

Chapter 18

Revenue

Performance Outcomes in Revenue

Performance Outcomes in Revenue

18.1 The Revenue Commissioners are responsible for having systems, procedures and practices that are adequate to secure an effective check on the assessment, collection and proper allocation of revenue. It is my responsibility to satisfy myself as to whether the manner in which the systems, procedures and practices have been employed and applied is adequate.

18.2 Achieving maximum compliance with tax obligations in a self-assessment system is a shared responsibility where conformance with tax law is a responsibility of the citizen while the tax authority has the responsibility and accountability for encouraging and enforcing compliance. A fundamental mark of the adequacy of Revenue systems is the capacity to evaluate performance through the compilation of relevant measures based on reliable information, especially in relation to tax compliance.

18.3 The key risks to a successful tax administration system are

- that taxable activity is not identified and pursued
- that the full amount of tax is not declared and collected from identified taxable activity.

18.4 In 2009, the net collection represented 20.3% of Goss Domestic Product (GDP) down 2.2% from 2008 levels and 4.7% since 2007. Over that period, tax collection fell by 30% while GDP reduced by 13.8%¹³⁴.

Chapter Focus

While recognising that Revenue produces a set of measures that record its output in terms of the tangible results of its assessment and collection activities the ultimate test of its effectiveness is the level of compliance by the taxpayers. The audit sought to examine the extent to which Revenue monitors those outcomes and publicly reports the results.

Compliance

18.5 Full tax compliance would be achieved if all those liable to tax paid the full amount of tax due on time. There are four basic tax compliance obligations

- to register for the taxes to which liable
- to file tax returns on time
- to correctly report all tax liabilities
- to pay taxes on time.

18.6 Only by measuring the level of compliance and tracking it over time can a judgement be made on whether compliance is improving or not. In doing so, it is desirable to distinguish measures that capture the overall level of compliance and those that relate to each of the basic compliance obligations outlined above.

¹³⁴ Change in GDP at current market prices from Quarterly National Accounts, Quarter 4 2009 and Year 2009 (preliminary) March 2010, Central Statistics Office.

International Comparison

18.7 An OECD Report in 2008¹³⁵, drawing on the experience of a number of tax administrations, examined possible measures and indicators¹³⁶ of compliance. In order to provide a systematic approach to monitoring and measuring compliance, the report encouraged tax administrations to develop a compliance-monitoring framework. The report notes that the different policy and legislative environments that tax administrations operate in should be borne in mind in interpreting the guidance provided.

18.8 A compliance-monitoring framework was defined as a strategy for monitoring compliance and evaluating the impacts of specific compliance improvement activities. A major component is a comprehensive set of compliance measures and indicators, and accompanying measurement methodologies, for each of the key compliance obligations of the major taxes administered by the tax administration. As well as enabling tax administrations account for their performance, such a framework assists in internal planning.

18.9 The OECD report refers to the work of some European countries including the Netherlands, Sweden and the United Kingdom, in developing an approach to monitoring compliance levels and trends. In some cases this includes estimating what is known as the 'tax gap'.

Measuring Tax Gaps

The tax gap is the difference between the amount of tax paid and the amount that would have been paid had all those liable to tax met all their compliance obligations.

Estimates of tax gaps can be based on 'top down' estimates or 'bottom-up' models or a combination of both. 'Top down' estimates use macroeconomic data from national accounts and data on consumption from surveys to estimate the total tax that should be collected. 'Bottom-up' models estimate components of the tax gap using data from internal sources such as surveys and operational data which is then extrapolated across the relevant population.

In countries where tax gap estimates are produced, the 'top down' approach is generally used for indirect taxes and the 'bottom-up' approach for direct taxes. Estimates of tax gaps for direct taxes generally focus on the components of the tax gap, such as type of non-compliance or type of taxpayer, rather than the total taxhead gap.

An example is the 2009 EU Commission report¹³⁷ on the VAT gap in the EU. The report was prepared for the Commission by an economic consultancy company and quantifies and analyses the VAT gap in each member state for the period 2000 to 2006. The study used a 'top-down' approach to calculate the theoretical liability from national accounts data and only used publicly available data. As well as fraud and evasion, the gap calculated includes legitimate tax avoidance measures and VAT not paid due to business insolvencies. The approach used does not allow the tax gap to be characterised in terms of identifying the sector, goods or type of business that are most susceptible to fraud. The VAT gap calculated for Ireland was 5% of the theoretical VAT liability in 2000, increasing to 7% in 2003 and falling each year until 2006 when it was calculated at 2%. The VAT gap for the EU-25 was estimated at 13% in 2000 and 12% in 2006.

¹³⁵ OECD, Forum on Tax Administration Compliance Sub-Group, Final Report, Monitoring Taxpayers' Compliance: A Practical Guide Based on Revenue Body Experience, June 2008.

¹³⁶ The term 'measure' is generally used where quantification of performance is possible. Indicators provide a less direct assessment of performance.

¹³⁷ EU Commission, Study to quantify and analyse the VAT gap in the EU-25 Member States, DG Taxation and Customs Union, September 2009.

Direct Compliance Measures

18.10 The OECD report identified the main measures of compliance used by tax administrations internationally and these are set out in Figure 95. That figure also provides an indication of whether those measures are used in Revenue.

Figure 95 Compliance Measures used Internationally

Compliance Component	Measure	Used by Revenue ^a
Registration	Percentage of businesses registered — number of taxpayers registered compared to independent data on the number of taxpayers from statistical authorities	X
Filing	Percentage of returns filed on time (or within a specified period of the due date) — the number of returns filed compared to the expected number of returns	√ ^b
	Non-filing tax gap — the total liability of late and non-filers minus the amount they pay	X
Correct Declaration	Percentage of overall tax liabilities correctly declared as measured by random audit programmes	X
Payment	Percentage of taxpayers paying on time	√ ^b
	Percentage of tax paid on time — amount of tax paid compared to the amount debited for a given period	√
Composite	Estimates of tax gaps for each tax	X

Notes:

- a “√” denotes used in Revenue reporting and “X” denotes not used.
 b Revenue do not report these measures separately but if they disaggregated the current timely compliance measure both of these measures would be available.

18.11 Revenue reports a timely compliance rate which is a composite measure that records the extent to which taxpayers submit returns or payments on time i.e. under this measure a taxpayer is considered to be compliant if either a return or payment is received in the due month (‘due month compliance’). Cases are also measured for returns or payments submitted one month after the due month (‘due month +1 compliance’). The rates are calculated by aggregating, within bands based on three case sizes (large, medium and other), the compliance rates for each taxhead on a weighted basis. The weighting is based on the annual yield for each taxhead, so greater importance is attached to compliance in the taxheads with the greatest yield. Rates are reported by case size category and show the ‘due month’ and ‘due month +1’ rates. The target compliance rates to be achieved by the end of 2010 and the actual rates for 2007 to 2009 are shown in Figure 96.

Figure 96 Timely Compliance Rates 2007 to 2009

Case Size	Due Month Compliance				Due Month + 1 Compliance			
	Target	2007 ^a	2008	2009	Target	2007 ^a	2008	2009
Large cases	95%	92%	92%	92%	99%	n/a	97%	96%
Medium cases	90%	86%	86%	85 %	95%	n/a	94%	93%
All Other cases	75%	68%	72%	72 %	85%	n/a	81%	81%

Note:

- a The definition of case sizes changed in 2008. The comparative figures for ‘due month compliance’ in 2007 have been restated accordingly. Restated 2007 figures for ‘due month + 1 compliance’ are not available.

18.12 Despite an increase of over €800 million in the amount of tax outstanding between 2007 and 2009¹³⁸, the compliance rates for large and medium cases have remained virtually constant. The compliance rates for the other cases category have also remained constant since an improvement in due month compliance in 2008. This apparent anomaly underlines the risks associated with combining the two aspects of compliance (filing and payments) into one indicator.

Views of the Accounting Officer

18.13 The Accounting Officer informed me that the lack of reliable independent data and the existence of registration thresholds for certain taxes make it difficult to ensure a reliable registration indicator. She also pointed out that Revenue report the percentage of random audits that do not produce a yield.

18.14 In relation to the timely compliance rate, the Accounting Officer stated that, as a result of the economic downturn, the environment in which Revenue operates fundamentally changed in the latter part of 2008. Consequently, Revenue considers that the timely compliance rates currently being achieved, while not reaching target, represent positive outcomes. She also said that this measure is designed to give an overview of returns and payment compliance and therefore is not as sensitive to changes in its component parts as specific measures. Changes in the level of outstanding tax are separately measured by Revenue.

Indicators of Trends in Compliance

18.15 As well as direct measures of compliance, movements in compliance levels can also be monitored through correlation between changes in tax receipts and changes in external statistics. Ascertaining attitudes to compliance is also valuable in analysing compliance levels. The use of indicators by tax administrations internationally was collated in the 2008 OECD Report and the indicators available which might be appropriate in an Irish context are

- the number of companies registered for tax compared with the number registered with a corporate regulatory body
- the income of self-employed taxpayers reported to the tax administration compared with the amounts estimated by the Central Statistics Office
- percentage of net corporate income that was taxable
- the amount of tax payable as a percentage of corporate profits before tax
- the amount of income tax payable as a percentage of net income
- effective tax rates — the average amount of tax raised compared with net business income
- the proportion of returns that are assessed as being ‘at risk’
- ratio of outstanding tax to annual gross or net collection
- survey findings on attitudes to compliance
- growth of net VAT compared to growth of retail sales and personal expenditure.

¹³⁸ Amount of tax outstanding was €1,286 million at 31 March 2008 and €2,112 at 31 March 2010.

18.16 In this context, Revenue use and report on two of these indicators

- The ratio of debt available for collection¹³⁹ to annual gross collection. This ratio has increased from 1.4% in 2007 to 2.8% in 2009. Such an upward trend may indicate a decline in payment compliance and/or reduced efficiency and effectiveness in debt collection.
- Revenue conducts surveys that include questions designed to probe compliance behaviour.

Views of the Accounting Officer

18.17 The Accounting Officer stated that many of these indicators have limitations to which solutions must be found before they can be incorporated into a compliance-measurement framework. These limitations include the lack of reliable independent data sources for the number of tax liable companies. Another limitation which is identified by the OECD is the fact that changes in the relationships between incomes and profits from independent sources and what is reported on tax returns may reflect factors other than changes in taxpayers' compliance. She said that the countries that use many of these indicators operate different compliance regimes and have different revenue requirements to Ireland. Therefore, a study of the effectiveness, validity and robustness of these indicators would be necessary before their inclusion in an Irish compliance measurement framework.

18.18 In relation to the increasing ratio of debt to annual gross collection, the Accounting Officer does not consider that the efficiency or effectiveness of Revenue's compliance programmes has been reduced. She said that Revenue is working with viable businesses that are unable to meet their tax obligations due to the current economic environment. Revenue is fully committed to make the necessary decisions, including closing businesses that are not viable or that seek to deliberately evade the obligation to pay on time.

Opportunities to Improve Compliance Information

18.19 In measuring its performance, Revenue needs to clearly distinguish between the outputs of its activities and the impact of those activities as measured by changes in compliance. Revenue's current measures are predominantly focused on outputs. Revenue needs to develop a comprehensive set of measures and indicators sufficient to demonstrate performance in relation to each compliance obligation. Only by doing so can it demonstrate that to the maximum extent possible all relevant economic activity is captured for tax purposes and that it has discharged its responsibility to evaluate the effectiveness of its operations. Opportunities to improve compliance information are set out below.

¹³⁹

Debt available for collection is the portion of tax outstanding that is not the subject of a taxpayer appeal.

Determine the Audit Gap

18.20 There is an opportunity for Revenue to determine the audit gap¹⁴⁰ using the results of its random audit programme. So far Revenue has not made full use of the data derived from random audits. Currently, the numbers of yielding and non-yielding random audits are reported. While this is indicative of the number of persons who do not comply in all respects with their obligations, it is not useful as a measure of the extent to which tax is underdeclared. It should be relatively simple to develop an indicator of correct declaration by expressing the underdeclaration¹⁴¹ as a percentage of the original declared liability.

Disaggregate Timely Compliance Measure

18.21 Disaggregating filing and payment compliance would give a clearer view of performance for both activities. The timely compliance rate currently measures a case as compliant if either a return or a payment has been submitted. It is noticeable that at a time when many taxpayers are facing financial difficulties, this measure is remaining static while the overall level of tax outstanding is increasing. As an indication of performance this is misleading. Consideration should be given to disaggregating this measure into its component parts i.e. return filing compliance and payment compliance.

Estimate the Tax Gap

18.22 By measuring the tax gap and tracking changes in it, Revenue would be better equipped to assess the level of non-compliance. Thereafter, in order to tailor its responses to the collection challenge it would need to devise relevant reviews and studies designed to identify the underlying factors that contribute to non-compliance.

Indicators of Trends in Compliance

18.23 There is scope to identify changes in compliance through correlation between movement in tax receipts and changes in economic variables. In general, tax collection can be compared with GDP to derive a lead indicator of collection compliance. There are clearly many reasons why the historic relationship between GDP growth and tax receipts could arise, but differences between the two that are not readily explained might at least provide a tentative indicator of changes in collection patterns¹⁴².

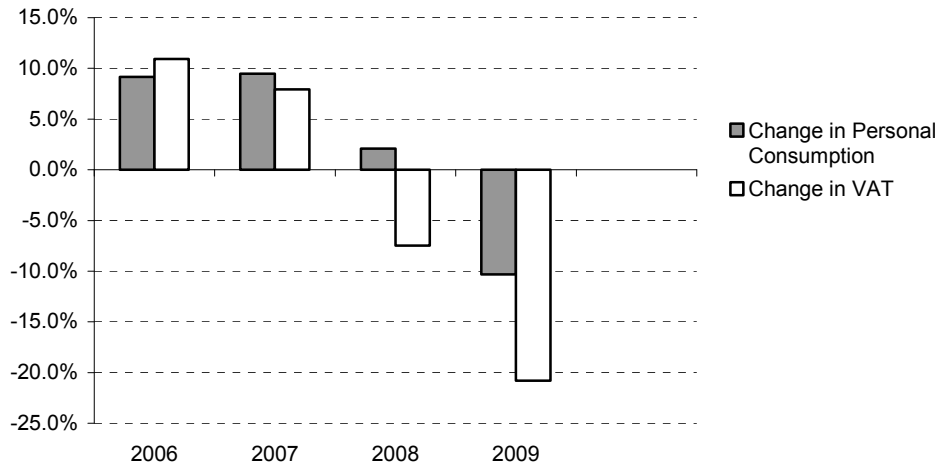
18.24 For instance, as VAT is a tax on consumer spending it would be expected that changes in the amount collected are closely related to changes in personal consumption of goods and services.

18.25 Figure 97 compares the percentage change in personal consumption of goods and services between 2006 and 2009 with the percentage change in net VAT receipts in the same period.

¹⁴⁰ The audit gap is a measure of the extent to which taxpayers have correctly declared their liabilities and is calculated as the difference between the amount of tax that would be collected if all taxpayers were audited by Revenue and the amount currently collected.

¹⁴¹ The amount of the underdeclaration may be different from the actual yield due to the fact that the audit settlement is an amount agreed between Revenue and the taxpayer as well as the fact that the agreed settlement may not be recoverable in all cases due to inability to pay.

¹⁴² While the focus of this chapter is on publicly reported performance information, it is acknowledged that Revenue has begun to include this indicator in its internal performance report.

Figure 97 Percentage Change in Personal Consumption^a and VAT 2006 to 2009

Note:

a Personal consumption of goods and services at current market prices from Quarterly National Accounts Quarter 4 2009 and Year 2009 (preliminary, March 2010, Central Statistics Office).

18.26 VAT as a percentage of personal consumption was 16% in 2006 but this fell to 12.6% in 2009. It would be useful to track changes in such relationships in order to prompt questions about the efficacy of the system in encouraging or enforcing compliance. It is accepted that a recession may lead to a shift in patterns of consumption towards lower rated or zero rated goods and services and as a result the fall in VAT may be greater than the fall in measured consumption. It could be useful to conduct studies into changes in consumption patterns and use the results as an aid to interpreting changes in these relationships.

18.27 A further potentially useful correlation would be between earnings as reported to Revenue¹⁴³ and the total wages and salaries estimated by the Central Statistics Office using its survey methodologies.

Survey Data

18.28 In addition to using compliance indicators, surveys can provide valuable feedback by helping to identify changes and patterns in compliance behaviour as well as the factors that influence behaviour. Revenue has, on a number of occasions in recent years, conducted surveys of taxpayers. In 2008, a survey of Small and Medium Sized Business Customers included questions designed to identify factors that influence compliance for this taxpayer group.

¹⁴³ Details of taxable income of each employee are provided to Revenue by the employer on the annual P35 return.

Conclusion

Revenue has responsibility for evaluating the effectiveness of its operations. This is best judged in terms of outcomes in the form of taxpayer compliance. Revenue does not have a well developed set of outcome focused measures and indicators of compliance.

Opportunities to improve compliance information include

- using the results of a systematic random audit programme conducted on the basis of representative sampling to measure the audit gap
- disaggregating the timely compliance measure to obtain separate measures of filing compliance and payment compliance
- measuring and tracking changes in tax gaps
- correlating movements in tax receipts with changes in relevant economic variables.

In the area of VAT which is directly linked to economic activity, Revenue might explore whether a comparison of trends in VAT collected and trends in measures of relevant economic activity such as consumer spending, could assist in identifying material changes in compliance. It is, of course, accepted that many factors will influence VAT collection such as shifts in patterns of spending and relative price changes across goods and services. However, such a comparison would be useful as an initial step in identifying areas for closer scrutiny using Revenue's compliance and audit powers.

It is recognised that measures and indicators, such as estimates of movements in the tax gap, only provide a starting point for the evaluation of performance and that many factors need to be considered to make the information more explanatory. Nevertheless, only by developing those measures and indicators can a comprehensive compliance measurement framework be put in place.

Observations of the Accounting Officer

18.29 The Accounting Officer stated that the distinction between output, outcome and impact is not always clearcut. She stated that Revenue has an extensive range of measurement systems and compliance evaluation methodologies that enable it to report on progress in improving taxpayer compliance. The measures in place cover a range of areas including collection, compliance, debt, audit and customer service. They provide an important input into the overall evaluation of performance and inform business and resource allocation priorities. She accepts the importance of enhancing Revenue's understanding of taxpayers' behaviour and the need to continue to enhance the measures in place.

18.30 She said that Revenue would consider disaggregating the payment and return compliance measure to determine whether it would deliver enhanced compliance reports. She has some concerns that doing so may not reflect the positive compliance dimension where a taxpayer submits a return and pays as much as possible in a situation where there are cashflow problems. Such problems need to be distinguished from deliberate non-engagement.

18.31 The Accounting Officer considers that although tax gaps can be useful indicators of overall trends, they are not suitable to track or isolate individual factors that give rise to movement in the gap. Measuring tax gaps would require considerable resources. Revenue is, however, exploring other methods of tracking VAT changes over time and against trends in other variables. Ireland is one of the member states that has expressed doubts about the methodology used in the EU study of VAT gaps.

18.32 Revenue has begun to do some research in linking economic variables to changes in tax collection. Preliminary work has been carried out to assess changes in VAT and excise with changes in retail sales data from the Central Statistics Office. The Accounting Officer said that the problem that arises with all such work is that it identifies divergences between tax collection and economic variables but it cannot explain the divergences because they tend to be multifactorial. A comparison of the overall trend in VAT collected and the amount that would be collected if VAT were applied to all consumption (known as the VAT Revenue Ratio) is also being examined.

18.33 The Accounting Officer noted the usefulness of surveys of taxpayers and said that they offered a unique insight into taxpayer behaviour and attitudes not otherwise available.

18.34 The Accounting Officer said that Revenue has measures in place under two of the four compliance components and part of a third one and sees value in developing these further. A project has commenced which seeks to measure changes in overall compliance behaviour based on tracking changes in risk scores. In addition, Revenue is examining models that will map its main inputs and outputs, describe the impact of those outputs and determine intermediate outcomes.