



Comptroller and Auditor General

Report on Value for Money Examination

Office of the Revenue Commissioners

Value Added Tax Collection and Control

Baile Átha Cliath
Arna fhoilsiú ag Oifig an tSoláthair

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The report was prepared on the basis of information, documentation and explanations obtained from the Office of the Revenue Commissioners

The draft report was sent to the Office of the Revenue Commissioners and its comments were requested. Where appropriate, these comments were incorporated in the final version of the report.

Report of the Comptroller and Auditor General

Value Added Tax Collection and Control

I have, in accordance with the provisions of Section 9 of the Comptroller and Auditor General (Amendment) Act, 1993, undertaken a value for money examination on Value Added Tax collection and control

I hereby submit my report of the above examination for presentation to Dáil Éireann pursuant to Section 11 of the said Act.

A handwritten signature in black ink, appearing to read 'John Purcell', with a large, stylized initial 'J' and a long, sweeping horizontal stroke extending to the right.

John Purcell
Comptroller and Auditor General

31 December 1997

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Summary

Value Added Tax (VAT) collection and control procedures are based on a self assessment system. The overall objective of the system is to maximise the collection of VAT revenue by maximising the levels of voluntary compliance and by deterring evasion. The principal compliance elements in the system are the checking of submitted VAT returns and the follow-up of overdue returns and payments (collection work), the checking of the accuracy of VAT returns through a VAT audit (control work) and the referral of debts for enforcement action (enforcement work)

There are two approaches to VAT collection and control work. an equity approach which applies the same collection and control procedures to all traders regardless of their size or VAT liability and an efficiency approach which schedules audit and enforcement work based on the amounts most at risk. In recent years the Office of the Revenue Commissioners (Revenue) has moved towards the efficiency approach.

The purpose of the examination was to review the current organisation of VAT collection and control procedures with particular reference to the results achieved from registration, collection, control and enforcement work over the past five years. The examination also sought to identify opportunities for further system refinements which would contribute to increasing the effectiveness of the procedures.

Registration Practices

Procedures performed at registration contribute to the effectiveness of the later collection and control procedures. The number of registered traders has increased steadily over recent years and stood at almost 150,000 traders in May 1997. Revenue relies on a mix of formal and informal information sources to detect unregistered traders who exceed the registration threshold. The examination found that the use of information obtained from audit activity and from the Companies Registration Office should be further developed to assist in detecting unregistered traders.

The detection of unregistered liable traders is hindered by a lack of knowledge of the extent of this area within the black economy. Several methods for estimating the population of these unregistered traders have been proposed but no reliable approach has emerged and Revenue has not attempted this exercise. The activity to detect unregistered traders is co-ordinated across all tax heads and is controlled by setting national detection targets. As the quality of information on detection rates improves, better estimates of the unregistered trader population should be possible which, in turn, should impact on Revenue's approach to detection.

At registration, traders are assigned a low, medium or high risk rating which is intended to be used for planning VAT audits but is not yet fully developed. The refinement of the risk rating depends on the quality of information available to Revenue about the trader's business affairs. Since 1995, there has been a policy for district tax officials to make new business education visits to traders to provide them with information about the operation of the VAT regulations and their obligations. These visits could also be used to gather information needed for risk rating. The examination found that targets for making education visits are not being met by some

district tax offices and there is a need for Revenue to re-emphasise the importance of the visits.

Self Assessment and Collection

Revenue regards traders as being compliant if the VAT3 return and any associated payment is received in the month in which it is due. The examination found that there has been a gradual improvement in collection rates since 1993. By the end of 1996, on average, 69% of returns and 93% of VAT revenue were collected within two months of the due month.

Where traders are not compliant, the Collector-General's Office may issue a Section 22 estimate of liability. In the past, there was a tendency to overstate the estimate to encourage the trader to discharge it by submitting a VAT3 return. Inspectors of Taxes may also issue Section 23 assessments which may adjust a VAT3 return or replace a Section 22 estimate. There was also an historical tendency for Section 23 assessments to overstate the trader's liability. As a result, for all VAT years up to 1993, there has been a build up of notional VAT arrears for Section 22 estimates and Section 23 assessments of £62 million and £105 million respectively.

Arrears Verification Units have been established in each district tax office to determine the true outstanding liability and reduce the level of arrears by discharging the estimates, collecting the amounts due or referring arrears for enforcement or write-off. The examination found that the Arrears Verification Units have made progress in reducing the VAT arrears. Furthermore, the practice of issuing Section 22 estimates and Section 23 assessments has been refined since 1994. This, together with improvements in the computer information systems, has increased the quality of information available to Revenue concerning the collectibility of the arrears.

An annual accounting scheme, where only one return and payment was required per year, was introduced in 1989 for small traders whose annual VAT liability was less than £5,000. There was a high level of defaulting traders in this group and it was not possible to apply the normal collection procedures. While a special follow-up campaign has brought some results, Revenue now encourages small traders to set up direct debit arrangements, which is a more effective system for collecting VAT.

VAT Audits

A programme of audits is performed to maximise VAT revenue by detecting underpaid VAT and to provide assurance as to the overall level of voluntary compliance.

Audits can be performed for single tax heads such as VAT or for all tax heads (comprehensive audits). The detection of underpaid VAT is best served by an audit programme which targets the groups where tax is considered to be most at risk. The assurance of the overall level of voluntary compliance is achieved by selecting some audit targets at random. Trade and industry organisations believe that there is too much audit emphasis on the collection of additional VAT and not enough on the

assurance objective. The level of random audits performed is very low. No single tax head VAT audits are selected at random and only 52 out of 3,969 comprehensive audits performed in 1996 were selected at random.

Although it is inevitable that some audits will not result in additional VAT revenue (i.e. a nil yield), there is a higher risk that randomly selected audits will result in a nil yield. The incidence of nil yielding audits could be used as a performance measure for the appropriateness of the mix of targeted and random audits.

The planning of single tax head VAT audits has improved in recent years mainly due to the availability of better information and to the adoption of a sectoral approach. These audits are interrelated with audits under other tax heads. However, no formal risk analysis techniques or software are used in the planning process. The number of single tax head VAT audits performed has fallen from 13,158 in 1993 to 8,424 in 1996 due to a reallocation of resources towards comprehensive audits and an increase in the duration of audit to enable more VAT periods to be covered. The result is that the average yield per audit has increased from £2,356 in 1993 to £3,917 in 1996.

Although Revenue's accounting systems are not designed to record the full cost of performing an audit, the difference between the audit yield and the direct manpower cost suggests that VAT audit activity is good value for money and that the allocation of more resources to audit would further increase the yield. Revenue should improve procedures to monitor more accurately the cost effectiveness of VAT audits.

Enforcement

Enforcement procedures are not confined to particular tax heads. The principal methods used are sheriff and solicitor enforcement. Certificates covering specific tax arrears are sent to sheriffs for action in situations where it is believed that the trader possesses business assets which may be seized and used to recover the tax debt. Solicitors, including the Revenue Solicitor, pursue cases considered unsuitable for sheriff enforcement.

The costs and poundage involved in sheriff enforcement are borne by the defaulter. This acts as an incentive for settling liabilities directly with the Collector-General's Office. Approximately £343 million (25%) of the face value of certificates issued in respect of VAT arrears in the period 1993 to 1996 was collected directly or indirectly as a result of sheriff enforcement. The examination found that sheriff enforcement has a higher relative success rate than the use of Section 22 estimates or the issuance of reminders and demands.

Cases amounting to £60 million in VAT arrears were referred to solicitors for enforcement between 1993 and 1996. A total of £18 million was collected during this period.

Value Added Tax Collection and Control

1 Introduction

- 1.1 Value Added Tax (VAT) is a tax on consumer spending which was introduced in November 1972 under the Value Added Tax Act, 1972 as part of Ireland's preparation to join the European Union (EU). VAT replaced turnover tax and wholesale tax.
- 1.2 The yield from VAT has risen steadily over the past 10 years and amounted to some £3.1 billion in 1996. This figure is net of £0.9 billion in VAT repayments. VAT is a significant source of government revenue and accounted for over 57% of indirect taxes and 26% of all taxes, duties and levies collected by the Office of the Revenue Commissioners (Revenue) in 1996. In EU terms, the proportion of VAT revenue to total tax revenue in Ireland is high, being surpassed only by Greece. The current level of VAT yield is attributed by Revenue to continuing consumption buoyancy and improvements in VAT compliance.

The VAT Compliance System

- 1.3 VAT is collected by VAT registered traders on their supplies of goods and services. Each such trader, in the chain of supply from manufacturer to retailer, charges VAT on sales and is entitled to deduct from this amount the VAT paid on purchases. The effect of offsetting purchases against sales is to impose the tax at each stage of production on the added value. The final consumer, being unregistered for VAT, absorbs the VAT as part of the purchase price.
- 1.4 A taxable person may be an individual, company or other body. Taxable persons whose annual turnover from supplies of taxable goods and services, or the value of whose acquisitions of goods from traders in other EU States, exceed, or are likely to exceed, certain limits are obliged to register for VAT.
- 1.5 Applicants for registration must complete a form and return it to the Taxes Central Registration Office or to the local inspector of taxes as appropriate. Registration is effective from the beginning of the next taxable period.
- 1.6 A VAT registered person normally accounts for VAT on a bi-monthly basis (January/February, March/April etc). The return is made on the VAT3 form and this form together with a payment for any VAT due must be furnished to the Collector-General on or before the 19th day of the month following the end of the taxable period. There is also a facility for monthly payment by direct debit or for annual payment in the case of small traders.
- 1.7 Returns which show an amount of tax due must be accompanied by payment in respect of the amount stated. If the VAT due is less than the total VAT deductible, the excess is repaid to the registered person by the Collector-General. If a taxable

person fails to make a VAT return by the due date, Revenue has power to make an estimate of the VAT due under Section 22 of the Value Added Tax Act, 1972

- 1 8 If a trader fails to comply with his legal obligations, the case can be transferred for enforcement action. Revenue also carries out a programme of Revenue audits to maximise the level of compliance under the self assessment system by verifying the validity of returns submitted by traders
- 1.9 The current general objective of VAT compliance is to maximise the collection of short term and longer term VAT revenue. This is achieved through maximising the levels of voluntary compliance and by deterring avoidance and evasion
- 1 10 There are two broad approaches to VAT compliance, the equity approach and the efficiency approach.
- 1.11 The equity or extensive coverage approach ensures that all traders regardless of their size, activity or location have a similar probability of being audited or subjected to VAT enforcement procedures where necessary. This approach organises VAT tasks for the systematic pursuit of all VAT debts, which should deter taxable persons from future non-compliance
- 1 12 The efficiency approach is based on the proposition that revenue maximisation is best served by allocating available resources to detect and correct the liability of groups of traders for which the expected increase in tax liability is highest. This is organised on the basis of a risk analysis of traders. It is also felt by Revenue that the projection of an image of efficiency helps to deter avoidance and induce voluntary compliance
- 1 13 Due to limitations on the resources available for VAT compliance in the context of an increasing population of taxable persons, there has been a general move towards the efficiency approach to VAT compliance in the EU. In Ireland this was reflected by many of the changes envisaged in the first Revenue Corporate Plan covering the years 1994 to 1996 and in the latest Corporate Plan covering the years 1997 to 1999

Purpose and Scope of the Examination

- 1 14 A full value for money examination of VAT collection and control would be concerned with both the economy and efficiency of the application of established procedures and with the systems in place to measure the overall effectiveness of those procedures. An examination of the economy of the inputs applied to VAT collection and control was not possible at this time because the relevant data about the costs and time spent solely on these activities was not available.¹

¹ *Revenue estimates that the cost of VAT administration is around 1% of the revenue collected.*

- 1.15 Accordingly, this report examines aspects of the efficiency of the established procedures which are applied in the major phases of VAT collection and control. In particular, the examination was concerned with
- the adequacy of the systems and procedures for ensuring that liable persons are registered for VAT
 - the extent to which compliance is maximised under the self-assessment system
 - the quality of audit planning and the outturn of the programme of audits
 - the effectiveness of the enforcement procedures used to clear outstanding VAT debts
- 1.16 The report is also concerned with highlighting opportunities for Revenue to further refine the systems and improve the quality of information available to measure the effectiveness of VAT collection and control procedures. Procedures governing the repayment of VAT were not reviewed as part of the examination.

Examination Methodology

- 1.17 The examination was carried out by staff of the Office of the Comptroller and Auditor General. The fieldwork consisted of interviews with officials and a review of the systems and procedures relating to VAT registration, assessment and collection, audit, and the enforcement of debt. Performance trends in each of these areas were reviewed. The Collector-General's Office in Limerick and six district tax offices² were visited to confirm the operation of procedures at first hand and to review individual files selected on a sample basis. In addition, the Chief Inspector's Office and the Taxes Central Registration Office, located in Dublin, were also visited during the examination.

² *Cork, Tralee, Limerick, Castlebar, Athlone and Dundalk*

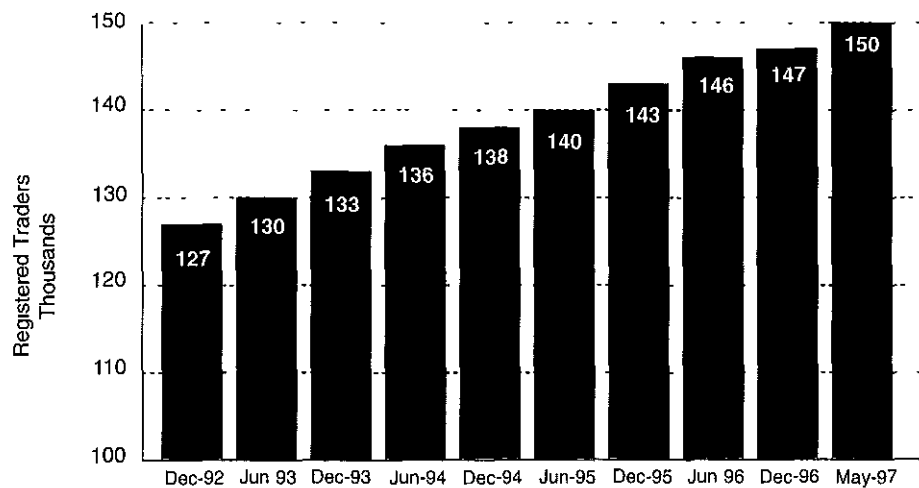
2 Registration Practices

- 2.1 Procedures for the registration of traders, liable for VAT, on a timely basis make an important contribution to the overall VAT compliance objectives of revenue maximisation through voluntary compliance and the deterrence of avoidance and evasion. Apart from ensuring that liable traders are brought into the tax net as soon as possible, the administrative procedures at registration must also facilitate an initial risk rating of the trader and the gathering of relevant information about his activities. This information becomes important in later phases of the VAT compliance cycle.
- 2.2 The following four activities during the registration phase were examined to determine their contribution to the overall effectiveness of VAT collection and control procedures:
- registration of the trader within a reasonable period of time
 - detection of unregistered traders
 - risk rating of traders to identify potential collection risks
 - new business education visits

Registration of Traders Within a Reasonable Period of Time

- 2.3 Traders who satisfy the VAT registration criteria normally register for VAT at the nearest district tax office to their proposed trading location. Within Dublin districts, registration applications are processed by the Taxes Central Registration Office. Following registration, the trader is sent a VAT3 form at the appropriate intervals.

Figure 2.1 VAT registered traders 1993-1997



Source: Office of the Revenue Commissioners

- 2.4 The number of registered traders has increased by over 18% from 126,754 in December 1992 to 149,857 in May 1997. The average number of registrations across all tax districts was 350 per month during 1995 and 1996
- 2.5 All applications are required to be checked and processed within 10 days of receipt. It was noted that some district tax offices visited did not record the timeliness of registration in relation to the set target and, accordingly, Revenue are not in a position to monitor the general achievement of this target

Detection of Unregistered Traders

- 2.6 Administrative effort at the registration phase includes the commitment of resources to detect unregistered traders with a turnover in excess of the registration threshold. In an ideal situation, the level of resources to be committed to this activity would be determined on the basis of the known level of such traders
- 2.7 However, in common with other areas of the black economy, the precise number of unregistered traders is unknown and since a major objective of those unregistered traders who exceed the registration threshold is to avoid detection, efforts to measure the number of unregistered traders or the value of VAT lost can only be achieved by indirect means³. The results of exercises in recent years to estimate the size of the black economy vary widely⁴. This suggests that any attempt to derive the true level of VAT non-compliance from such findings would probably not be successful
- 2.8 The estimation of the number of unregistered VAT traders is a problem common to other EU States. Two approaches have been used to estimate the level of unregistered activity. One approach, used by three member states, uses macro-economic data on the performance of the economy to estimate the overall level of business activity and compares this against the level of fiscal receipts.
- 2.9 An alternative approach, adopted in the United Kingdom, is to estimate the unregistered population from statistics of detected evasion from the results of audits or other detection activity. The use of this approach would be affected by the method of selecting traders for audit. This is discussed in more detail in Chapter 4 of this report. Where a targeted selection method is used, the method of estimation is likely to be biased towards overstating the extent of unregistered traders

³ *According to Revenue, the majority of registered traders will only conduct business with other registered traders in order to obtain the benefit of offsetting VAT on purchases. This operates as a control over the extent of unregistered liable traders.*

⁴ *A discussion of the methods used to measure the size of the black economy in Ireland can be found in Gabriel P. Fagan, The Black Economy in Ireland, Irish Banking Review, July 1997*

- 2.10 In the absence of a methodology for estimating the size of the population of unregistered traders, the difficulty of determining the appropriate level of resources which should be committed to detection will continue
- 2.11 Activity for the detection of unregistered taxpayers is co-ordinated across all taxheads. The rate of detection is largely dependent on the quality and quantity of information flowing into district tax offices on previously unknown economic activity in the area. Revenue manages detection activity for all tax heads by allocating an annual target for the discovery of unregistered taxpayers. The targets are set by district managers as part of an annual planning exercise
- 2.12 The national targets for detecting unregistered taxpayers were set at 2,100 taxpayers for 1995 and 1,800 taxpayers for 1996 and the actual detection level achieved was 1,755 tax payers in 1995 and 1,353 in 1996. The 1997 target is to detect 1,605 unregistered taxpayers
- 2.13 As more experience is gained in this work and more statistics become available, it should be possible to set more meaningful targets. This should improve the accuracy with which estimates of the unregistered trader population can be made

Methods to Detect Unregistered Traders

- 2.14 District tax offices rely on a variety of informal sources of information to assist them in ensuring that all taxable activity is brought to their attention. These sources include information from the public, observation by inspectors of new activity in the district and informal contact between districts

Improving the Effectiveness of Internal Information

- 2.15 Revenue officials engaged in audits and inspections who suspect evasion by traders, or who require further evidence as to the validity of transactions in the books of a trader, complete a form VAT63 which records details of suspicious transactions. This form is sent to the district tax office where the trader in question should be registered. The receiving office should verify the transactions by means of an inspection visit or audit. A VAT63 form may also be generated for internal use in a district tax office, for example, in the case of a notification to a VAT auditor following an enquiry during a comprehensive audit
- 2.16 VAT63 forms are a useful source of information about potentially incorrect or irregular transactions and for the detection of unregistered traders. However, the examination found that there was inconsistent use made of this source of information in the districts visited. Some districts deal with VAT63 forms immediately on receipt while others schedule them into ongoing work. A review of procedures for acting on

information received on VAT63 forms would be useful in assisting the timely detection of unregistered traders or evasion.

Use of Companies Registration Office Data

- 2 17 The Companies Registration Office (CRO) regularly sends a computer file containing information on newly registered companies to Revenue. On the basis of this information, the Taxes Central Registration Office writes to each company on the file to advise them of their general obligations regarding registration for tax, including VAT.
- 2 18 The matching of the CRO data with Revenue's own records could provide a useful source of information in detecting unregistered trading activity. Revenue has stated that due to the high level of inactive or dormant companies on the CRO data, this matching procedure would be of little benefit. Revenue should consult with the CRO to identify how this information might be refined to be of assistance in detecting liable unregistered companies.

Risk Rating of Traders at Registration

- 2 19 At registration, each trader is assigned a low, medium or high risk rating by the district tax office based on the information available relating to the case, the trader's business sector and the expected future VAT liability. The risk rating at registration is used for the planning of audit and inspection work. It is not used by the Collector-General's Office to plan collection and enforcement action. A separate analysis based on the actual VAT liability at risk is used for this purpose.
- 2 20 The examination noted two specific areas where the risk assessment system might be used more effectively.
- Unregistered traders who are detected and compelled to register could present a higher than average risk of subsequent default and should be rated accordingly regardless of the amount at risk. At present, Revenue does not separately identify these cases in any special manner in the risk rating system. Such cases should be closely monitored for at least one year after registration. Revenue currently takes the view that such traders represent a small revenue risk and that intensive monitoring may not be cost-effective.
 - High risk traders should be monitored closely, particularly in the first year of trading, to ensure that compliance is maintained at a high level. More active use of the risk rating system, combined with an automated reporting system to the Collector-General's Office where non-compliance occurs, should increase the overall effectiveness of follow up procedures.

- 2 21 The risk rating system should be subject to continuous review Revenue has stated that the current risk rating system has not yet been fully developed and that only the initial manual rating at registration is in place. It is proposed that the subsequent updating of the risk rating will be a programmed procedure in the further development of Revenue's computer systems.

New Business Education Visits

- 2 22 The allocation of a reliable risk rating for newly registered traders depends to a large extent on the quality of information about the business affairs of the trader that is available to the district tax offices This information is also important in the operation of an efficiency driven targeting approach for the scheduling of VAT audits and for the pursuit of non-compliant traders. Moreover, the provision of information to newly registered traders, often in the process of setting up a new business, to advise them of their administrative responsibilities for maintaining records for VAT purposes and to explain their legal obligations to comply with the VAT regulations, makes an important contribution to improving subsequent compliance rates.
- 2.23 Since 1995, Revenue has a policy of arranging for an early 'business education visit' to newly registered traders. The purpose of the visit is to provide information to traders about VAT regulations and their obligations. The visit is also a useful means of gathering information from traders about their business affairs. Based on feedback from district tax offices the consensus within Revenue is that, if visits are to be of use to traders, they should take place approximately 6 months after registration
- 2 24 As the information required by district tax offices is important for the scheduling of subsequent administration work, the programme of new business education visits is a significant administrative activity in the registration phase Although there are several inexpensive ways of providing information to the trader (provision of leaflets and videos) and indirect methods of obtaining the information needed for the risk rating system (correspondence or third party enquiry), the practice of making a personal visit to the trader is a highly effective means of imparting information to the trader and gathering valuable information for risk rating purposes.
- 2.25 Since 1995 Revenue has set annual targets for district tax offices to carry out business education visits to newly registered traders. Table 2 1 sets out the targets and numbers of visits made in 1995 and 1996 by the district tax offices examined.

Table 2.1 New business education visits made by selected district tax offices

District	1995		1996	
	Target	Achieved	Target	Achieved
Dublin ^a	-	-	1,910	2,066
Cork	1,000	1,220	1,100	761
Tralee	231	171	260	140
Limerick	370	334	500	356
Castlebar	-	-	24 ^b	31
Athlone	300	163	200	197
Dundalk	272	30	270	53

Note a Although a target of 1,610 visits was set for Dublin districts in 1995, new business education visits did not commence in Dublin until 1996 when the aggregate target for 1995 and 1996 was met

b The target of 24 visits was originally set in 1995

Source Office of the Revenue Commissioners

- 2 26 Table 2.1 indicates that while some districts were close to target, the performance in other district tax offices fell far short of the targets set. This suggests that some offices do not give sufficient priority to visiting newly registered traders. In view of the importance of these visits Revenue should set clearer guidelines on the necessity for these visits and should continuously monitor the performance of district tax offices to ensure that targets are being met

Contribution of Registration Practices to Effectiveness

- 2 27 The overall effectiveness of VAT collection and control procedures is determined by the extent to which the twin objectives of revenue maximisation and the deterrence of evasion are met. The risk rating of traders at registration is an important step in applying an efficiency based approach to audit and inspection activity. A key input to the risk rating system should be the quality of information received from the new business education visits. Accordingly, the performance of these activities at registration would have a direct influence on the effectiveness of later audit and enforcement procedures
- 2 28 While the present registration practices are appropriate for achieving a high degree of effectiveness, there are further refinements which could be made, principally in the co-ordination of work between Revenue and the district tax offices and in the monitoring of activities performed and the achievement of targets set at district tax office level.

- 2 29 There is scope for further development and subsequent use of the risk rating system and the timeliness and effectiveness of new business education visits. Estimation of the extent of the unregistered trader population, who are above the registration threshold, would help in establishing the level of resources which should be applied to the effort of detecting unregistered traders.

3 Self Assessment and Collection

3.1 The systems and procedures which contribute to the effectiveness of a self assessment system include steps for the efficient processing of returns and payments and the execution of an effective audit programme. VAT audits are considered in Chapter 4 of this report. The assessment and collection practices which contribute to the effectiveness of the VAT system are examined in this chapter under the following headings

- VAT3 returns compliance
- Section 22 estimates
- Section 23 assessments
- compliance levels by large liability traders
- special incentive schemes

3.2 In paragraph 10 of my 1996 annual report on the Appropriation Accounts, the total VAT outstanding as at 31 May 1997 was reported as £331 million of which Revenue estimated that £83 million was likely to be collected

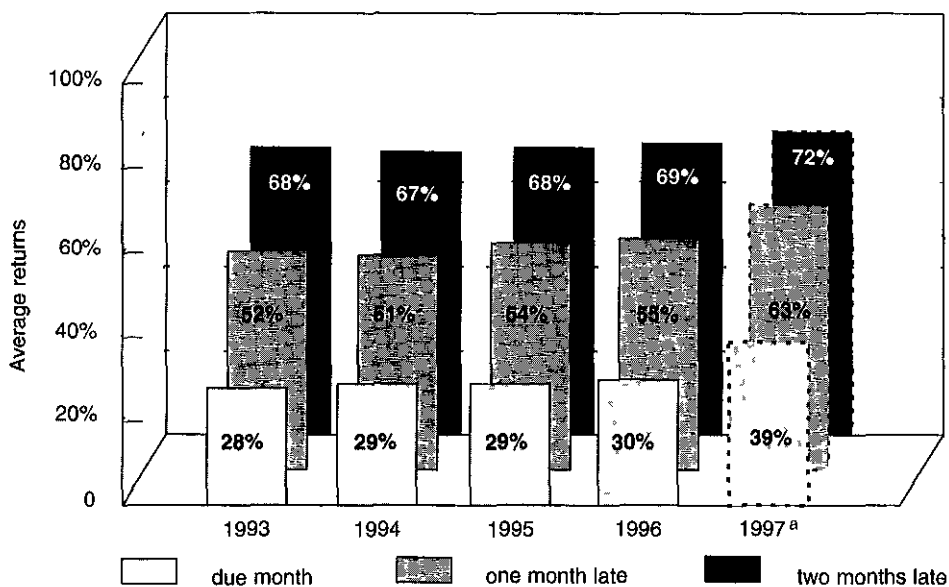
VAT3 Returns Compliance

3.3 A VAT3 form returned by a trader declares a VAT liability which is payable on the 19th day of the month following the end of the VAT period and establishes a legally enforceable debt against him. The trader is regarded as being compliant by the Collector-General's Office if the return and the amount payable are received in the payable month. The level of compliance on the basis of VAT3 forms returned is a key indicator used by the Collector-General's Office to assess the overall effectiveness of VAT compliance

3.4 Figure 3.1 shows the average percentage of VAT3 forms which had been returned to the Collector-General's Office in the due month, one month late and two months late, in the years 1993 to 1996 and in respect of the first four bi-monthly periods of 1997. Figure 3.2 shows the timeliness of VAT collected during the same period

3.5 In Figures 3.1 and 3.2 the data in respect of the 1997 period is not directly comparable with the data from earlier years. The basis of measuring compliance was improved in 1997 to take account of traders paying by direct debit. More sophisticated analysis techniques in the Collector-General's Office also allowed returns and payments lodged on the last day of the month to be taken into account in that month rather than in the following month as had been the case in the periods prior to 1997

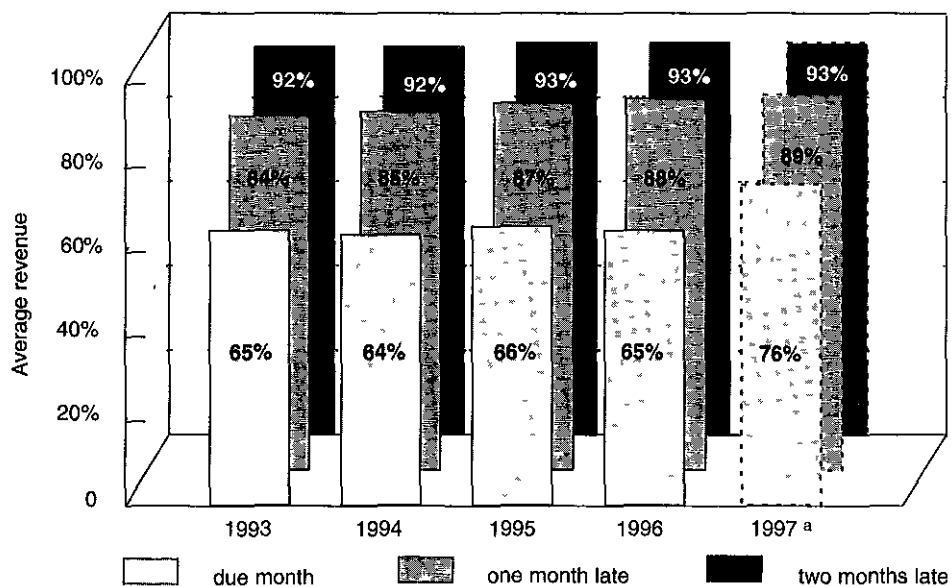
Figure 3.1 Timeliness of submission of VAT3 returns, 1993-1997



Note ^a The figures for 1997 are in respect of the first four VAT periods only and are not directly comparable with the figures for the years 1993 to 1996 (See Paragraph 3 5)

Source Office of the Revenue Commissioners

Figure 3 2 Timeliness of collection of VAT revenue, 1993-1997



Note ^a The figures for 1997 are in respect of the first four VAT periods only and are not directly comparable with the figures for the years 1993 to 1996 (See Paragraph 3 5)

Source Office of the Revenue Commissioners

- 3.6 As shown in Figures 3.1 and 3.2, the trend in the submission of VAT3 returns and in the collection of revenue has been consistent over the four years from 1993 to 1996. Revenue has stated that overall compliance rates for the receipt of VAT3 forms eventually exceed 90%.
- 3.7 On the basis of the analysis set out in Figures 3.1 and 3.2, there is clearly room for improvement in the basic compliance rate, particularly in respect of small traders. It would appear that such traders, in general, take prolonged credit by ignoring initial demands for payment and only pay at the later stages of the collection process. It is recognised that procedures for improving compliance levels among lower yielding cases must take into account resource limitations and the costs involved.

Section 22 Estimates

- 3.8 Section 22 of the Value Added Tax Act, 1972 provides that when a trader fails to submit a VAT3 form and to pay the tax due within the prescribed period, the Collector-General's Office may issue an estimate of the amount due which then becomes a legally enforceable debt. If a VAT3 form is subsequently returned to the Collector-General's Office, it displaces the amount calculated on the Section 22 estimate.

Section 22 Estimates Issued in the Period 1994 to 1996

- 3.9 In 1995, Revenue decided that the method of calculating Section 22 estimates should be changed from basing the estimate on the taxpayer's highest liability in the previous two years to an averaging system covering the same period, as this would provide a more accurate reflection of the trader's potential liability.
- 3.10 It was also decided to limit the number of consecutive estimates issued to three, after which the case would be signalled for compliance attention on the basis that there was little point in continuing to issue Section 22 estimates if a trader was failing to respond. This revised approach, a component of the Active Intervention Management (AIM) system, should ensure that administrative savings are made in reduced paperwork and associated processing costs while focusing on persistent non-compliers which make up the bulk of VAT arrears (see Appendix A). In general, Revenue believes that this should result in more efficient and effective collection procedures.
- 3.11 The new approach has resulted in a reduction in the number of Section 22 estimates issued in recent years. Table 3.1 sets out the number of Section 22 estimates issued compared to the number of VAT3 forms issued between 1994 and 1997.

Table 3.1 VAT3 returns and Section 22 estimates issued: 1994-1997

Year	VAT3 forms	Section 22 estimates	Section 22 estimates as a % of VAT3 forms
1994	564,461	258,489	45
1995	576,578	182,835	31
1996	624,850	206,312	33
1997 (10 Months)	564,367	141,596	25

Source Office of the Revenue Commissioners

Section 22 Estimates in Arrears

- 3 12 Traders who do not submit VAT3 forms, or who fail to settle their VAT liabilities in response to the receipt of a Section 22 estimate, advance to further stages of the collection and enforcement process. Table 3.2 sets out the arrears position as at April 1997 arising from the issue of Section 22 estimates up to the end of 1996.

Table 3.2 Analysis of Section 22 estimates in arrears

Year	Under review ^a	At Pre-enforcement stage ^b	At enforcement stage ^c	Total
	£m	£m	£m	£m
1972 to 1993	19	27	16	62
1994	11	20	3	34
1995	5	6	3	14
1996	3	18	15	36
Total	38	71	37	146

Notes a Normal collection and enforcement procedures have temporarily stopped while the case is under investigation

b Cases which are currently at demand or reminder stage. Older cases may have been returned to the Collector-General's Office following unsuccessful enforcement action

c Cases which have been referred to the sheriff or solicitor for further action

Source Office of the Revenue Commissioners

3.13 Revenue's own estimate of amounts likely to be collected is approximately 25% of the total VAT outstanding in respect of declared liabilities and estimates combined. However, as at 31 May 1997, the likely collection rate for Section 22 estimates was 15%⁵. On this basis, only £22 million of the total £146 million in Table 3.2 is considered likely to be collected.

Section 23 Assessments

3.14 An Inspector of Taxes may independently raise an assessment of a trader's liability following an audit or inspection of the trader's records. This assessment, known as a Section 23 assessment, can augment or reduce the previously declared VAT liability or replace a Section 22 estimate. Table 3.3 sets out the current position in relation to outstanding Section 23 assessments.

Table 3.3 Analysis of Section 23 assessments in arrears

Year	Under review ^a	At Pre-enforcement stage ^b	At enforcement stage ^c	Total
	£m	£m	£m	£m
1972 - 1993	32	40	33	105
1994	3	1	2	6
1995	2	2	1	5
1996	1	1	0	2
Total	38	44	36	118

Notes a Normal collection and enforcement procedures have temporarily stopped while the case is under investigation

b Cases which are currently at demand or reminder stage. Older cases may have been returned to the Collector-General's Office following unsuccessful enforcement action

c Cases which have been referred to the sheriff or solicitor for further action

Source Office of the Revenue Commissioners

3.15 Most of the debt for which collection is under review relates to traders who are in a liquidation process or in instalment arrangements with the Collector-General's Office.

⁵ The estimate of amounts likely to be collected is calculated by reference to current trends in the collection of tax arrears. These trends take account of the age profile of the various components in the debt and potential future bad debts.

Estimates and Assessments Issued in the Period 1972 to 1993

- 3 16 Revenue acknowledges that, in the past, the tendency was to over-estimate the value of Section 22 estimates and Section 23 assessments. This approach has resulted in a notional uncollectible debt which has built up on Revenue's files for that period
- 3.17 In 1989, Revenue established an Arrears Verification Unit (AVU) in each district tax office to assist in determining the true liability of all tax estimates, including those relating to VAT. The AVUs are responsible for reducing the amount of arrears by discharging the estimates or assessments, collecting amounts due or referring arrears for enforcement action or to the Collector-General's Office for write-off as irrecoverable
- 3 18 The contribution of the AVUs is significant when measured in terms of the cash yield compared to the amount of arrears removed from the records. Table 3.4 sets out this contribution in respect of the district tax offices visited during this examination

**Table 3.4 Performance of Arrears Verification Units in 1995 and 1996
All tax heads for selected district tax offices**

Year	Arrears reduced £m	Cash yield £m	Cash yield as a % of arrears reduced
1995	90.0	7.1	8%
1996	15.0	3.2	21%

Source: Office of the Revenue Commissioners

- 3.19 The total tax collected by AVUs in respect of all district tax offices was almost £23 million in 1995 and £18 million in 1996

Compliance by Large Liability Traders

- 3.20 Certain categories of traders are subject to special monitoring procedures under the AIM system to ensure that their VAT3 forms and the appropriate payment are received promptly. This approach was initially followed in relation to approximately 2,300 'big cases' who account for about 75% of the annual revenue yield from VAT. A 'big case' refers to a trader whose potential VAT liability exceeds £50,000 for any one VAT period over the previous two year period.
- 3 21 Big cases are divided into seven categories denoted by the letters P to V. Table 3.5 sets out the number of cases in each category and their significance in terms of VAT yield

Table 3.5 Categories of big cases as at 30 April 1997^a

Case size code	Number of cases	Percentage of VAT yield	Average bi-monthly yield per case
P	760	5%	£33,000
Q	380	3%	£47,000
R	720	11%	£85,000
S	220	8%	£197,000
T	70	5%	£333,000
U	30	3%	£512,000
V	110	40%	£2,100,000
Total big cases	2,290	75%	£178,000
Total all cases	150,000	100%	£4,000

Note a Taking averages of 1995 and 1996 yields from big cases

Source Office of the Revenue Commissioners

3.22 The special monitoring procedures have now been extended to medium size cases where the potential liability is greater than £15,000 in any one VAT period. This involves the systematic monitoring of a further 7,500 cases which account for about 15% of the annual VAT revenue yield. It is intended to further extend this approach as resources permit.

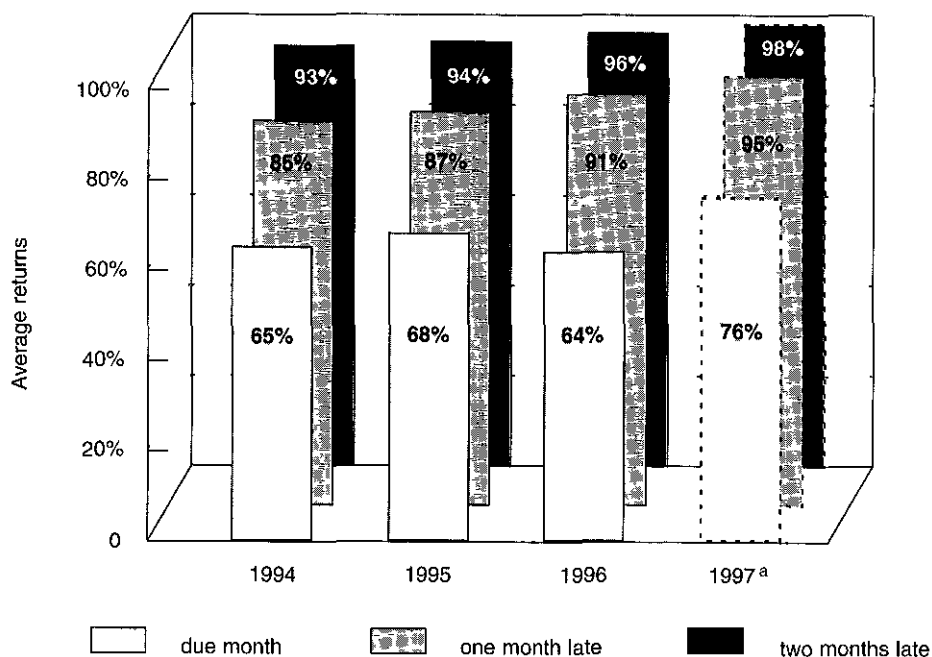
3.23 Apart from systematically monitoring the cases with significant current liabilities, all cases, irrespective of case size, with arrears of over £25,000 are examined on a monthly basis to ensure that appropriate action is being taken in each case.

Compliance by Big Cases

3.24 A report is produced on big cases which have not submitted a VAT3 form by the due date. This report is provided to the Big Cases Section in the Collector-General's Office for immediate follow-up by way of telephone contact with the traders concerned. The Collector-General's Office also employs a range of measures including the charging of interest on late payment and referral to an enforcement agency to deter further non-compliance.

3.25 Figure 3.3 sets out the average percentage of VAT3 forms returned in the due month, one month late and two months late in respect of big cases for the years 1994 to 1996 and in respect of the first four bi-monthly periods of 1997. As previously noted in paragraph 3.5, the data for 1997 is not directly comparable with earlier years due to changes in the basis of presentation.

Figure 3 3 Timeliness of submissions of VAT3 returns by Big Cases 1994-1997



Note ^a The figures for 1997 are in respect of the first four VAT periods only and are not directly comparable with the figures for the years 1994 to 1996 (See Paragraph 3 5)

Source Office of the Revenue Commissioners

- 3 26 As shown in Figure 3 3, the timeliness of the submission of VAT3 forms by big cases is significantly better than the overall rate for all traders. The special monitoring procedures used in respect of these large liability traders help to ensure better overall compliance rates. An examination of returns for the six bi-monthly periods in 1995 shows that overall compliance rates for big cases eventually reach 99.8%.

Special Incentive Schemes

Annual Accounting Scheme

- 3 27 A special VAT annual accounting scheme was introduced under Section 58 of the Finance Act, 1989 to allow certain VAT registered traders to make single annual VAT returns for each year ending 31 August instead of the standard bi-monthly returns. The purpose of the scheme is to reduce the administrative burden on small traders and to improve compliance rates. The scheme is applied to traders whose net VAT payments are less than £5,000 per annum. Traders may opt out of the scheme and continue to make bi-monthly returns.

3 28 Table 3.6 sets out the number of traders participating in the annual accounting scheme since 1992, the amount of yield, and the level of compliance as at September 1997. The number of traders participating in the scheme has fallen in recent years mainly because Revenue now encourages small traders to join a direct debit scheme (see paragraph 3.33). Existing traders who default in the annual accounting scheme are also generally obliged to set up a direct debit arrangement.

Table 3.6 Participation in the annual accounting scheme 1992-1996

Year	Number	Yield £m	Level of compliance ^a
1992	32,112	18	83%
1993	35,296	13	82%
1994	36,792	22	78%
1995	30,698	29	70%
1996	25,703	30	54%

Note a The table shows the level of compliance at September 1997 in respect of each year. The lower compliance rates in more recent years should improve over time as a result of continuing Revenue action against defaulters.

Source Office of the Revenue Commissioners

3 29 Section 22 estimates are not raised by the Collector-General's Office in the case of failure by traders operating under the annual accounting scheme to submit annual returns. Therefore, Revenue must resort to non-standard procedures to track defaulters and pursue the debt to enforcement. Having regard to the basis of the annual accounting scheme, Revenue may have to wait for 12 to 18 months from registration before a trader in the scheme can be identified as being in default.

3 30 Revenue considers that, in view of the small liabilities involved, normal enforcement procedures are inappropriate for annual accounting cases. In a campaign in 1996 to follow-up on traders in the annual accounting scheme who were in default, 8,000 cases were targeted. After the elimination of cases which responded to initial warnings or had ceased trading or had a minimal VAT liability, the issuance of proceedings was considered appropriate in only seven cases.

3 31 A similar system to the annual accounting scheme operates in the United Kingdom. However, the United Kingdom authorities make a formal assessment of the track record of the applicant and discourage or refuse unsuitable traders admission into the scheme where their record is not acceptable. The United Kingdom authorities also insist that small traders make interim payments by electronic funds transfer⁶.

⁶ Except where the previous annual VAT liability was less than £2,000 and turnover is below £100,000.

- 3 32 While the cost effectiveness of pursuit measures must be kept in mind, Revenue should consider carrying out a systematic examination of the operation and effectiveness of the current annual accounting scheme to establish the most appropriate methods for improving compliance levels, including the promotion of the direct debit scheme for traders still in the annual accounting scheme

Direct Debit Scheme

- 3 33 The direct debit scheme, introduced in October 1992, is available to all taxpayers to enable them to make monthly payments to Revenue as part payment of their eventual tax liability in respect of any or all tax heads. The amount of the monthly payment is calculated on the basis of the taxpayer's previous year's trading results. The taxpayer is required to submit an annual return and a net payment or refund is made as appropriate.
- 3 34 The direct debit scheme improves the timeliness of the collection of VAT and also enables collection problems to be identified at an earlier stage than the annual accounting scheme. It also contributes to the efficiency of VAT collection through the reduction in paperwork associated with the processing of VAT3 forms
- 3.35 The number of direct debit arrangements has grown in recent years. Table 3.7 sets out the number of direct debit arrangements in operation between 1992 and 1996 and the amount of resulting VAT yield. The Table shows that, in 1996, almost 10% of the net VAT yield was collected through direct debit arrangements.

Table 3.7 VAT yield from direct debit arrangements: 1992-1996

At year end	Number of traders	Yield £m
1992	1,478	5.9
1993	2,017	50.9
1994	6,100	123.5
1995	8,125	201.5
1996	10,251	297.0

Source: Office of the Revenue Commissioners

- 3.36 There are currently 2,234 traders in the direct debit scheme who have also entered into an instalment arrangement with the Collector-General's Office for payment of arrears arising from default.

Contribution of Collection Procedures to Effectiveness

- 3 37 Collection procedures for VAT can be regarded as being efficient with an overall compliance level of 90% achieved generally for all traders and almost 100% in the case of large liability traders. However, it would appear that many small traders take prolonged credit by ignoring initial demands for payment and only pay at the later stages of the collection process. While the targeted approach currently adopted provides for more effective collection, Revenue should continue to systematically review these procedures. Revenue should also review the operation of the annual accounting scheme for small traders in order to improve compliance rates.

4 Value Added Tax Audits

Programme of VAT Audits

- 4.1 The objectives of a VAT audit are the same as the general objectives of other VAT administrative activity, i.e. to maximise VAT revenue and to deter evasion. The audit also serves to provide assurance as to the level of voluntary compliance. The revenue maximisation objective is achieved through an audit programme which is determined by the efficiency approach of targeting groups at risk. The assurance objective is achieved by the performance of randomly selected audits.

Requirement for Random Audits in a Self Assessment System

- 4.2 Under a self assessment system, a programme of audits should be undertaken by Revenue to establish the accuracy of returns. While resources are principally directed towards undertaking audits where VAT3 forms give grounds for suspecting significant evasion (i.e. an efficiency based selection approach), an element of random selection, where every taxpayer has the possibility of being selected for audit, is also essential to measure the level of compliance.
- 4.3 Although an efficiency driven approach to audit selection appears to result in a better use of resources, in a self assessment system randomly selected audits are needed to provide confidence that the system is operating as intended and that the overall VAT compliance procedures are fair to all traders. The public perception of fairness in the tax system encourages compliance.
- 4.4 The inclusion of randomly selected audit targets is considered important by industry groups⁷ for maintaining public confidence in the equity of tax administration. The Irish Business and Employers Confederation (IBEC) has expressed the view that Revenue tends to select larger compliant companies for audit rather than seeking out the black economy non-taxpaying enterprises. IBEC also suggested that a higher proportion of VAT audits should be selected on a purely random basis.
- 4.5 While respondents to a questionnaire produced by the Institute of Taxation in Ireland were generally very positive about the audit process, it was noted that 56% of respondents regarded the Inspector of Taxes' focus as solely on obtaining additional VAT. The Irish Small and Medium Enterprises Association (ISME) and IBEC have also expressed reservations with regard to the conduct of VAT audits. According to ISME, there appeared to be an expectation by the VAT Inspector that additional money would be collected as a result of the audit. ISME believes that audit success

⁷ The views of the Institute of Taxation, IBEC and ISME on the administration of VAT were obtained during the course of the examination and are set out in more detail in Appendix B

should also be based to some extent on nil results, i.e. assurance that the correct VAT revenue was received

- 4.6 At present, random audits are not carried out on single tax heads such as VAT. However, as part of its programme of comprehensive audits each year, Revenue carries out a small number of random audits. For example, in 1996, only 52 of the 3,969 comprehensive audits were selected at random.

Comprehensive Audits

- 4.7 The majority of tax audits carried out by Revenue are specific to single tax heads such as VAT but in recent years a significant number of comprehensive audits have also been carried out which focus on all taxes payable including VAT but which in practice tend to concentrate on income tax, corporation tax and capital gains tax. Table 4.1 sets out the overall yield and the VAT yield from comprehensive audits.

Table 4.1 Comprehensive audits and VAT yield

Year	Number of audits	Overall yield £m	VAT yield ^a £m
1993	2,537	20	2
1994	3,838	40	6
1995	4,058	53	10
1996	3,969	69	8

Note a Not all taxpayers subject to comprehensive audit are liable for VAT. In many comprehensive audits VAT would not be the major revenue at risk.

Source Office of the Revenue Commissioners

Selection of Traders for Single Tax Head VAT Audit

- 4.8 Single tax head VAT audits (VAT audits) are carried out in accordance with an annual audit programme which sets out policy issues for the guidance of the VAT auditors. The programme is approved by senior management in the Office of the Chief Inspector of Taxes, following submissions from the district tax offices.
- 4.9 A VAT audit consists of the following steps:
- analysis of information submitted on the VAT3 form and checking it against other information available about the trader's activities
 - selecting traders for audit
 - performing the audit, i.e. checking the VAT3 forms in more detail against trader specific indicators or general ratios

- 4 10 In order to plan for VAT audits, the computer branch of Revenue supplies each audit district with data on traders which districts use as part of the process of identifying a pool of potential audit cases. No formal risk analysis techniques or software applications are available to districts to aid the selection process.
- 4 11 An increasing proportion of cases are selected on the basis of intelligence which ranges from the auditor's observations to information from a trader's records which suggests irregularities in other traders' affairs. In this respect, information obtained from new business education visits may also be of assistance in the selection process.
- 4 12 The effectiveness of selection is further helped by dividing the trader population into sectors. The annual audit plan sets out the economic sectors on which district tax offices should focus. However, each office has autonomy in choosing the specific cases for audit. The sectoral approach has been useful for Revenue in the following two areas
- identification of sectors considered to be high risk based on previous audit results
 - identification of significant cases or previously yielding cases, such as
 - cases of high levels of chargeable and deductible VAT
 - cases previously audited resulting in a VAT undercharge
- 4 13 Apart from the specific planning of VAT audits, the single tax head VAT audit programme fits in as part of the overall tax audit programmes. All audit programmes are inter-related and interactive. The more intensive, in-depth approach to audit (taking in all tax head implications) involves spending more time on each individual case so as to identify all likely tax risks. In practice, if as a result of single tax head audits, matters come to notice which give rise to liability under other tax heads, this additional liability is also pursued. The identification of cases suitable for VAT audits using this comprehensive process is considered by Revenue to be an improvement on earlier methodologies.

VAT Audit Activity

- 4 14 Table 4.2 sets out the number of VAT audits carried out in the period 1993 to 1996, the yield from those audits and the average yield per audit.

Table 4.2 VAT audits and yield - 1993-1996

Year	Target number of audits	Audits performed	Target yield £m	Achieved yield ^a £m	Average yield per audit
1993	*	13,158	*	31	£2,356
1994	*	13,632	*	32	£2,347
1995	11,000	10,351	32	37	£3,574
1996	9,500	8,424	38	33	£3,917

Note a Up to 1995, the achieved yield figure was the inspector's assessment of trader liability, regardless of whether that amount was eventually paid to Revenue. From 1996, the achieved yield is cash actually received.

* No targets were set in 1993 and 1994.

Source Office of the Revenue Commissioners

- 4 15 In paragraph 13 of my 1996 annual report on the Appropriation Accounts, I refer to the fall in the number of single tax head audits completed by Revenue in 1996 from 1995 and to the fall in the overall tax yield from audits. The Accounting Officer informed me that the reduction in the number of audits in 1996 reflects a more in-depth approach to audits and the switching of some resources from single tax head audits such as VAT audits to comprehensive audits. Better screening methods have resulted in more efficient targeting of cases with the result that there is a higher yield per case as against the yield in 1995.
- 4 16 Prior to 1994 the single tax head audit programmes were primarily based on the extensive coverage approach, i.e. visiting all taxpayers over a given period of time. This meant that all taxpayers received a visit periodically. However, Revenue did not regard this as an efficient use of resources since each taxpayer, regardless of size, received the same level of scrutiny.
- 4 17 Since 1994, the single tax head audit programmes have focused on the more efficient approach of pursuing tax which is most at risk and extending the duration of the audit from a half-day visit to one or more days. This has reduced the number of single tax head audits and means that some small taxpayers, for example, those in the annual accounting scheme, may not be subject to audit.
- 4 18 As part of the annual management of the VAT audit programme, district managers set targets for the number of audits to be carried out and the expected monetary yield. Table 4 3 sets out the performance of the districts examined against these targets in 1996.

Table 4.3 VAT audit performance for selected tax districts 1996

District	Target audits	Performed audits	Target yield £m	Achieved yield £m
Dublin	6,190	4,476	21.5	18.8
Cork	1,000	653	4.2	2.7
Tralee	320	255	0.9	1.1
Limerick	750	661	2.8	3.1
Castlebar	300	295	0.6	0.6
Athlone	280	186	1.0	1.0
Dundalk	325	333	1.0	0.8

Source: Office of the Revenue Commissioners

- 4.19 The average direct staff cost per VAT audit in 1996 has been estimated at £500. The margin between current audit costs and audit yield suggests that VAT audit activity is good value for money and on this basis it is likely that additional VAT audits would produce additional yield. However, an extension of the programme of audits should be based on strategic review and risk analysis.
- 4.20 Revenue's accounting systems are not designed to record the full cost of audits. This information is necessary to properly monitor the continuing cost effectiveness of the audit programme and to plan audits on a more efficient basis. Revenue should take steps to develop a system of cost/benefit analysis which would ensure that continuing value for money is obtained from an increased level of audit activity.

Nil Yield Audits as a Performance Measure

- 4.21 According to Revenue, the elimination of half day VAT audits combined with the application of more sophisticated audit selection criteria have increased the overall percentage of yielding audits from approximately 40% in 1995 to approximately 55% in 1996.
- 4.22 In order to consider the incidence of nil yield audits, 134 VAT audits which took place in 1995 were reviewed. It was found that 61 of the audits had produced a nil yield. This is consistent with Revenue's own statistics.
- 4.23 While some level of nil yielding audits is always likely to be encountered, the proportion of such audits could be used as a performance target for the measurement of the overall effectiveness of the programme of audits. Any deviation from the expected norm could signify that the audit case selection criteria require realignment or that the actual mix of audits between targeted audits and random audits should be adjusted.

Contribution of Audit to Effectiveness

- 4 24 The effectiveness of the audit programme and the yield per audit have been improved by the operation of a planning system which assists in identifying cases involving tax at risk and in increasing revenue yield. The 'ideal' audit programme should provide for a mix of random audits and targeted audits which adequately achieves the twin targets of revenue maximisation and compliance assurance. The current proportion of randomly selected audits included in the comprehensive audit programme is not sufficient to provide assurance regarding the level of compliance in a self assessment system.

5 Enforcement

- 5 1 This chapter of the report gives a limited overview of some of the main methods used by Revenue to pursue outstanding VAT liabilities. The principal methods are sheriff and solicitor enforcement action and the power of attachment. As enforcement procedures are not confined to particular tax heads, I propose to conduct a separate value for money examination in 1998 on the economy and efficiency of enforcement procedures and on the systems used to measure the effectiveness of these procedures.

Effectiveness of Enforcement Action

- 5 2 Revenue measures the effectiveness of sheriff and solicitor activity by the level of payment received either directly or indirectly as a result of the enforcement action. Indirect returns arise when defaulters remit payments to the Collector-General's Office following initial contact by either the sheriff or solicitor.

Sheriff Action

- 5 3 Sheriffs are collection agents with powers assigned by the Courts. A certificate⁸ covering specific tax arrears is sent to the sheriff where Revenue believes that the trader possesses business assets which may be seized and used to recover the debt. In some cases local collection agents visit the traders to attempt to collect the amounts outstanding prior to the commencement of sheriff action.
- 5 4 A crucial aspect of sheriff action is that the taxpayer will always find it more expensive to pay his tax liabilities through the sheriff than through payment to the Collector-General's Office. The costs and poundage of the sheriff action are borne by the defaulter and are not deducted from the payment made.
- 5 5 Table 5.1 shows that over the period 1993 to 1996 approximately 25% of the face value of the certificates for VAT issued to the sheriffs was satisfied.

⁸ *Certificates are issued to sheriffs under Section 485 of the Income Tax Act, 1967. More than one certificate may issue in respect of the same person for different taxes due, or for amounts of tax due for different periods.*

Enforcement

Table 5.1 Sheriff certificates issued and debts satisfied for VAT: 1993-1996

Year	Number of certificates issued ^a	Value £m	Number of debts satisfied ^a	Amounts received ^b £m
1993	78,389	444	39,029	95
1994	70,034	455	42,148	105
1995	30,135	322	25,897	83
1996	44,167	171	18,776	60

Note a Due to timing differences, the number and value of debts satisfied in any one year is not necessarily related to certificates issued in that year

b Includes an estimate of amounts received by the Collector-General's Office which Revenue deems to be attributable to enforcement action

Source Office of the Revenue Commissioners

5.6 In order to obtain an indication of the relative success of sheriff activity, in relation to VAT only, a random sample of 29 non-compliant traders was examined covering the period October 1994 to August 1996. Table 5.2 sets out the effectiveness of the various collection and enforcement actions taken in respect of these traders over the period

Table 5.2 Relative effectiveness of collection and enforcement action

Collection stage	Number issued	Number satisfied	Percentage
Section 22 estimates	95	52	55%
Collector-General reminders/demands	112	29	26%
Sheriff certificates	35	27	77%

Source Office of the Comptroller and Auditor General

Solicitor Action

5.7 The Revenue Solicitor deals with cases involving arrears of over £30,000. Two firms of solicitors are also retained by Revenue to pursue smaller cases which are deemed unsuitable for sheriff enforcement, for example, where the trader has few seizable assets. Interest is also charged on the liability outstanding. These firms are paid directly for their services.

5.8 Table 5.3 shows that over the period concerned approximately 30% of the value of VAT cases referred to solicitors was satisfied.

Table 5.3 Solicitor cases issued and satisfied for VAT: 1993-1996 ^a

Year	Number of cases issued	Value £m	Number of cases satisfied	Amounts received £m
1993	1,386	17	1,483	3
1994	1,250	14	1,270	4
1995	3,341	27	2,232	6
1996	555	2	2,144	5

Note a the number and value of cases satisfied in any one year is not necessarily related to cases issued in that year

Source Office of the Revenue Commissioners

Power of Attachment

- 5 9 The power to attach amounts owed by a third party to a taxpayer who has defaulted in the payment of certain taxes was given to Revenue in the 1988 Finance Act. The power of attachment is used in cases which may not lend themselves to sheriff or other forms of enforcement action. The attachment process is applied to a broad range of sectors and orders to secure payment have been issued to a wide variety of institutions including banks, building societies, co-operative societies and government departments. Since its introduction in 1989, the power of attachment has yielded £26.5 million in respect of all relevant tax heads, including £1.4 million in 1996.

Appendices

Appendix A

Active Intervention Management

The Active Intervention Management (AIM) system was fully implemented for VAT in mid-1996. It is used to facilitate the earlier identification of arrears and to manage the collection and enforcement of these arrears.

Prior to the implementation of AIM, the Collector-General's Office collected and pursued VAT largely by means of a process driven system whereby the computer was programmed to produce paper output in the form of estimates, reminders, demands and sheriff certificates at regular intervals and issue them directly to the trader, largely without intervention from the Collector-General's Office. This process brought non-compliant traders to the enforcement stage of collection relatively quickly, but did not take into account the complete tax liability of a trader nor the circumstances which might affect his ability to pay the debt.

AIM uses the Consolidated Taxpayer Project (Contax)¹ computer system to enable staff to focus on the rapid pursuit of large liabilities, the detection and pursuit of seriously non-compliant cases and the monitoring of delinquent business sectors. The main benefits of the AIM approach are expected to be

- a co-ordinated Revenue approach to compliance
- a consolidation of tax liabilities
- a case selection strategy based on the 'tax at risk' concept
- improved information about cases
- the reduction of costs

AIM relies heavily on a case worker approach to debt management. Computer files are periodically scanned to detect non-compliant cases and these are assigned to individuals for action. This action may take a variety of forms including

- visiting the trader, direct telephone contact or written communication
- authorising issue of demand notices, sheriff certificates and solicitor referral notices
- negotiating settlement of arrears
- obtaining trader authorisation for set-off of liabilities against tax credits elsewhere

¹ *The Contax project is the name given to a series of initiatives which have commenced or will be started by Revenue enabling an integrated approach to be taken of taxpayers' affairs. In brief, it will enable a view to be taken over all tax heads when dealing with taxpayers with a view to increasing administrative efficiency and organisational effectiveness. It also has the objective of improving customer service.*

The process driven system continues to operate but the critical difference from the point of view of the trader is that there is intervention from a specific individual who has authority to negotiate with the trader and to delay pursuit and enforcement of debt if there is a realistic probability of securing compliance through other means

Appendix B

Views of Business Representative Bodies

During the examination the views of the Institute of Taxation in Ireland, the Irish Business and Employers Confederation (IBEC) and the Irish Small and Medium Enterprises Association (ISME) were sought on the administration of the Value Added Tax (VAT) system. These views are summarised below.

Institute of Taxation in Ireland

In response to a request for their views on the administration of VAT, the Institute of Taxation carried out a survey of 350 members. The responses to the questionnaire from 100 members countrywide, who are mainly taxation consultants, are summarised below.

VAT Audit Process	59% of respondents were of the view that in conducting VAT audits Revenue understands the client's business and individual circumstances. However, 56% felt that the sole focus of the audit was to obtain additional VAT revenue.
Quality of Service	There was a large degree of satisfaction in the quality of service provided by Revenue. 80% of respondents felt that inspectors act with courtesy and in accordance with the VAT legislation and practice statements, with only 3% disagreeing. 83% believe that they get prompt answers to queries and 65% believe that Revenue acts in a business-like manner. While 80% of respondents felt that Revenue was of assistance in keeping members up-to-date on VAT developments, the remainder indicated that Revenue was of little or no help.
Cost	82% of respondents believe that their clients do not recover the cost of VAT collection through their pricing structure.
Simplification	56% of respondents thought that the scope and rates of VAT could be simplified in some way. Almost all members suggested that the legislation concerning VAT on property was too complex.

Irish Business and Employers Confederation (IBEC)

IBEC considered that, in general, the operation of the VAT system is efficient and that there are relatively few areas in which changes are needed. However, concerns were expressed in relation to the areas set out below

- It was felt that procedures in relation to registration and VAT3 returns do not need any change. However, the Intrastat return poses a considerable burden for business but it was noted that this was an EU Commission requirement which was at present under consideration in Brussels.
- The low level of self employed and small companies which avail of the direct debit scheme was unsatisfactory. Revenue should consider whether any incentives, such as those introduced by Telecom Eireann and the ESB, should be employed to improve the take up of this facility.
- Considerable concern was expressed about the basis for undertaking a VAT audit. There appeared to be excessive zeal on the part of some auditors to find errors by tax compliant companies which resulted in prolonged audits and disruption of the business of the companies concerned. Where audits were not completed within one or two weeks, the burden on businesses could be considerable. It was felt that Revenue, in reviewing its audit procedures, should take into account the impact the audit would have on the trader's business when planning the duration of a visit.
- A further concern of IBEC was that, in selecting companies for audit, there was a tendency to select large tax compliant companies rather than seeking black economy non-taxpaying enterprises. In addition, it was felt that a higher portion of VAT audits should be on a purely random selection basis and a greater effort should be made by Revenue to ensure that all potential taxpayers were included in the tax net.

Irish Small and Medium Enterprises Association (ISME)

The following were the views of ISME

- The cashflow of Small and Medium Enterprises (SMEs) suffers because VAT is paid to Revenue long before it is collected from customers. In effect companies are having to borrow money from the banks or take longer credit themselves to fund the VAT liabilities. Payment at the end of the month is more logical as business is geared towards month-end accounting. In addition, this would provide a better chance of recovering the VAT from customers before payment to Revenue. In general, the costs associated with VAT administration are not built into prices of goods and services.

- The direct debit system is useful in terms of balancing the cash flows for SMEs. However, there should be some regard for the current trading profile of the company rather than basing the direct debit payment on past performance. As some 60% of SMEs trade on a cash receipts basis, ISME would like to see VAT accountable on a cash receipts basis used more widely
- With regard to VAT audits, there appears to be an expectation by Revenue that money will be collected and this was evident in the attitude and the time spent in a company by Revenue officers. Audit success should be based to some extent on nil results which would provide assurance that the correct VAT revenue was received