices cannot happen again.

# Audit Concerns

For the year ending 2005, expenditure on tribunals and inquiries under the aegis of the Department of Health and Children (Subhead E) amounted to approximately €44.4m. Some €1m of this charge related to Post-Mortem Inquiries bringing the total legal and administrative costs of the Post-Mortem Inquiries to €12m. These costs do not include office fit out costs and rental costs which are charged to other subheads of the vote or the costs incurred by hospitals and health boards (now the HSE) in responding to the inquiry.

It is recognised that there is a delicate balance to be achieved when inquiries are undertaken. On one hand, the facts must be established through an objective and independent process while, on the other, there needs to be a cost effective inquiry which gathers sufficient relevant and reliable evidence to enable the State to address the issues and concerns which arise. This would suggest the importance, at the outset, of focusing attention on certain key features of inquiries

- agreeing the general scope of the Inquiry and specific, focused and unambiguous terms of reference
- establishing a methodology based on achieving cost effective evidence-gathering focused on defined Inquiry issues
- providing for review milestones and reporting deadlines.

# Queries to the Department

Arising out of these concerns I asked the Accounting Officer what steps were taken at the outset of the Inquiry and during its course by the Department to reduce the exposure of the State to cost escalation and to ensure timely reporting. I also enquired as to what lessons have been learned in regard to the conduct of this Inquiry in the areas of scope setting, methodology and the establishment of review milestones and reporting deadlines, and the extent to which such lessons have been or are capable of being applied to other Inquiries. I also asked the Accounting Officer for his best estimate of the costs incurred by the Health Service Executive (formerly the Health Boards) and of hospitals in connection with the Inquiry.

# Accounting Officer's Response

With regard to the role of the Department in reducing the risk to the State of cost escalation and ensuring timely reporting the Accounting Officer informed me that it is necessary to address this question in the

context of the position that obtained in 1999/2000 when issues in relation to post mortem practice and organ retention came to public attention. This was a highly emotional issue for parents and the motives of the hospitals and clinicians involved were being questioned, particularly in relation to the extraction of pituitary glands. There were demands that where appropriate those involved be "named and shamed" and many believed that the Department itself was at least partially culpable for what had occurred.

The Government Decision in April 2000 was that a non-statutory inquiry should be conducted by a senior counsel, who would act independently of the Department. The terms and conditions of the Inquiry chairman were approved following consultations with the Attorney General and the Department of Finance in accordance with the arrangements that applied generally to Inquiries at that time. The Government also approved the terms of reference of the Inquiry subject to any modifications which the Minister considered necessary following consultation with key parties. In February 2001 at a meeting with the chairman the Minister confirmed that the interpretation of the terms of reference was strictly a matter for the chairman. At that stage it was agreed to extend the timeframe for her work from six months to 18 months i.e. until September 2002.

At a meeting with PFJ shortly after the Government decision to establish the Inquiry, the Minister assured the group that the workings of the Inquiry were independent of him and of the Department, and that there was no question of dictating to the chairman what she should or should not do. In this context it was essential that the Inquiry was completely independent in carrying out its investigation, particularly as the Department itself was under investigation.

At the outset of the Inquiry, the Department had no reason to believe that the task could not be completed within the six-month time-scale that was originally envisaged. For example, the then most recent Tribunal of Inquiry into the Blood Transfusion Service Board which the Department had dealt with and which was equally emotionally-charged had been completed within 5 months. In the light of this, the six month time-scale seemed reasonable.

Considerable delays were experienced in obtaining suitable accommodation for the Inquiry, which ultimately did not become available until January 2001 despite the best efforts of the Department and the OPW. In addition, there were difficulties in sourcing clerical and administrative staff to assist the Inquiry. The combination of these factors meant that the Inquiry only became operational in March 2001.

The first formal indication that the Inquiry was running behind schedule was in August 2002 when the chairman advised the Minister that the Inquiry was a long way from reaching a stage at which a report would be available and she sought an extension of the time-scale for the Inquiry. At the request of the Minister the chairman submitted a Progress Report in October 2002 which indicated that the chairman was not in a position to estimate the timescale for completion of the work of the Inquiry and that she considered that it would be some considerable time before the report could be completed. The Minister and the Department were concerned at the absence of a definitive time scale. Considerable thought was given to possible options to expedite the Inquiry, including the possibility of effecting changes in the terms of reference. Having taken advice, the Minister came to the conclusion that it would not be practicable, at that stage, to revise the terms of reference or to replace the Inquiry with some new structure. One of the primary concerns was that any such change could invalidate the work done to date such as interviews with witnesses and could mean having to start the investigation afresh. A further concern was that any move to alter the terms of reference might fuel demands from PFJ for a statutory Tribunal of Inquiry.

Having decided against a change in the terms of reference, the Minister, at a meeting with the chairman and her legal team in December 2002, stressed the need to expedite the investigation. It was agreed that a report on paediatric hospitals would be provided by the end of 2003, to be followed by reports on maternity hospitals and general hospitals at six month intervals. The chairman indicated that her legal team would need to be augmented in order to achieve these revised deadlines. The Department sought sanction from the Department of Finance for an increase in the legal staffing but this was not

forthcoming. In the light of this, the chairman advised the Minister in June 2003 that the deadline of end 2003 for the completion of the report on paediatric hospitals might not be achievable. However, she undertook to keep the matter under review with a view to making a more definitive statement within the following two months or so. In the event, on 16 October 2003 the chairman wrote to inform the Minister that she would be unable to furnish the report by the end of that year. Her letter, which was accompanied by a 12 page progress report, did not specify when it was anticipated that the report would become available. The Minister met with the chairman and her legal team on 17 November 2003 and expressed his concern that the deadline for the paediatric hospital report would not be met.

In April 2004 the Inquiry advised that, with some exceptions, it was at the end of the second stage of its work in relation to the paediatric hospitals i.e. the information gathering was complete and the issue of analysing the information and establishing which matters remained in dispute had been concluded. The Inquiry was next to consider the third and final stage of its work, which was the resolution of matters in dispute and the conclusion of the Report. The Inquiry added that it was keeping in mind the need to be in a position to commence the work in relation to the maternity hospitals as soon as the paediatric report was completed.

In July 2004, the Attorney General, on behalf of the Government, conducted a review of all Tribunals and Inquiries then in being to establish their likely completion dates. On 1 September 2004 the Government decided, inter alia, that the chairman should be informed that the Inquiry should furnish to the Minister for Health and Children not later than 31 March, 2005 a Final Report based on all information and evidence obtained by and available to the Inquiry at that time and that the Inquiry would then cease to exist.

With regard to the lessons learnt the Accounting Officer stated that, although the terms of reference were approved by the Government, it would have been preferable if the capacity to interpret these, and to provide input to the methodology to be employed, had been reserved. However, for the reasons set out above, this was not possible in this instance.

It would have been preferable if the contractual arrangements with the chairman and her legal team had been so structured as to provide certainty for early completion of the work. However, the terms and conditions were set in accordance with the arrangements that applied generally to Inquiries at that time and it is not clear that it would have been possible to secure the services of the relevant people on any other basis.

It would have been preferable if provision had been made for interim progress reports. Had this been the case, the Department would have been alerted at an earlier stage that there were problems with the timeframe for the Inquiry. However, when it became evident in October 2002 that it would be some considerable time before the report would be presented, the Minister decided that it would not be practicable, at that stage, to revise the terms of reference or to replace the Inquiry with some new structure. Accordingly, regular interim reports would not necessarily have changed the outcome.

With regard to the costs incurred by the HSE (formerly the Health Boards) the Accounting Officer informed me that the Department provided specific funding for Inquiry-related expenditure to the Eastern Regional Health Authority (and subsequently the Health Service Executive), which, for the period 2000-2005, amounted to €6,350,000. The Department does not have information in relation to expenditure incurred by health boards/ hospitals outside the former ERHA region.

# Chapter 14

# Health Service Executive

# 14.1 Discretionary Medical Cards

## Introduction

Section 45 of the Health Act 1970 (the Act) provides that adults and their dependants have full eligibility for health services if they are "unable without undue hardship to arrange general practitioner, medical and surgical services for themselves and their dependants". The Act gives the Minister for Health and Children the power to make regulations specifying a class or classes of people who may be deemed to meet this criterion. No such regulations have been made.

There are a number of groups who are entitled to full eligibility for health services regardless of means. These include people over the age of 70, certain EU migrant workers, persons affected by the drug thalidomide and persons with retention entitlement under government schemes designed to encourage people into employment. Apart from these groups, medical cards are issued by the Health Service Executive (formerly by the health boards) to persons who, in the opinion of the HSE are unable to provide general practitioner medical and surgical services for themselves and their dependants without undue hardship. In practice, cards are issued largely on the basis of an assessment of the applicant's income. Income guidelines for the award of medical cards are drawn up each year by the HSE. People whose income is below the guideline figure for their circumstances get a medical card[50]. In general, those whose income is above the guideline figure do not qualify unless they have particularly high medical expenses or there is other evidence of hardship. The term " discretionary medical card" has come to be applied to cards awarded to persons whose income exceeds the guideline figure.

## Payments to Doctors for Discretionary Medical Cards

In 2001 the Department of Health and Children agreed with the Irish Medical Organisation (IMO) that, pending an examination of the discretionary medical card area, a sum of €2.54m would be paid to doctors under the General Medical Services Scheme (GMS) in respect of services to certain discretionary medical card holders. The figure of €2.54m was arrived at in the light of the Department's understanding that there were about 20,000 discretionary medical cards in issue. The money was allocated to individual doctors in proportion to GMS patient panel size as at 1 January 2001. The payment was in addition to the normal capitation payment made to doctors for their GMS patients.

In informing the health boards of the agreement with the IMO, the Department indicated that the examination of the discretionary medical card area would commence in 2001 and would seek to determine the nature and extent of discretionary cards in the GMS scheme. In the event of the examination not being completed by the year-end, with appropriate agreed alternative arrangements put in place, the sum of €2.54m adjusted for national pay increases would also be paid in 2002 on the same basis.

In April 2002, the Department wrote to the Chief Officer in the General Medical Services (Payments) Board, now the Primary Care Reimbursement Service (PCRS) and part of the HSE, stating that the payments for 2001 should be increased from €2.54m to €9.52m. This was on the basis that the Department now believed that the estimated number of discretionary medical cards was 75,000 and not 20,000 as previously thought. The arrears for 2001 were to be paid in 2002 and the payment for 2002 was to be made on a monthly basis in proportion to the size of each doctor's GMS patient panel. A second letter in April 2002 from the Department to the health boards and the GMS clarified that the additional payment to doctors in respect of discretionary cards was not intended to remunerate them in respect of all discretionary card holders. The Department indicated that, in this context "discretionary medical cards are understood to refer to those given to persons who, although significantly above the income guidelines

[50] A new GP Visit Card scheme was introduced in the 2005 Budget. The scheme provides free access to GP services only, for eligible individuals and families. Income guidelines are 25% higher than for medical cards.

for medical card eligibility, would by virtue of a condition or illness, necessitate a GP visitation rate significantly above the norm, thereby incurring increased costs." This was a significant narrowing of the definition of a discretionary medical card for the purpose of paying the extra amount to GPs.

The Department also indicated that when the actual numbers covered by discretionary medical cards became known an adjustment to the aggregate amount for each year, e.g. the €9.52m for 2001, would be made. The Department also asked for details of required changes to the systems in the GMS and at health board level in order that these more narrowly defined discretionary cards could be identified and payments could be made on foot of actual numbers. In a letter to the health boards, the Department stated "health boards should take the necessary steps to ensure that it is possible in future to associate discretionary medical cards with individual doctors for payment purposes."

€10.046m was paid in 2005 in respect of 75,000 cards. Each year since it issued the original instruction, the Department has confirmed in writing that payments should continue under the arrangements. A total of €50.7m has been paid out to GPs under these arrangements up to 31 December 2005.

# Audit Objectives

The audit objectives were

- To determine if the discretionary medical card scheme operated in a uniform way across the health service
- To review what progress had been made in moving towards paying doctors for the actual numbers of discretionary card holders on their panels, as originally envisaged by the Department in 2001.

As part of the audit, the HSE regions were asked to provide details of all current GMS Medical Cards on their systems as at 31 December 2005 and the numbers which had been awarded on a discretionary basis. The PCRS provided details of the number of GMS medical cards on its system.

# Audit Findings

## Operation of Scheme

Table 46 shows the total number of discretionary medical cards issued by region, discretionary cards as a percentage of eligible individuals and discretionary cards as a percentage of eligible family units.

**Table 46– Discretionary Medical Cards by HSE Region**

| Region | Number of Discretionary Medical Cards Issued | Discretionary cards as % of eligible individuals | Discretionary cards as % of eligible family units |
|---|---|---|---|
| Eastern | 7,418 | 2.17 | 3.19 |
| Midland | 4,885 | 6.98 | 10.33 |
| Mid Western | 4,950 | 4.94 | 7.18 |
| North Eastern | 1,428 | 1.43 | 2.17 |
| North Western | 2,915 | 2.95 | 4.76 |
| South Eastern | 8,415 | 6.06 | 9.09 |
| Southern | 11,878 | 6.85 | 9.64 |
| Western | 3,794 | 2.84 | 4.17 |
| **Total** | **45,683** | **3.95%** | **5.84%** |

As the results shown in Table 46 seem to suggest that the scheme is not administered across the country in a uniform way, I asked the Accounting Officer the basis on which discretionary medical cards are

awarded and for an explanation for the significant variations in the percentage of discretionary cards to eligible persons between the different HSE regions.

The Accounting Officer informed me that in the first instance every application for a medical card is assessed based on the national income guidelines. In cases where applicants are deemed to be in excess of the guidelines the HSE can take account of extenuating medical and or social circumstances of applicants. Medical circumstances might relate to a person or indeed family unit who, despite being in excess of the income guidelines, require frequent visits to their GP and outlay on drugs or medicines due to family member(s) having an established medical condition, such that the costs of meeting their medical needs outweighs the assessed income excess. An example of a social circumstance could be a family unit where, despite being assessed as being in excess of the means guidelines, the HSE becomes aware that the bread winner has an addiction problem and is not adequately supporting the spouse and children. To alleviate the ensuing hardship, the HSE can exercise its discretion and grant a medical card to the spouse and children in such circumstances.

The Accounting Officer stated that geographical variations in the percentage of discretionary medical cards as a proportion of all cards is an issue that warrants further examination and this will be conducted as part of a process currently under way to validate the total number of discretionary medical cards. It should be noted however, that the HSE has issued standardised national guidelines in the last year which deal with, among other things, the exercise of discretion in the issue of medical cards.

## Establishing the Number of Discretionary Cards

The remuneration of doctors for medical cards assumes the existence of 75,000 discretionary cards. The figures provided by the HSE regions suggest the real figure may be far lower, perhaps as low as 45,600. The figure recorded on the PCRS database is lower still at 36,000. The Accounting Officer has indicated that the ongoing validation exercise in all HSE regions is likely to reveal that the figure is between 65,000 and 68,000.

These figures refer to all discretionary cards regardless of the circumstances that gave rise to their issue. On the other hand, it is clear from the Department's correspondence to the health boards in 2002 that the intention was to pay additional remuneration to doctors only in respect of cards issued to persons whose income was "significantly" above the income guidelines and who by virtue of a condition or illness required a rate of GP visit "significantly" above the norm.

The HSE's national guidelines on medical card entitlement lists the following matters as factors to be taken into account in considering whether undue hardship arises in any case

- Illness or medical circumstances
- The cost of providing general medical and surgical services
- The cost associated with the provision of medical, nursing and dental treatment
- The cost of physiotherapy and speech and language therapy
- Transport cost to hospitals and clinics
- Addictions such as drink, drugs and gambling
- Poor money management
- Social deprivation – including poor home management
- The cost of medical aids and appliances.

It is clear from this list that there is a range of circumstances in which discretionary medical cards might be issued that might not involve a rate of GP visit in excess of the norm. It follows that the discretionary

cards that give rise to the extra payment to doctors is likely to be less than the total number of discretionary cards recorded on the HSE systems.

I was concerned that payments continued to be made on the basis of the 75,000 estimate, which now appears to be too high, and that the payments continue to be made to doctors in proportion to patient panel size instead of on the basis of the actual number of their patients holding discretionary medical cards.

In response to my enquiries, the Accounting Officer informed me that at the time of the agreement with the IMO the former health boards were not routinely collecting details such as frequency of GP visits by individual patients or details of patients' income levels. The best available figure was the estimated number of all cards where the applicant's income was above the guidelines. He considered this to be a critical point because the number involved i.e. 75,000 was not and could not be sufficiently refined to reflect only those whose incomes were considerably above the guidelines and who require frequent visits to their GP.

The Department, as the brokers of this agreement, had been requested on a number of occasions to give a working definition of the discretionary cards that were intended to be comprehended by this agreement (i.e. what is the threshold for "significantly above the guidelines" etc.). As part of the Schemes' Modernisation Programme, the HSE has even gone as far as suggesting a definition to the Department, but a determination on this is still awaited. In anticipation of a clear definition against which an actual assessment of discretionary cards can be based, the HSE has introduced a coding system in which discretionary cards are categorised according to income excess bands. This enhancement will make it easier to calculate the exact number of such cards going forward. On renewal of each discretionary medical card, HSE areas are collecting data which enables coding of the card into one of four income bands above the qualifying income thresholds. All new discretionary medical cards are subject to this coding system also. The income coding bands are up to 25%, 25%-50%, 51%-85% and in excess of 85% above the qualifying income threshold for a medical card. The coding exercise was rolled out nationally in mid-2005. Given that the average period of issue for medical cards is 2 years, the majority of cards will be re-issued and appropriately coded within a 2 year timeframe. A definition from the Department is still a necessity however.

The Accounting Officer said that in his opinion payments can be made in respect of actual numbers of discretionary medical cards, subject to clarifications of definitions by the Department and application of those definitions to each individual record thereafter. There would, however, be a considerable workload in doing this first time off, but, once done, it would then become a data management issue. The recalculation of amounts paid to date would have to be considered with the Department following the validation exercise and clarification of definitions.

## Views of the Department of Health and Children

In light of the comments of the Accounting Officer, I asked the Department of Health and Children for its observations on the matter.

The Department's Accounting Officer informed me that the arrangement regarding medical cards agreed with the IMO arose in the context of difficult industrial relations negotiations aimed at giving effect to the Government's decision to extend eligibility for a medical card to all persons aged 70 or over. During those negotiations, the IMO tabled a wide range of issues which they sought to have resolved before their members would agree to provide a service to all over 70s, free of charge to the patient. In particular, the IMO sought extra payment in respect of discretionary medical cards on the basis that these were cards awarded to a significant number of persons not by reference to their means but because of a requirement to visit a GP frequently. The IMO argued that these patients represented a predictable high workload and that, instead of having a balance of low and high workload patients, GPs' patient panels were becoming

increasingly skewed towards high demand clients. Payments were made on a notional figure of 20,000 discretionary medical cards, subject to review.

In 2001 and 2002, the Department made a considerable effort to obtain information from the health boards in relation to the number of discretionary cards. In several cases, the health boards were unable to provide the information and it became clear that the interpretation of the term "discretionary medical card" varied considerably between health boards.

A further difficult industrial relations situation developed in March 2002 and there was a threatened withdrawal by GPs from the GMS scheme. The issue of discretionary cards was again raised by the IMO who contended there were an estimated 75,000 persons covered by discretionary cards. The information the Department had by then obtained from the health boards supported this figure and it was decided payment would be made on the same basis as previously in respect of 75,000 discretionary cards.

The Department continued to request the health boards to put systems in place to identify the actual number of discretionary cards so they could be associated with individual GPs' panels. The Department's standard definition of "discretionary medical card" which it issued in April 2002 was meant to enable the health boards adopt a common approach. The definition was intended to differentiate between persons awarded a card based on means, even if they were marginally above the income assessment threshold, and those where the impact of a medical condition was the main determining factor. It was anticipated that when the health boards had established accurately the number of discretionary medical cards, it would provide a basis to re-engage with the IMO on the matter.

The Accounting Officer also stated that the whole issue of discretionary medical cards will now have to be addressed in the context of a major review of all aspects of the GMS contract which has been underway since late 2005 under the auspices of the Labour Relations Commission (LRC). He said it would be inappropriate at this stage to deal with the matter outside of the LRC process and that there were a number of other issues that would need to be taken into account in addressing the matter -

- The significant adjustments made to the system and guidelines for assessment of applicants for a medical card in 2005
- The introduction of the new GP visit card
- A current review of eligibility legislation
- The draft national partnership agreement "Towards 2016" which provides for a review of the eligibility criteria for the assessment of medical cards.

# 14.2 Nursing Home Subventions

The Health (Nursing Homes) Act 1990 (the Act) provided for the introduction of the Nursing Home Subvention Scheme by health boards. The purpose of the scheme is to provide financial support for eligible persons who avail of private nursing home care. Eligibility is determined by reference to two criteria

- The degree of dependency of the person
- The person's means and circumstances.

The way in which these two criteria should be assessed is set out in detail in regulations introduced in 1993 and amended on a number of occasions up to 2005. Application for subvention can be made either by the person concerned or someone acting on his or her behalf. The HSE became responsible for administering the scheme in 2005, following the dissolution of the health boards.

## Assessment of Dependency

Dependency is determined by means of a clinical assessment. The assessment involves an evaluation of the ability of the person, in respect of whom a subvention has been sought, to carry out the tasks of daily living, the level of social support available to the person and the medical condition of the person. Assessment is based on of degree of mobility, ability to dress unaided, ability to feed unaided, ability to communicate, extent of orientation, level of co-operation, ability to bathe unaided, quality of memory and degree of continence. There are three levels of dependency:

Medium Dependency – the person requires nursing home care because the appropriate support and nursing care required by the person cannot be provided in the community.

High Dependency – the person's independence is impaired to the extent that s/he needs nursing home care but is not bed bound.

Maximum Dependency – the person's independence is impaired to the extent that s/he requires constant nursing care.

The level of dependency assessed under the scheme determines the maximum weekly rates of subvention. The current rates are

- Medium Dependency €114.30 per week
- High Dependency €152.40 per week
- Maximum Dependency €190.50 per week.

## Assessment of Means and Circumstances

The regulations provide that in assessing the means of a person the HSE must take all sources of income into account, including wages, salary, pensions, allowances, payments for part time and seasonal work, income from rentals, investments and savings and all contributions from whomsoever arising. The HSE is permitted (but not obliged) to consider any assets of the person in assessing the means.

While the HSE has discretion as to whether or not to take assets into account in assessing means, there are specific rules set out in the regulations in relation to how assets are to be taken into account should it choose to do so. In particular, the HSE may refuse to pay any subvention if either of the following apply

- the claimant's principal residence is valued at €500,000 (for properties in the Dublin area) and €300,000 (for the rest of the country) and the claimant's income is greater than €9,000 per annum or
- the value of the claimant's assets (excluding principal residence) is greater than €36,000.

There are two significant exceptions to these rules

- the first €11,000 of any assets must be disregarded
- a claimant's principal private residence is not taken into account if it is occupied immediately before the application and continues to be occupied by the claimant's spouse, a child aged under 21 or in full-time education or a relative in receipt of disability allowance, blind person's pension, disability benefit, invalidity pension or Old Age Non Contributory Pension.

## Enhanced Subvention Payment

Articles 22.3 and 22.4 of the Nursing Home (Subvention) Regulations make provision for the payment of enhanced subvention. Effectively, this means that the HSE may make an enhanced payment in addition to the maximum weekly rate. The sum of these amounts, when taken in conjunction with the individual's available income can in some cases meet the full cost of the bed in the private nursing home. Enhanced payments arise in situations where, even with the maximum subvention, the family or individual cannot afford to meet the shortfall in costs of nursing home care and there are long waiting lists for public beds. The amount of each enhancement will differ, as the amount granted is based on the person's income, their level of dependency, the nursing home fees and on budgetary constraints.

There are no clear rules in the regulations about who is entitled to get enhanced payments. In practice, the making of enhanced payments is a matter for each HSE Area and each case is assessed individually. There is no maximum amount for enhanced subvention in the regulations and it is a discretionary matter for the relevant Local Health Office (LHO) areas.

## Legal Cases

A number of High Court challenges (104 at July 2006) are being taken to test the constitutionality of the Health (Nursing Homes) Act 1990 and the related regulations. The legal cases relate to entitlement and eligibility, with the claimants arguing that they had to use private nursing homes, as there were no public beds available.

## Expenditure - 2005

The total amount paid out under the scheme in 2005 was €109.8m of which €49.2m was in respect of enhanced subvention.

# Audit Findings

In the course of the audit, the 19 LHOs responsible for administering the scheme were surveyed to establish the extent of the different approaches to the treatment of principal residence in assessing means and the payment of enhanced subvention. The survey did not seek to establish whether the means testing of income was carried out in a consistent way.

### Assessment of Principal Residence

The survey revealed that there were some inconsistencies in how a principal residence is treated in assessing means. Specifically, 7 LHOs indicated that they do not take a principal residence into account if the house is occupied by a relative. This is not in line with the regulations which provide that the principal residence should only be disregarded if it is occupied by a spouse, a child aged under 21 or in full-time education or a relative in receipt of certain Social Welfare benefits. While the other 12 LHOs took the principal residence into account for means purposes in accordance with the rules, two areas indicated that they had not done so until December 2005. The main reason advanced for this approach was that property prices in these areas were low.

### Payment of Enhanced Subvention

The survey also indicated widely different practices in calculating the amount of the enhanced subvention. In summary

- 10 LHOs pay a maximum payment between €360 and €680 -less assessable income
- 3 LHOs pay up to the cost of the bed less assessable income
- 5 LHOs pay between €38 and €250 - plus the standard subvention
- 1 LHO pays an agreed amount.

Applying the different practices to a typical case showed that an individual or supporting family members could end up paying varying amounts to meet the cost of private nursing home fees depending on the area in which they were located. For example, in the Southern, North East and three Dublin/East HSE areas no contribution would be required, whereas in the South East, Mid-West and Western areas a substantial contribution could be required. Moreover, in some counties in the Midland and North West areas a substantial contribution could be required, while in other counties in the same areas no contribution would arise.

The results of the survey reflect the approach taken by LHOs in the generality of cases. However, in cases of hardship LHOs may exercise discretion to increase the amount of enhanced subvention to cover the balance of the cost of a nursing home bed not met by the individual. The LHO will often seek to negotiate an agreed charge with the nursing home or to fix the charge for a period of around 12 months. The instructions used by LHOs do not give any guidance on how such discretion ought to be exercised, and it is not possible to say whether discretion is exercised in a reasonably consistent basis across LHOs.

## Audit Concern

In light of the apparent inconsistencies in approach, both to assessment of means and to the payment of enhanced subvention in the HSE regions, I sought the views of the Accounting Officer.

## Accounting Officer's Response

The Accounting Officer informed me that the discretionary nature of the enhanced subvention, as it operated in the old Health Board system, is fundamental to the inconsistencies which now exist and which are being addressed by the HSE in the context of a unified delivery system. In the old Health Board system, each Health Board established criteria for a methodology of payment of basic and enhanced subvention arrangements which generally would have been reported formally to the Health Boards' members in the context of the monthly Board meetings, etc. However, the overall extent of discretionary support would be influenced by budgetary constraints and the amount of funding provided by the Department of Health and Children.

In the old system each individual Health Board was a legal entity in its own right and was entitled to provide for such arrangements as part of the annual service plans agreed with the Department.

The Accounting Officer detailed the underlying issues giving rise to the inconsistencies in the operation of the Nursing Home Subvention Scheme nationally

- The 1993 Subvention Regulations were open in a number of sections to varying interpretations
- The guidelines which accompanied the regulations were not detailed and comprehensive
- Lack of communication between Health Boards led to inconsistencies in interpretation of the legislation and guidelines
- There was a significant degree of variation between Health Boards in resources available to services for the elderly e.g. long stay beds, etc.
- There were varying per capita budgets allocated to Health Boards for the subvention scheme
- Differing demographic and geographical profiles between Health Boards resulted in differing emphases within Health Boards.

The demand for enhanced subvention in any area tended to be influenced by a number of factors

- The percentage of the population over 65 in need of continuing care
- Total number of continuing care beds available, both public and private, to meet that need
- Number of public beds available.

The ratio of public beds to the number of people over the age of 65 varied significantly between Health Boards. Where there were a large number of public beds available in local Health Board long stay hospitals, the demand for subvention within that area was reduced. Likewise, if a Health Board had few public beds available, proportionate to the local need, the pressure for support from the subvention scheme tended to be greater. In practice, this may have led to a more comprehensive enhanced subvention scheme in such Boards.

The cost of private nursing home care also varied widely between Health Boards. Currently, fees charged by private nursing homes can range from €550 per week to €1,100 per week depending on location. The main factors that determine these costs include local supply and demand for places and local costs such as building and staffing. The variation in private care costs is reflected in the value of enhanced payments.

As part of the transition of the Health Board system to the HSE, a comprehensive risk assessment was undertaken by the outgoing CEOs of the Health Boards at the time and this was provided by way of a report to the then CEO of the HSE. This document identified the risks associated with the merging of 11 Health Board structures to a unified system with the inconsistencies of interpretation of various services including the Nursing Home Subvention Scheme.

In the context of the varying degrees to which these inconsistencies existed in the old system, the Accounting Officer stated that there are arrangements which existed in the Health Boards, and continue to exist in the HSE, to deal with individual cases which arise where anomalies are highlighted arising from inconsistency in interpretation or application of the scheme. These cases are generally dealt with by the Appeals Officers and are also dealt with by Local Health Managers and Assistant National Directors as appropriate.

The HSE recognises that the move towards a unified system with a standardised interpretation and application of the legislation and regulations can only be implemented on a phased basis. This is because

of the resource issues involved and the necessity for arrangements to underpin the legislative and regulatory amendments through the Department.

Since the establishment of the HSE, arrangements are now being put in place to address the inconsistencies. In relation to Services for Older People, a National Steering Group has been established and through this process arrangements are being made to progress this agenda on a systematic basis. Within this national framework, a Working Group has been established and one element of its work relates to the development of a standardised approach towards the implementation of the Nursing Home Subvention Scheme across the health service. The Working Group's terms of reference include the effectiveness of current legislation in terms of

- The legislation's implications regarding equity of access
- Clarification of the HSE's legal obligations
- Identification of gaps and risks and the highlighting of their implications (financial and other) to the HSE.

The approach being taken by the HSE is to standardise the arrangements within the existing legislative and regulatory framework, while at the same time working with the Department to ensure a more appropriate and equitable legislative framework for the future. The underlying issues related to eligibility and entitlement and funding arrangements in relation to the provision of Long Stay Care for Older People, both public and private, have been the subject of ongoing consultation with the Department in the old Health Board system and also since the establishment of the HSE. The Department, in the Health Strategy and more recently following a Supreme Court decision on Long Stay charges, has confirmed that it is at an advanced stage in developing a comprehensive legislative and regulatory framework which will address the overall eligibility and entitlement for these services including the Long Stay Care for Older People.

The Accounting Officer concluded by stating that significant work had been undertaken over the past couple of years in this area and the Government established a high-level Departmental group chaired by the Department of An Taoiseach to address Long Stay Care for Older People, which will also address equitable arrangements for the funding of Long Stay Care for Older People going forward. This work is grounded in the Mercer and O'Shea Reports, and the HSE understanding is that recommendations will be going to Government shortly on the matter. The HSE is working closely with the Department in relation to these issues.

# 14.3 Extra Remuneration

Public financial procedures prescribed by the Department of Finance require that each Appropriation Account shows the total amount charged to the Account in respect of overtime and extra attendance, the number who were paid overtime and the highest individual overtime payment in the year. Because of the nature of the health service, the HSE Appropriation Account also includes details of extra remuneration in respect of allowances, night duty, weekend pay, on-call and other payments. Total expenditure on extra remuneration in 2005 was €585,651,417 as shown in Table 47.

**Table 47**

| | € |
|---|---|
| Allowances | 92,528,783 |
| Overtime | 187,148,078 |
| Night Duty | 64,451,495 |
| Weekends | 166,379,057 |
| On-Call | 49,019,852 |
| Other[51] | 26,124,152 |
| **Total** | **585,651,417** |

It should be noted that certain individuals receive extra remuneration in more than one category.

Total payroll costs for the HSE for 2005 (per the Income and Expenditure Account) was €4,029,586,638 of which extra remuneration represented 14.5%.

The results of an audit analysis of the 30 highest recipients of extra remuneration in the different categories[52] in each of the 10 former health board areas are shown in Table 48.

**Table 48 – Analysis of high earners**

| € | Overtime | Weekends | Allowances | NightDuty | On-call | Other | Total |
|---|---|---|---|---|---|---|---|
| 125,000 - 150,000 | 7 | 0 | 0 | 0 | 0 | 0 | 7 |
| 100,000 - 125,000 | 15 | 0 | 4 | 0 | 0 | 1 | 20 |
| 75,000 - 100,000 | 66 | 0 | 4 | 0 | 3 | 2 | 75 |
| 50,000 - 75,000 | 161 | 0 | 9 | 0 | 17 | 5 | 192 |
| 25,000 - 50,000 | 51 | 2 | 73 | 0 | 254 | 35 | 415 |
| 0 - 25,000 | 0 | 298 | 210 | 300 | 26 | 167 | 1,001 |
| **Total** | **300** | **300** | **300** | **300** | **300** | **210**[52] | **1,710** |

A further analysis showed that the 22 largest overtime payments (i.e. all those greater than €100,000) were to Non-Consultant Hospital Doctors (NCHDs). The 3 highest earners worked for 3,530; 3,193 and 2,419 hours in 2005 on top of their normal working week of 39 hours. This involved average overtime hours of 75; 68 and 51 hours per week respectively, for 47 working weeks.

[51] Other pay includes group and individual arrears apart from national agreements and miscellaneous allowances.
[52] Not all HSE areas categorise payments in the "other" category.

It should be noted that 28 of the 300 highest overtime earners were also in the top 30 recipients of payments from the other extra remuneration categories in their areas and received amounts ranging from €6,311 to €61,226 in this respect. Other high overtime earners may have been in receipt of payments in the other extra remuneration categories but were not in the top 30 recipients for their area.

While accepting that a level of extra remuneration payments will always be necessary and desirable because of the nature of HSE operations, I asked the Accounting Officer

- what measures the HSE has in place to ensure that resources expended on extra remuneration payments are used economically and efficiently
- what day-to-day management, budget control and monitoring procedures are in place in the HSE in relation to extra remuneration
- whether the HSE is satisfied that its attendance and rostering systems and controls are adequate to manage such significant additional payroll expenditure.

The Accounting Officer said he was acutely conscious of the need to ensure optimum use of resources, while minimising cost exposure or reliance on additional allowance / overtime etc, and always maintaining the levels of coverage for the provision of care. The HSE's Medical Manpower Managers continuously examine NCHD rosters in the interests of safe service provision, training and value for money, with a particular focus on reducing hours in the context of the European Working Time Directive (EWTD).

Day-to-day management and control of NCHD overtime relies on a requirement that all NCHD hours, including overtime, must be signed off by the supervising consultant. These hours, as recommended for payment by the consultant, are then matched against agreed service rosters for each grade and specialty. Claims for payment are checked against rosters and on-call rotas by payroll or medical administration staff under the supervision of a Medical Manpower Manager or Hospital Manager.

The nature of acute health service provision is such that emergency situations or delays at scheduled theatre or clinic sessions will arise intermittently, with a consultant requiring additional unrostered NCHD cover. Prior to 2006, monitoring and control of the cost of unrostered cover was effected by obtaining details of unrostered hours and routinely auditing and verifying them against hospital activity before payment for this additional unscheduled work. Where patterns of unrostered hours were developing, these were addressed with individual NCHDs and their supervising consultants as necessary.

The Accounting Officer informed me that the HSE is aware that NCHDs are working increasingly beyond their rostered hours, resulting in unsustainable overtime costs. In May 2006, the National Hospitals Office issued directions to all Hospital Managers in relation to unrostered NCHD overtime. The directions require that all NCHDs work in line with their rostered hours. Hospital Managers were instructed to approach individual consultants and inform them that the current budget cannot support unrostered NCHD overtime.

The new directions require Hospital Managers to

- confirm the roster for each individual specialty on the basis of service need
- remind all NCHDs directly of their individual unit roster and
- advise NCHDs that they will be paid for their rostered hours only and must finish duty at their rostered time.

A new control was introduced to the effect that any requirement for NCHD to work beyond his/her rostered hours must now have the prior approval of the Hospital Manager. This arrangement took immediate effect. It is supported by a policy of monitoring all overtime sheets to verify that the hours claimed have been approved by each Hospital Manager. Overtime claims which do not have the required approval will not be paid and will be returned to the individual NCHD for correction.

The Accounting Officer added that that the use of sophisticated rostering IT solutions may present local management with potential advantages in managing attendance levels and rostering arrangements. He indicated that the integrated HR information and payroll system (PPARS), which had been planned by the former health boards had been intended to address, inter alia, some concerns in this area. However, the HSE had suspended any further roll-out of this project until it is satisfied as to the value proposition involved.

## Consequences for Service Delivery

I also asked the Accounting Officer whether the recruitment of additional staff would increase the quality and quantity of service provided and reduce costs.

The Accounting Officer informed me that in certain cases the availability of additional resources would assist the situation and would have possibilities in terms of reducing reliance on overtime arrangements. There are, however, many factors which would be part of this equation including availability of skill mix etc. He assured me that the quality of service is never compromised. He also made the point that, at present, the HSE does not enjoy full flexibility to recruit additional staff, regardless of whether or not this would result in a reduction in extra remuneration levels or reliance on agency staff. There is an employment ceiling allocated to each element of the service and additional staff may not be recruited in excess of this ceiling. Dialogue is on-going with the relevant Government Departments on an overall adjustment to the HSE employment ceiling.

## Implication of the European Working Time Directive (EWTD)

The provisions of the EWTD, as they apply to NCHDs, were introduced into law in Ireland in 2004. As a result, the working hours of such doctors have been limited by law to a maximum average of 58 hours per week since August 2004. The 58 hour maximum is to be reduced to 48 hours on a phased basis over the period to August 2009. The Directive, and case law that emerged in recent years in relation to it, imposes other significant constraints on doctors' working hours. Doctors must not work more than 13 hours in each 24 hour period, and are entitled to 35 consecutive hours rest in every 7 day period, or 59 hours rest in every 14 day period. In addition, where the daily 13 hour limit is exceeded, then the doctor concerned will be obliged to take sufficient rest to meet the terms of the Directive and this will have implications for starting times on the following day. In the light of the levels of overtime noted in the course of the audit, I was concerned that the HSE was not complying with the terms of the Directive.

The Accounting Officer informed me that the terms of the EWTD are being adhered to in full in respect of 30% of NCHDs. In relation to the remaining 70% of NCHDs, discussions are continuing with the Irish Medical Organisation, under the auspices of the Labour Relations Commission, to agree arrangements which will effect a reduction in the hours of NCHDs to comply with the working hours and rest provisions of the EWTD.

An industrial relations process is in place which will oversee a number of pilot attendance arrangements for NCHDs in nine locations and which will be EWTD compliant. The pilots will last for 4 to 6 months during which they will be evaluated. In addition, it is envisaged that discussions on a revised contract for NCHDs will take place concurrently. The successful pilots should then be mainstreamed and a revised contract for NCHDs agreed.

# Chapter 15

# National Treasury Management Agency

# 15.1 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 €19.9m on administration in 2005 (€16.5m in 2004 as adjusted for FRS17).

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 2005 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 2005 and its balances at year end.

Table 49 shows the outturn for the National Debt in the five year period 2001-2005.

**Table 49 National Debt 2001 – 2005**

| | National Debt Outstanding €m | Debt Service Cost €m |
|---|---|---|
| 2001 | 36,183 | 2,379 |
| 2002 | 36,361 | 2,169 |
| 2003 | 37,610 | 2,277 |
| 2004 | 37,846 | 2,203 |
| 2005 | 38,182 | 2,238 |

The composition of the National Debt[53] at 31 December 2005 is shown in Table 50.

**Table 50 Composition of National Debt as at 31 December 2005**

| | €m |
|---|---|
| Medium/Long term Debt | 31,936 |
| Short term Debt | 3,688 |
| National Savings Schemes | 4,741 |
| Less: Domestic Liquid Assets | (2,183) |
| National Debt | 38,182 |

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 €25.6m.

[53] The National Debt is stated on the basis of nominal amounts of principal originally borrowed.

# 15.2 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 2006 they reported to me on their audit of the 2005 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 51.

**Table 51 Post Office Savings Fund**

| | **2005 €m** | **2004 €m** |
|---|---|---|
| Liability in respect of funds due to depositors and creditors | 1,489 | 1,304 |
| Value of related investments held by Post Office Savings Bank Fund (at cost prices)[54] | 1,499 | 1,315 |
| **Surplus at 31 December** | **10** | **11** |

[54] The market value of the investments held by the Fund was €1.6m less than their cost price.