



## **Dáil Éireann**

### **An Coiste um Chuntais Phoiblí**

**An Tríú Tuarascáil Eatramhach do 2003  
(Éisteachtaí an Choiste, Deireadh Fómhair 2004 go Iúil  
2005)**

**Oifig na gCoimisinéirí Ioncaim; Gníomhaireacht  
Bainistíochta an Chisteáin Náisiúnta; agus an Cúlchiste  
Náisiúnta Pinsean**

*Nollaig 2005*

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### **Committee of Public Accounts**

**Third Interim Report for 2003  
(Committee hearings October 2004 to July 2005)**

**Office of the Revenue Commissioners; National Treasury  
Management Agency; and National Pensions Reserve Fund**

*December, 2005*



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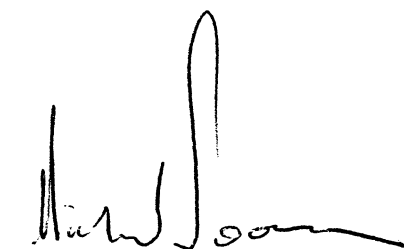
## *Chairman's Preface*

This interim report of the Committee of Public Accounts continues the practice of the Committee, which commenced with the Committee's reporting on 2002, of doing so periodically on a thematic basis. The subject matter of this report details the Committee's consideration of the Report of the Comptroller and Auditor General into the Office of the Revenue Commissioners, the National Treasury Management Agency and the National Pensions Reserve Fund.

The Committee will, in the next year, publish further interim thematic reports on a number of issues, namely, Department of Health and Children, Department of Education and Science and Department of Social and Family Affairs; Civil Service Commission, Department of the Environment, Heritage and Local Government and Department of Finance; Department of Communications, Marine and Natural Resources, Office of Public Works, Department of Transport and the Department of Enterprise, Trade and Employment; An Garda Síochána, Department of Defence and the Department of Foreign Affairs; Department of Agriculture and Food and Teagasc.

As Chairman, I want to thank the relevant State agencies for their co-operation in making the compilation of these report possible. I also want to compliment the members of the Committee for their diligent work throughout the year.

The Committee recommends this report to Dáil Éireann.

A handwritten signature in black ink, appearing to read 'Michael Noonan', written over a horizontal line.

Michael Noonan, T.D.,  
Chairman.

December, 2005



## ***Members of the Committee of Public Accounts***

### ***FIANNA FÁIL***

Seán Ardagh T.D.	Dublin South-Central
John Curran T.D.	Dublin Mid-West
John Dennehy T.D.	Cork South-Central
Seán Fleming T.D.	Laois-Offaly
John McGuinness T.D. ( <i>Vice-Chairman</i> )	Carlow-Kilkenny
Michael Smith T.D. <sup>4</sup>	Tipperary North

### ***FINE GAEL***

John Deasy T.D. <sup>2</sup>	Waterford
Tom Hayes T.D. <sup>3</sup>	Tipperary South
Michael Noonan T.D. <sup>1</sup> ( <i>Chairman</i> )	Limerick East

### ***LABOUR***

Joan Burton T.D. <sup>5</sup>	Dublin West
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### ***GREEN PARTY***

Dan Boyle T.D.	Cork South-Central
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### ***SOCIALIST PARTY***

Joe Higgins T.D.	Dublin West
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<sup>1</sup> Deputy Michael Noonan replaced Deputy Padraic McCormack by order of the House on 18<sup>th</sup> June, 2003.

<sup>2</sup> Deputy John Deasy replaced Deputy Paul Connaughton by order of the House on 20<sup>th</sup> October, 2004.

<sup>3</sup> Deputy Tom Hayes replaced Deputy John Perry by order of the House on 20<sup>th</sup> October, 2004.

Deputy Michael Noonan elected as new Chairman on 21<sup>st</sup> October 2004.

<sup>4</sup> Deputy Michael Smith replaced Deputy Batt O'Keeffe by order of the House on 16<sup>th</sup> November, 2004.

<sup>5</sup> Deputy Joan Burton replaced Deputy Pat Rabbitte by order of the house on 29<sup>th</sup> November, 2005.





## Orders of Reference of the Committee of Public Accounts

156. (1) There shall stand established, following the reassembly of the Dáil subsequent to a General Election, a Standing Committee, to be known as the Committee of Public Accounts, to examine and report to the Dáil upon—
- (a) the accounts showing the appropriation of the sums granted by the Dáil to meet the public expenditure and such other accounts as they see fit (not being accounts of persons included in the Second Schedule of the Comptroller and Auditor General (Amendment) Act, 1993) which are audited by the Comptroller and Auditor General and presented to the Dáil, together with any reports by the Comptroller and Auditor General thereon:  

Provided that in relation to accounts other than Appropriation Accounts, only accounts for a financial year beginning not earlier than 1 January, 1994, shall be examined by the Committee;
  - (b) the Comptroller and Auditor General's reports on his or her examinations of economy, efficiency, effectiveness evaluation systems, procedures and practices; and
  - (c) other reports carried out by the Comptroller and Auditor General under the Act.
- (2) The Committee may suggest alterations and improvements in the form of the Estimates submitted to the Dáil.
- (3) The Committee may proceed with its examination of an account or a report of the Comptroller and Auditor General at any time after that account or report is presented to Dáil Éireann.
- (4) The Committee shall have the following powers:
- (a) power to send for persons, papers and records as defined in Standing Order 83;
  - (b) power to take oral and written evidence as defined in Standing Order 81(1);
  - (c) power to appoint sub-Committees as defined in Standing Order 81(3);
  - (d) power to engage consultants as defined in Standing Order 81(8); and
  - (e) power to travel as defined in Standing Order 81(9).
- (5) Every report which the Committee proposes to make shall, on adoption by the Committee, be laid before the Dáil forthwith whereupon the Committee shall be empowered to print and publish such report together with such related documents as it thinks fit.

- (6) The Committee shall present an annual progress report to Dáil Éireann on its activities and plans.
- (7) The Committee shall refrain from—
  - (a) enquiring into in public session, or publishing, confidential information regarding the activities and plans of a Government Department or office, or of a body which is subject to audit, examination or inspection by the Comptroller and Auditor General, if so requested either by a member of the Government, or the body concerned; and
  - (b) enquiring into the merits of a policy or policies of the Government or a member of the Government or the merits of the objectives of such policies.
- (8) The Committee may, without prejudice to the independence of the Comptroller and Auditor General in determining the work to be carried out by his or her Office or the manner in which it is carried out, in private communication, make such suggestions to the Comptroller and Auditor General regarding that work as it sees fit.
- (9) The Committee shall consist of twelve members, none of whom shall be a member of the Government or a Minister of State, and four of whom shall constitute a quorum. The Committee and any sub-Committee which it may appoint shall be constituted so as to be impartially representative of the Dáil.

## **The Report**



# **1. Office of the Revenue Commissioners – Vote 9; and Chapters 3.1 to 3.5**

## **1 Proceedings of the Committee**

1.1. The Committee heard evidence from Mr Frank Daly Chairman, Office of the Revenue Commissioners and his officials; from Department of Finance officials; and from the Comptroller and Auditor General on 18 November 2004.

## **2 The Background**

2.1. Chapter 3.1 of the Report of the Comptroller and Auditor General deals with his statutory mandate in respect of the audit of Revenue. Net receipts at €32.2 billion, were almost €3 billion more than in 2002. The net receipts were €405 million in excess of the budget target figure of €31.809 billion. This surplus over the target figure was due mainly to better than expected yields from capital gains tax and stamp duties.

2.2. Chapter 3.2 deals with tax write-offs. The amount written off during the year was €19 million in comparison with €178 million in 2002. Revenue's objective is to minimise bad debts and only write them off when it is satisfied that they genuinely cannot be uncollected or are uneconomic to pursue. The amounts written off in 2003 represented about one quarter of 1% of the gross collection, including PRSI.

2.3. Chapter 3.3 summarised the revenue audit programme activity during 2003. Although the number of audits completed in 2003 was less than in 2002, the yield was greater by €160 million, mainly because of audits involving bogus non-resident accounts. In 2003, cases were not selected for audit on a purely random basis but rather identified by districts as representing the greatest risk taken from an initial random sample.

2.4. Chapter 3.4 details the prosecution of persons for not submitting tax returns and also the small number being prosecuted for serious tax evasion. In addition to the activity reported on in these areas, there was a considerable number of Revenue prosecutions in the Customs and Excise area, including 65 convictions for smuggling, 145 for marked mineral oil offences and 169 for unlicensed trading.

2.5. Chapter 3.5 summarised the position in each of the special investigations being undertaken by Revenue. The amount collected for the bogus non-resident accounts investigation stood at €782 million, made up of €225 million in DIRT paid by financial institutions, €227 million under the voluntary disclosure scheme and €330 million paid in subsequent investigations. The figure for the NIB-CMI investigation stood at €3 million and for the Ansbacher investigation, €44 million. The figure for the follow-through on the Moriarty, Mahon and Flood tribunals was €25 million. The figure for the offshore assets investigation stood at €705 million. The running total, as a result of these investigations, was at the time €1,609 million, which represented an increase of more than €50 million since the last report to the Committee on 22 July 2004.

2.6. Vote 9 shows that the estimated net cost of running the Office of the Revenue Commissioners in 2003 was in the region of €350 million, taking account of notional and allied services. Vote 9 no longer covers the cost of the Office of the Appeals Commissioners which are now met by way of a separate Vote, with one of the Appeals Commissioners as its Accounting Officer.

### **3 The Accountability Issues**

3.1. The accountability issues examined by the Committee were:

- Investigation of tax evasion using single premium insurance policies
- Investigation of Bogus Non-Resident Accounts
- Offshore Accounts
- Prosecutions
- Random Audits
- Tax Write Offs
- Tax incentive schemes – Cost benefit analysis and quantification of tax foregone

### **4 Examination of the issues**

#### **Investigation of tax evasion using single premium insurance policies**

4.1. According to the Department of Enterprise, Trade and Employment, the total amount underwritten in single premium insurance policies was in excess of €3 billion between 1988 and 2001. €25 billion was underwritten in single premium insurance policy business alone. Revenue's interest lies in the practice of using these products to hide untaxed income. In June 2004, Revenue indicated that it would commence a significant investigation into tax evasion in this area. The steps involved are:

- a preliminary identification of a area of risk to tax evasion. This was completed and Revenue is satisfied that it is a significant risk area
- structuring the investigation and deciding on the methodology and structure to be applied. Revenue engaged with the industry to see the level of co-operation it could secure. It defined a voluntary disclosure period

4.2. The investigation is focusing on the source of the money invested as a lump sum in the first instance. Until January 2001, tax paid on the accumulated growth in the fund and responsibility for collecting it lay with the insurance company which paid it on as part of its corporation tax. There was no tax liability attaching to the individual investor. In January 2001, the system was changed. Since then the accumulated growth in a fund is now taxed at 23% and the liability rests with the investor. The change was brought about because previously the exit tax regime had applied to policies written in the financial services area and it was required to bring the two together.

## **Investigation of Bogus Non-Resident Accounts**

4.3. The Committee considered the eligibility and liability reviews conducted as part of the bogus non-resident investigation. For the eligibility review, all disclosures were subject to the eligibility check and 17 of them (less than 0.5%) were found to be ineligible. Of the 17, eight have settled with additional payments of €851,000. One of the eight was successfully prosecuted and paid an additional amount of €299,000. The same individual also received a two-year suspended prison sentence.

4.4. For the liability review Revenue reviewed a sample of 268 cases, of which 143 were selected centrally at random and 125 were selected by the tax districts using local knowledge. They zoned in on the ones they thought most likely to have under-declared. In the C&AG's report 40 out of 222 completed cases had understated the liability. For the random cases, 112 of those reviewed were accepted as returned. In 14 cases an uplift was required. The total amount was €342,400. The total yield was €2.9 million.

## **Offshore Accounts**

4.5. The Committee noted that for the offshore accounts investigation, Revenue got co-operation from the ten financial institutions involved. Revenue contacted the account holders and 15,000 made disclosures. Revenue pursued those who did not make disclosures.

4.6. The extension of this investigation to offshore banks involved the gathering of information from voluntary disclosures. There were people among the 15,000 who voluntarily disclosed in respect of accounts they had with offshore institutions. That gave a basis for beginning some inquiries. There were extensive developments on the international scene as a result of the EU savings directive and the OECD tax information exchange agreements. A significant development was the requirement for financial institutions and other bodies to report suspicious transactions, to both the Revenue authorities and to the police.

## **Prosecutions**

4.7. The statutory offence in the tax code is one of knowingly aiding, abetting, assisting, inciting or inducing another person to knowingly or wilfully make an incorrect tax return. The legislation is focused on the tax return and not on advice being given to put money offshore. Revenue sought to level the playing field in terms of its ability to take such prosecutions. Legislation is not retrospective, so this will not help in respect of activities that took place in the past.

4.8. The Committee noted that the number of prosecutions for serious tax evasion, six in 2003, is very small. A special prosecutions unit was set up in 2003 but has not made inroads from the point of view of prosecutions. The division has a focus on bringing criminal prosecutions but the process is slow. Its success can be measured from the number of cases currently under investigation for prosecution. This takes account of referrals at various stages to the solicitor's office, the DPP, the Revenue Commissioners and the Office of Chief State Solicitor, attendance at court and adjournments.



4.9. The Committee reviewed the outcome of the court cases in 2003. In one case a defendant and the company to which he belonged was involved in evading €1.6 million in tax and was fined only €1,750 in court A second owed €804,000 in tax and the third owed €448,000. For the first time, in a recent case, a defendant was sentenced to community service in respect of tax evasion. By contrast, a person who wrote fraudulent cheques for €5,300 received a jail sentence of 18 months. This could be viewed as a glaring prejudice on the part of the establishment.

### **Random Audits**

4.10. Revenue undertakes approximately 16,000 audits per year. A new and totally risk-focused compliance programme will evolve in Revenue in the coming years. There were 274 random audits in 2003, which was fewer than expected. The yield from the audits was substantial, between 40% and 45% of those who were randomly audited had a liability. Random auditing is used as a means of controlling self-assessment. It is important that the self-assessment stick should be powerful enough to ensure that people are tax compliant. The Committee considered whether the increase in yield meant that taxpayers were more likely to take chances. Revenue clarified that the 274 audits were not selected at random. The yield from purely random audits has traditionally been low and accordingly random audits have been stratified and targeted over the years. The degree of targeting has increased progressively in recent years.

4.11. With the reintroduction of purely random audits tax compliance will be tested on three fronts — payment compliance, filing compliance and reporting compliance. The purpose of the exercise is to establish the liability that should have been paid for the relevant period and to compare it with the amount that was paid. The primary purpose of a subsequent audit will be to establish or verify the liability for each tax for which the customer has a liability. The comprehensive audits, which are by their nature the most resource intensive, will cover all of the taxes which are due. Another purpose of the new audits is to extrapolate and to try to get a picture of how self-assessment is working. The new cases, which are being selected entirely at random, will be sent to the regions. It is being made clear to regional officials of Revenue that exactly the same level of attention will need to be paid to random audits as to targeted audits. The first analysis of the results of the new programme will be available at the end of 2005.

4.12. The Committee considered if the random audit revealed 20% of cases where tax was underpaid then it could be concluded that 20% of all cases from which the audit samples are drawn are under-reported to a similar extent. In this case, a significant amount of money is written off without anybody making a decision on it. Revenue agreed that in this scenario, there would be a legitimate concern. Realistically, it is not possible to audit everybody. There are some 2.5 million tax paying entities and a staff of 6,500 people. The only way to optimize effectiveness is to continue refining risk so that the audits are more and more targeted at the ones that will yield.

## **Tax Write Offs**

4.13. The Committee noted that €17.5 million was written off in the PAYE sector in 2003 and €42.65 million in 2002. Income tax of €34.6 million was written off in 2003 and €23.7 million 2002. Approximately 75% of that, or €9.4 million, related to 28% of all cases. There are seven or eight grounds on which taxes are written off, including liquidation and receivership. There are two write-off methods. The vast bulk of writing-off is done by case working. The start of the process occurs when a person builds up arrears or gets into difficulties, following which the tax case workers try to collect the tax. If officials come to the view that the tax is not collectible, they have authority, depending on the amount involved, to recommend the writing off of the liability. Every month or six weeks, the Revenue Chairman, as Accounting Officer, takes the decision to write off the tax.

4.14. The average write-off was €1,033 in 2002 and approximately €2,700 in 2003. The two categories that stick out involve income tax, which largely concerns the self-employed and farmers, and VAT, which concerns businesses that have not made their returns. In 2003, the number of income tax related cases in the non-automated write-off category was 7,142. The figure for the automated write-off of income tax for 2003 was 18,323. The number of VAT-related cases in the non-automated category was 3,539 in 2003, and the number in the automated category was 5,171.

4.15. The Committee noted that the €1.6 billion arising from the various forms of tax evasion Revenue has managed to track does not represent the total amount being evaded in the economy. Revenue has not carried out a study of this issue. Some three or four have been carried out by independent experts during the years, not just in respect of Ireland, but in respect of EU and OECD countries. Their conclusions fluctuate wildly and no two agree. It is a matter to which Revenue has given some thought.

4.16. Tax evaders who are tracked down by Revenue, in addition to paying the taxed owed, pay interest and penalties. The amount in interest and penalties, is quite substantial. In addition to the additional revenue collected the real benefit is that the people concerned are brought into the tax net. In the medium to long term, while the money collected is important, strategically, the more important outcome is increased compliance.

## **Tax incentive schemes – Cost benefit analysis and quantification of tax foregone**

4.17. Many reliefs have been introduced for good and valid policy reasons. They had social and economic effects which were important at the time they were brought in. These include support for the provision of multi-storey car parks in most towns and addressing the shortage of nursing home beds. The Committee feel that nobody has carried out a cost-benefit analysis when considering the impact of tax reliefs to assess whether the amount of tax foregone was proportionate to the economic or social gain. This issue kicks into other areas such as public private partnerships. The question is whether the State would be better off building roads and bridges through the public capital programme, public private partnerships or a combination of the latter and tax levers which encourage private sector involvement.

4.18. In the case of 33 schemes that permit people to legitimately minimise their tax, it is not possible for the Department of Finance or the Revenue Commissioners to quantify the tax forgone. There are a number of schemes where Revenue has not looked for information on tax returns and is not in a position to quantify the tax costs. There is a move to a situation where the information on all of the more significant schemes will be captured. This will become available at the end of 2005 and be analysed and available early in 2006. In some cases it was a matter of the Revenue Commissioners and the Department of Finance making a decision to collect this data while in others it required legislation.

## **5 Findings and recommendations**

### **The Committee of Public Accounts**

#### **Finds specifically that:**

1. Taxes of some €32.2 billion were collected in 2003, an increase of €3 billion over 2002 and €405 million above the budget target figure.
2. Taxes written off in 2003 were €19 million which is about 0.25% of total collections.
3. The number of revenue audits carried out in 2003 was decreased from 2002 by 408 to 15,778 but the yield from these audits increased by €160 million to €29.5 million.
4. The results from various investigations underway by Revenue (bogus non-resident accounts, NIB-CMI schemes, offshore assets investigations) are satisfactory. Approximately €1.6 billion had been collected at 17<sup>th</sup> November, 2004.
5. For many of the tax incentive schemes brought forward in recent years it is not possible for Revenue or the Department of Finance to quantify the tax foregone through these schemes.

#### **And recommends in general that:**

1. Purely random audits should be included in the Revenue audit programme. The Committee welcomes the decision to do this with effect from 2004.
2. The Department of Finance and Revenue should put in place a mechanism for evaluating the effectiveness of the changes, made in the Finance Act 2005, that support the pursuit of those aiding and abetting tax evasion.
3. All future tax incentive schemes should have mechanisms built in to enable a proper monitoring of both the tax foregone and the benefits to be gained. The Committee welcomes the current initiative to review tax incentive schemes.

4. All proposed tax incentive schemes should be the subject of an ex-ante evaluation of the likely costs and benefits.
5. Whilst the Committee acknowledge the progress that has been made in tackling tax evasion it is timely for Revenue to establish, from macroeconomic and other data, the scale of the shadow economy that currently exists.



## **2. Office of the Revenue Commissioners – Vote 9; and Chapters 3.6 to 3.8**

### **1 Proceedings of the Committee**

1.1. The Committee heard evidence from Mr Frank Daly Chairman, Office of the Revenue Commissioners and his officials; from Department of Finance officials; and from the Comptroller and Auditor General on 2 December 2004.

### **2 The Background**

#### *Outstanding tax debt*

2.1. At the end of March 2004, outstanding debt on Revenue's books was €1.36 billion and Revenue expects to ultimately collect approximately 80% of this sum. The C&AG made a detailed review of how the figures were established and, in particular, the way in which the estimate of the amount likely to be collected was determined. He also examined, in a selection of cases, the extent of collection activity in the year. He found that the means of calculating overall tax arrears was generally sound and that any refinement to bring it up to financial reporting standard would have to be justified on a cost-benefit basis.

2.2. Looking at the specific collection targets in value terms, at the end of March 2004, 46% of the debt was over three years old while the target to be reached in 2005 is that no more than 25% of debt should be in that category. This is against a background where there is no provision for an increased level of write-offs and where the stated focus in the current strategy is on timely and robust action against late payment and non-payment of tax.

#### *The 1993 tax amnesty*

2.3. With regard to Chapter 3.8, the 1993 incentive amnesty was designed to give a final opportunity to individuals to put their tax affairs in order. Events in the past few years have resulted in the extensive disclosure of significant undeclared income which reached back into the amnesty periods. The terms of the incentive amnesty would have to be set aside for those who did not make a disclosure at the time. Of the 3,754 taxpayers who came forward in the voluntary disclose and pay phase of the bogus non-residents accounts investigation, 208 indicated that they had previously availed of the incentive amnesty. Some 62 of those lost the benefit of the amnesty and made additional payments totalling €3 million. The remaining 146 claimed that their amnesty declarations had disclosed their full liabilities at the time, including liabilities relating to bogus non-resident accounts, and that therefore, they did not have to make any additional payments in excess of those arising from their voluntary disclosures. It appears that, in general, these claims were accepted at face value by Revenue.

2.4. The incentive amnesty also comes into play in the case of those among the 8,000 who did not avail of the voluntary disclose and pay scheme but who had bogus non-resident accounts which pre-dated April 1991. Since it was mandatory for an

individual who had been in receipt of untaxed income or gains to avail of the incentive amnesty at the time, by not doing so such an individual would have committed an offence under the Waiver of Certain Tax, Interest and Penalties Act 1993.

2.5. The 1993 Act was an exceptional piece of law that balanced generous concessions with strong sanctions which were highlighted both during the passage of the legislation and in the promotion of the incentive amnesty at the time. However, no prosecution under the 1993 Act has been taken to date, although the Accounting Officer has indicated that prosecutions are being considered in a number of cases, notwithstanding the significant evidential and burden of proof difficulties.

### **3 The Accountability Issues**

3.1. The accountability questions examined by the Committee were:

- Restructuring of the Office
- Outstanding taxes
- Revenue-on-line-service
- The 1993 Tax Amnesty
- Cost-benefit analysis of tax incentive schemes

### **4 Examination of the Issues**

#### **Restructuring of the Office**

5.1. In 2003, Revenue completed the most fundamental restructuring of its organisation since it was founded in 1923. It involved the establishment of a large cases division that deals with the financial sector, high worth individuals and large corporations. These groups pay a significant amount of the tax paid in the State. The other significant division is the investigations and prosecutions section, with a focus on bringing more prosecutions into the frame. The majority of tax default will always be dealt with by settlement on payment of interest. However, it is recognised that there should be an increased number of prosecutions, even if only for the exemplary effect. The Collector General's division continues as the basis of collecting tax and there are various policy and legislation units in the national offices. The regional basis of the Revenue enables it to build up information on the tax base within that region.

#### **Outstanding taxes**

4.2. The Committee noted that the reconciliation between money paid by the taxpayer and Revenue's transaction recording systems (ITP) revealed differences under three different tax headings, (€74 million for PAYE, €34 million for PRSI and €3 million for VAT). The figure of €74 million is in the context of around €65 billion paid, that is, it represents 0.1% of the total, a very small amount.

4.3. Much progress has been made in reducing the debt even since the table was published on 31 May 2003. By 31 March 2004, during which €30.69 billion was raised in new charges, only €356 million or 1% of that current year charge was

outstanding. This emphasises the focus on current debt. There is €19 million of debt dating back to pre-1990.

4.4. The outstanding debt that related to the time period 1990 to 2001 was €737 million. For 2002 it was €223 million, and for 2003 it was €356 million. With regard to all of the debt, there is activity at some level by Revenue staff.

4.5. The proportion of the balance outstanding to the amounts raised vary for 2004. VAT is between 3% and 4%, PAYE is between 2% and 3%, PRSI is between 3% and 4%, income tax, other than PAYE, for self-employed and farmers is 15%, corporation tax is between 3% and 4% and capital acquisitions and capital gains taxes are approximately 9%. Small businesses with outstanding debt would not necessarily have gone out of business. They might have forwarded returns or there might be estimates which were unpaid. There could also be cases where companies had deducted PAYE and PRSI from employees' pay packets and not paid it over.

### **Revenue-on-line-service (ROS)**

4.6. There were capacity problems in 2003 when the number of filings increased from 9% to 40%. However, in 2004 when the number of business people and self-assessed taxpayers using ROS rose to 52%, it was thought to be working well. Revenue was paid €6.2 billion in 2003. The Committee was informed that at the end of 2004, Revenue won an international prize for the best security on an on-line site.

### **The 1993 Tax Amnesty (the second amnesty)**

4.7. Legislation enacted in 1993 provided for a number of offences in relation to the amnesty. It was an offence for a person to not avail of the amnesty if he or she had untaxed income and that penalties such as fines or terms of imprisonment were attached to that offence. If one availed of it there had to be full disclosure. The Director of Public Prosecutions is of the view that Revenue can go back more than ten years for indictable cases.

4.8. Inquiries were made into 91,000 account holders as part of the process. Approximately 2,000 of those account holders who received letters from Revenue came forward and admitted that they availed of the 1993 amnesty and 26 made additional payments. With regard to the rest of the 2,000, there is no evidence to date that they did not properly avail of the amnesty. While Revenue does not have concerns in that area, the post voluntary disclosure phase of the bogus non-resident campaign is ongoing.

4.9. In the ten years since the Act introducing the incentive amnesty of 1993 was passed, while there has been abundant evidence that the terms of the amnesty have not been complied with, no prosecutions have taken place. In that context, 8,000 people who had an opportunity to come clean on the bogus non-resident accounts under the voluntary disclose and pay scheme did not avail of the opportunity and may or may not have availed of the amnesty. It is likely that many of these individuals would have had pre-1991 bogus non-resident accounts. It seems that having a substantial bogus non-resident account prior to that date and failing to avail of the amnesty is *de facto* an offence. If it has taken ten years to even try a prosecution under it, it seems there



has been a failure somewhere along the line, even taking account of the laudable objective of Revenue of trying to maximise what it gets for what it puts in.

4.10. The general point is that when this legislation was put on the Statute Book in 1993, the way in which it was made a mandatory issue was understandable. If one had an issue, one had to avail of the amnesty. The confidentiality clauses in the legislation were aimed at encouraging everybody into availing of this amnesty and make as many people as possible compliant. However, the current reality for Revenue is that the confidentiality clause is a legislative handcuff in taking the type of prosecutions that were intended. It was good legislation at the time but, in hindsight, if it was under consideration now, it would be done in a different way.

## **5 Adoption of Reports**

5.1 The Committee disposed of Chapters 3.1 to 3.8 of the 2003 Annual Report of the Comptroller and Auditor General and noted Vote 9 of the 2003 Appropriation Accounts.

## **6 Findings and recommendations**

### **The Committee of Public Accounts**

#### **Finds specifically that:**

1. Revenue in 2003 completed the most fundamental restructuring of its organisation since its foundation.
2. The level of tax debt outstanding at March 2004 was €1.36 billion. Revenue expects to ultimately collect 80% of this amount.
3. At March 2004, 46% of tax debt was over three years old. The target for 2005 is that no more than 25% should be in this category.
4. Although the collection of tax debt may cause some hardship for small and medium sized companies and individuals there is no evidence that the collection of taxes pushes tax payers into bankruptcy. There are cases where tax debt is in respect of cases where PAYE and PRSI has been deducted from employees and has not been paid over to Revenue.
5. In 2003 the threshold for publication of tax defaulters (€12,700) had not changed since 1986. It has risen to €30,000 with effect from January, 2005.
6. The 1993 tax amnesty balanced generous concessions with strong sanctions. There is evidence that the terms of the amnesty have not been complied with but no prosecutions have been made to date. The confidentiality clause included in the amnesty provisions denies access to information needed to take a prosecution.
7. The number of business people and self-assessed taxpayers using the Revenue-on-line service (ROS) increased to 52% in 2004.

**And recommends in general that:**

1. Specific attention should be given to PAYE and PRSI debt, especially for business enterprises where the tax has been deducted from employees but not passed on.
2. The threshold levels for publication of tax defaulters should be occasionally reviewed.



### **3. National Treasury Management Agency – 2003 Accounts; National Pension Reserve Fund – 2003 Accounts**

#### **1 Proceedings of the Committee**

1.1. The Committee heard evidence from Dr Michael Somers Chief Executive, National Treasury Management Agency (NTMA), and his officials; from Mr Donal Geaney, Chairman of the National Pensions Reserve Fund (NPRF); from officials of the Department of Finance; and from the Comptroller and Auditor General on 10 March 2005.

#### **2 The Background**

##### *Public Accountability Issues*

2.1. Under existing legislative arrangements, the C&AG's annual report will always have a reference to the accounts of the NTMA and the NPRF even though there may be no critical comment, as is the case for 2003.

2.2. Apart from its responsibility for managing the national debt, the NTMA has been given operational responsibility over the years for several other activities of the State. Among the most prominent are those in respect of the State Claims Agency, the National Development Finance Agency, and the dormant accounts fund. A clear audit certificate was issued on all of those accounts for 2003 by the end of June 2004.

2.3. The NTMA has a management role in regard to the national pensions reserve fund. Overall responsibility lies with a Government-appointed commission which is very much independent in the exercise of its functions. There are, therefore, no public accountability issues arising from the financial audit process of the accounts under consideration.

##### *National Pensions Reserve Fund Commission*

2.4. The NPRF's objective is to meet the costs of social welfare and public service pensions from 2025 until at least 2055, when these costs are projected to increase dramatically due to the aging of the population. Three in every four people now working are expected to benefit from the NPRF during their retirement.

2.5. 2004 saw the end of the fund's infancy, with the completion of the averaging-in process to the capital markets and a decision to commit 18% of the fund to additional asset classes. The fund's value at the end of 2004 was €1,689 million, compared with €7,426 million two years earlier. Excluding the 2003 and 2004 Exchequer contributions, which total €2,280 million, the fund earned just less than €2 billion on its investments in that period. In percentage terms, the fund earned a return of 12.8% in 2003 and 9.3% in 2004. This strong performance has enabled the fund to recover from the bear market of 2002.

2.6. The fund was established in April 2001, through an initial Exchequer contribution of €6,515 million. As the economic and financial markets outlook was

not certain an averaging-in approach was pursued which would reduce the fund's market entry risk by spreading its market entry over time. The investment strategy was delayed as market conditions deteriorated throughout 2002 and assets were purchased at attractive valuations as recovery commenced in 2003. An averaging-in programme leads to a fund underperforming its benchmark in a rising equity market because it holds fewer equities and more cash than the benchmark. In 2004 as equity markets rose, the fund underperformed its benchmark by 2% as the averaging-in programme was completed. The fund has outperformed its strategic benchmark by a cumulative 8.9% over the period from inception in 2001 to the end of 2004.

2.7. During 2004, it was decided to allocate 18% of the fund to additional asset classes — 8% each to property and private equity and 2% to commodities. Private equity offers the prospect of substantial additional return, while property and commodities improve diversification. It was also decided to increase the fund's small cap equity allocation from 2% to 4% and to allocate 2% of the fund to emerging market equities. The diversification effect of the new asset classes reduces the fund's dependence on the performance of any single asset class.

2.8. The NPRF is committed to investing in PPPs on an opportunistic basis. €200 million has been available for investment in Irish projects since 2003 and more funds can be added should opportunities arise. While suitable projects have been slow to materialise, progress has been made in 2005, with the fund joining a consortium tendering for the M50 motorway upgrade. In future, rather than joining particular consortia in tendering for projects, the NPRF will make equity and/or debt finance available to the winning bidder, provided it is satisfied with the prospective rates of return.

### **3 The Accountability issues**

3.1. The accountability issues considered by the Committee were:

- Management of the National Debt
- National Pensions Reserve Fund
- Investing in PPP Projects
- Investing in private equity and property
- Post Office Savings Fund
- FRS 17

### **4 Examination of the Issues**

#### **Management of the National Debt**

4.1. The Committee noted that the costs of the NTMA's central fund rose from €9.7 million to €15.1 million (55%) between 2001 and 2003. Factors outside of NTMA control such as Government policy decisions have increased the national debt which stood at €7.6 billion at the end of 2003. The NTMA manages the debt's configuration in terms of the mix of short-medium and long-term debt and decides the amount of debt to be held within or outside of the State. The Committee inquired about the current debt management strategy. Interest rates are historically low. Interest rates, including fixed rates, were at the time at 3% or 4% for medium to long-

term money. The NTMA has sought to lock as much money in as possible at these attractive rates. The interest bill on the debt has fallen by €1 billion compared to when NTMA was created.

4.2. Increases in the rate of interest impact on the National Debt. It was calculated that at the time a 1% increase in interest rates in the eurozone would increase the cost of servicing the national debt by €6 million.

### **National Pensions Reserve Fund**

4.3. The Committee noted that the fund stood at €1.689 billion at the end of 2004. The State has given almost €10 billion directly to the fund and earnings have been approximately €2 billion, less the cost of maintaining the scheme. A review in 2004 indicated that the fund was 2% below the benchmark relating to the 80:20 allocation of equities and bonds. The reason for that was the holding of cash throughout this period. The NPRF consider that the appropriate benchmark is the cost to the State as opposed to the returns to the State of having these funds in this particular category. The overall objective is to produce a substantial additional return to the State over and above its opportunity cost, which is an important benchmark. The goal of 80% in equities, 20% in bonds and nothing in cash is close to being achieved.

4.4. The general prognosis for the coming years is that equities are not expected to yield much more than 7% to 9% cumulatively. Bonds could well be negative in that period. The 2004 performance was a yield of 11.2% on the bond portfolio. Interest accounted for around 3.5% of this. The remainder came from an appreciation in the price of the bonds. The only way this can happen is by falling interest rates due to the factor of the interest rate compared to the fixed rate on the bond. The opposite is very likely to happen. As soon as the economic conditions of France and Germany recover a rise in European interest rates is expected.

### **Investing in PPP Projects**

4.5. The Committee considered the potential conflict of interest arising from NTMA and NPRF involvement in PPP projects. The NPRF does not have any conflicts of interest but the NTMA may have as it has other functions relevant to the process. There was a perception of a conflict of interest in cases where NTMA was part of the bidding consortia for PPP Projects. Accordingly NTMA has decided that it will stay out of the bidding process and take on a role of providing finance to the winning consortium. The European Investment Bank does this in connection with providing loan finance at cheap rates through a winning group.

4.6. The Committee noted that the issue of a conflict of interest applied to the NDFA which had removed itself as an adviser to the M50 project. The NPRF joined a consortium and put €20 million into a bid of €100 million. The NTMA had its own ideas about how the M50 project could be funded, for example, to secure ties to the State's share of the tolls on the M50. It believed this would produce €400 million or €500 million and might require a PPP project on the funding side.

4.7. When PPPs started, the NTMA researched the rates of return on PFI projects in the UK. Initially the annual return was 25% on equity. More recently this has fallen to

just under 20%. Officials in the Department of Finance began to pay attention when they saw that the NPRF was interested in generating money for the pension fund through PPP projects, rather than borrowing. The mandate is to maximise the return for the taxpayer, within an acceptable level of risk.

### **Investing in private equity and property**

4.8. The amount of money to be invested in private equity is to increase substantially to 8% by 2009. The Committee considered the underlying reasons for this decision. The NPRF is unusual in so far as it does not have short-term liquidity requirements as it is not expected to pay out money before 2025. It is a sizeable pension fund which offers the ability to participate in particular types of investments that do not require immediate liquidity.

### **Post Office Savings Fund**

4.9. A management fee in the region of €25 million is paid by NTMA to An Post. The chief executive of An Post recently reported that NTMA was asking that this be cut by 33%, or €8 million. The fee is 2.75% of POSB funds. The interest rate NTMA is paying is in some instances as low as 0.1%, so most of the money is going to pay fees to An Post. POSB funds are increasing. An internal NTMA review indicated that An Post was probably making a profit of approximately €15 million on the fee.

### **FRS 17**

4.10. The Committee noted that Financial Reporting Standard (FRS) 17 is leading to more comprehensive disclosure of pension liabilities. From 2005 there is a requirement to show the full pension charge which was incurred in respect of the staff in the annual financial statements. If there was an indication of what the potential costs are, it might allow more for reasonable contributions to be made. FRS 17 is considered an artificial standard as there are fixed rules for calculating the pension liability, whereas actuarial valuations take into account the general circumstances of what one is looking at. FRS 17 does not take account of the long term outlook. It simply gives a snapshot at a point in time and it can change dramatically from one period to another. In terms of the semi-State sector, the biggest problem going forward is that many existing defined pension benefit schemes tie the pensions of future pensioners to current employees. When one pays for productivity, one gets a huge increase in pension liability, where there is no productivity.

## **5 Adoption of Reports**

5.1. The Committee disposed of the 2003 accounts for the NTMA and the NPRF and disposed of Chapters 14.1 and 14.2 of the 2003 Annual Report of the Comptroller and Auditor General.

## **6 Findings and recommendations**

### **The Committee of Public Accounts**

#### **Finds specifically that:**

1. The level of the national debt was €37.6 billion at the end of 2003. The management of the debt and control of the associated interest cost was satisfactory.
2. The value of the NPRF was €9.56 billion at the end of 2003. The fund performed well in 2003. The phasing-in period for the fund was completed in 2004 when the equity-bond allocation of 80:20 was almost reached.
3. The fund has reached a size where there are opportunities to diversify the asset classes in pursuit of higher returns, without a commensurate increase in overall portfolio risk.
4. The NTMA is taking an active interest in participating in PPPs in Ireland by offering finance to winning bidders. It has decided not to participate directly in bidding consortia due to a perceived conflict of interest. The NPRF has the capability to invest in major infrastructure projects in Ireland.
5. The management fee paid by NTMA to An Post in respect of the POSB funds is €25 million or 2.75% of the funds. By reference to the prevailing interest rates offered on these funds, the fee appears to be high.
6. The introduction of FRS 17 will focus more management attention on providing for future pensions. This is a positive development where productivity agreements can have a significant effect on the liability for future pensions.

#### **And recommends in general that:**

1. The NTMA and NPRF should continue to increase their involvement and expertise in supporting major infrastructure investments in Ireland, consistent with a satisfactory rate of return in association with the level of risk inherent in these ventures.
2. The level of fee paid by NTMA to An Post should be equitable to both parties.