



# Fifth Report

of the

## Commission on Taxation

(including index to the five reports)

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# TAX ADMINISTRATION

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October 1985

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## TABLE OF CONTENTS

	<i>Page</i>
Preface ... ..	17
The Key Elements of Proposed Reforms ... ..	21
List of Recommendations ... ..	35
Glossary ... ..	47

## PART I

### GENERAL APPROACH

<i>Chapter</i>	<i>Paragraph</i>	<i>Page</i>
<b>1. General Principles</b>		
Introduction ... ..	1.1	55
Basic Principles ... ..	1.2	55
The Existing System— Broad Impressions ... ..	1.5	56
<i>Criticisms of the System</i> ... ..	1.10	57
Assessment ... ..	1.11	58
Collection and Enforcement ... ..	1.14	59
Appeals ... ..	1.15	59
Consultation Procedures ... ..	1.16	59
<i>Effects of Our Proposals</i> ... ..	1.17	59
Conclusion... ..	1.18	60
<b>2. The Legislative Process</b>		
Introduction ... ..	2.1	62
<i>Present System</i> ... ..	2.2	62
A Range of Views ... ..	2.4	62
		5

Chapter	Paragraph	Page
<i>The Options</i> ... ..	2.11	65
Technical Finance Bill ... ..	2.12	65
Advance Publication of Legislation ... ..	2.14	66
Joint Oireachtas Committee ... ..	2.15	66
Advisory Committee ... ..	2.16	67
Permanent Review Body ... ..	2.21	68
Staff Mobility ... ..	2.23	68
Consolidation of Tax Legislation ... ..	2.25	69
Recommendations ... ..	2.28	69

### 3. Revenue Practice

Introduction ... ..	3.1	71
Present Position ... ..	3.2	71
Criticisms of the Present Position ... ..	3.5	72
Advance Rulings ... ..	3.9	73
Revenue Discretion ... ..	3.12	74
Specific Aspects of Revenue Practice ... ..	3.21	77
The Board of the Revenue Commissioners	3.27	78
Conclusion... ..	3.32	79
Recommendations ... ..	3.33	79

## PART II

### TAX ASSESSMENT

#### 4. Assessment Procedures

Introduction ... ..	4.1	83
<i>Existing Procedures</i> ... ..	4.3	84
Large Number of Appeals ... ..	4.7	85
Backlog of Appeals ... ..	4.8	85
The 1983 Legislation ... ..	4.12	87
<i>Self-Assessment</i> ... ..	4.17	89
Main Features ... ..	4.22	91
Experience with Self-Assessment in Ireland	4.24	92
Advantages and Disadvantages of Self-		
Assessment ... ..	4.33	93
Basis of Assessment... ..	4.40	96
A New Style Return Form... ..	4.42	97
Filing of Returns ... ..	4.45	97

Chapter	Paragraph	Page
Compliance Code ... ..	4.49	98
Arrangements for Payment of Tax ... ..	4.53	99
Checking and Auditing of Returns ... ..	4.55	100
Enforcement ... ..	4.58	100
Revenue Implications ... ..	4.61	101
Treatment of Capital Gains and Capital		
Acquisitions ... ..	4.63	102
Conclusion... ..	4.68	103
Recommendations ... ..	4.71	103

#### 5. Withholding Taxes

Introduction ... ..	5.1	105
The Issue in General ... ..	5.2	105
Withholding by Income Source—		
An Overview ... ..	5.8	106
Government Securities ... ..	5.9	107
Deposit Interest ... ..	5.13	107
Distributions ... ..	5.20	109
Capital Gains ... ..	5.26	110
Gifts and Inheritances ... ..	5.28	111
<i>Construction Industry Scheme</i> ... ..	5.33	112
Appeals ... ..	5.38	113
Rate of Tax ... ..	5.42	114
<i>Other Sectors</i> ... ..	5.43	114
Recommendations ... ..	5.46	115

#### 6. PAYE

Introduction ... ..	6.1	116
Main Features of Present System ... ..	6.2	116
Effects of Our Proposals ... ..	6.11	119
<i>Other Issues</i> ... ..	6.14	120
Non-cumulative System ... ..	6.15	120
Self-assessment for PAYE Taxpayers	6.24	123
Conclusion... ..	6.31	125
Recommendation ... ..	6.33	125

#### 7. Tax Appeals

Introduction ... ..	7.1	127
Appeals under Self-Assessment ... ..	7.2	127
Appointment of Appeal Commissioners ... ..	7.3	127

Chapter	Paragraph	Page
Circuit Court Appeals ... ..	7.5	128
Appeal to High Court ... ..	7.9	129
<i>In Camera</i> Appeals ... ..	7.11	130
Taxpayers Right to have Appeal Heard ...	7.13	130
Recommendations ... ..	7.15	131
<b>8. Compliance Costs and Taxpayer Assistance</b>		
Introduction ... ..	8.1	132
<i>Compliance Costs</i> ... ..	8.2	132
Compensation for Compliance Costs	8.7	133
<i>Taxpayer Assistance</i>		
Direct Assistance to Taxpayers ... ..	8.12	135
Forms and Publications ... ..	8.20	136
Parliamentary Questions ... ..	8.26	137
Recommendations ... ..	8.29	138

### PART III

## TAX EVASION AND AVOIDANCE

<b>9. Public Perceptions of Tax Evasion</b>		
Introduction ... ..	9.1	143
Public Perceptions ... ..	9.2	143
Conclusions ... ..	9.6	145
<b>10. Tax Evasion</b>		
Introduction ... ..	10.1	146
The Administrative Background ... ..	10.3	146
The Extent of the Problem ... ..	10.13	149
Administrative Data ... ..	10.17	150
Tackling Evasion ... ..	10.28	153
Conclusion... ..	10.33	155
Recommendations ... ..	10.35	155
<b>11. Tax Avoidance</b>		
Introduction ... ..	11.1	156
The Context ... ..	11.3	156
Official Attitudes to Avoidance... ..	11.5	157

Chapter	Paragraph	Page
Attitude of the Courts towards Tax Avoidance ... ..	11.8	158
Attitude of the Legislature towards Tax Avoidance ... ..	11.12	159
The Specific Approach ... ..	11.13	159
The Transactions at Arm's Length Approach	11.16	160
The Administrative Control Approach ...	11.19	160
The General Approach ... ..	11.22	161
Retrospective Anti-Avoidance Legislation	11.27	162
Conclusions ... ..	11.30	163
Recommendations ... ..	11.32	163

### PART IV

## EXAMINATION, COLLECTION AND ENFORCEMENT

<b>12. Information Powers of the Revenue Commissioners</b>		
Introduction ... ..	12.1	167
Principles ... ..	12.2	167
<i>Scope of Information Powers</i> ... ..	12.4	168
Income Tax and Corporation Tax ...	12.5	168
PAYE/Construction Industry Sub-Contractors ... ..	12.13	170
VAT ... ..	12.14	170
<i>The Issues</i> ... ..	12.15	170
Powers of Entry and Inspection of Records ... ..	12.16	171
Code of Conduct ... ..	12.23	173
Search of Premises ... ..	12.27	174
Power to Search Persons ... ..	12.32	175
Power to Obtain Information about Named Taxpayers ... ..	12.36	176
Power to Obtain Information about Tax Avoidance ... ..	12.41	177
Treatment of Banking Business ... ..	12.44	178
Occasional Information Returns ... ..	12.49	180
Compliance Costs ... ..	12.59	183
International Exchanges ... ..	12.60	183
Obligation to Keep Records ... ..	12.63	184

Chapter	Paragraph	Page
Period of Retention ... ..	12.65	184
Micro-film Records ... ..	12.68	185
Recommendations ... ..	12.69	185
<b>13. Tax Offences and Penalties</b>		
Introduction ... ..	13.1	188
Present Range of Offences and Level of Penalties	13.2	188
<i>Imposition of Penalties</i> ... ..	13.7	189
Back-duty Settlements ... ..	13.13	191
Publication of Names of Tax Defaulters	13.21	194
Summary ... ..	13.25	195
Recommendations ... ..	13.30	196
<b>14 A New Scheme of Offences and Penalties</b>		
Introduction ... ..	14.1	197
General Principles... ..	14.4	197
Incorrect Returns (Defaults) ... ..	14.7	199
Penalty Scale ... ..	14.14	200
Failure to Submit Returns ... ..	14.19	201
Failure to Notify Chargeability ... ..	14.23	202
Appeals Against Penalties ... ..	14.26	203
Mitigation of Penalties ... ..	14.28	204
Criminal Offences Related to Taxation ... ..	14.29	204
Criminal Investigations ... ..	14.36	206
Recommendations ... ..	14.37	207
<b>15. Collection and Enforcement of Payment</b>		
Introduction ... ..	15.1	209
Broad Impressions ... ..	15.2	209
<i>The Collection System</i> ... ..	15.6	210
Compliance ... ..	15.10	211
The Office of the Collector General	15.17	214
<i>Enforcement of Payment</i> ... ..	15.23	215
County Registrar/Sheriff Enforcement	15.28	217
Conclusion ... ..	15.38	219
<i>Proposed Enforcement Structures</i> ... ..	15.40	220
Powers to Enforce Collection ... ..	15.49	222
The Power of Seizure ... ..	15.50	223
Other Powers and Procedures ... ..	15.58	224
Conclusion... ..	15.68	227
Recommendations ... ..	15.69	227

Chapter	Paragraph	Page
<b>16. Special Collection Arrangements</b>		
Introduction ... ..	16.1	229
Instalment Arrangements and Deferred Payments ... ..	16.3	229
Write-off of Uncollected Taxes and Interest	16.11	231
Preferential Claims in Liquidation or Receivership ... ..	16.16	233
The Case for Revenue Preference ... ..	16.24	235
<i>The Phoenix Syndrome</i> ... ..	16.36	239
Identification ... ..	16.41	240
Special Measures ... ..	16.42	240
Recommendations ... ..	16.47	241

## PART V

### ADMINISTRATION OF SPECIFIC TAXES

<b>17. Administration of Direct Expenditure Tax</b>		
Introduction ... ..	17.1	245
Developments in the United Kingdom ... ..	17.3	245
Assessment of Tax ... ..	17.5	246
Information Required ... ..	17.8	247
Collection of Tax ... ..	17.11	248
Certificates from Financial Institutions... ..	17.14	248
<i>Treatment of Assets</i> ... ..	17.16	249
Housing ... ..	17.19	250
<i>Relief for Savings Made Before the Transition</i>	17.25	251
The Total Assets Method ... ..	17.30	252
The Net Assets Method ... ..	17.32	252
The Credit Method ... ..	17.34	252
The Capital Gains Tax Method ... ..	17.35	253
The Transitional Period ... ..	17.38	253
Conclusion... ..	17.40	254
<b>18. Administration of Value-Added Tax</b>		
Introduction ... ..	18.1	255
<i>Accounting for Value-Added Tax</i> ... ..	18.2	255
VAT Accounting Periods ... ..	18.8	257

<i>Chapter</i>	<i>Paragraph</i>	<i>Page</i>
VAT on Imports ... ..	18.20	259
VAT Waiver on Imports for Re-Export	18.25	261
Deferred Payment of VAT on Imports	18.30	262
Imported Goods of £200 or less ... ..	18.36	264
Registration for VAT ... ..	18.40	265
Anomalies in VAT Registration ... ..	18.48	268
Second-Hand Goods ... ..	18.53	269
Recommendations ... ..	18.58	271

19. **Administration of Customs and Excise Duties**

Introduction ... ..	19.1	272
Broad Impressions ... ..	19.2	272
Legislation ... ..	19.6	273
Appeal Procedures ... ..	19.11	274
Customs Clearance Procedures ... ..	19.20	276
Inland Clearance Depots ... ..	19.21	276
Computerisation ... ..	19.26	278
Enforcement and Penalties ... ..	19.29	278
Seizure ... ..	19.33	279
Offences and Penalties ... ..	19.43	282
Recommendations ... ..	19.48	283

20. **Administration of Motor Vehicle Duties**

Introduction ... ..	20.1	285
Problems of Present System ... ..	20.2	285
Rates ... ..	20.3	285
Administration ... ..	20.4	286
Motor Insurers ... ..	20.5	286
An Post ... ..	20.13	288
Evasion ... ..	20.17	288
Recommendations ... ..	20.27	291

21. **Re-structuring the System of Taxation**

Introduction ... ..	21.1	292
Classification of Taxes ... ..	21.2	292
Rising Level of Taxation... ..	21.4	293
Constraints... ..	21.5	293
Revenue Effects of Our Proposals ... ..	21.8	294
Timing ... ..	21.9	294
Possible Tax Structures ... ..	21.10	294
Basis of Estimates ... ..	21.15	296

<i>Chapter</i>	<i>Paragraph</i>	<i>Page</i>
Income Distribution Effects of Our Proposals ...	21.21	297
Incidence ... ..	21.22	298
Equity... ..	21.24	298
Reservation by Mr Daniel Murphy ... ..		301

**APPENDICES**

<i>Appendix</i>	<i>Page</i>
1. Construction Industry: Tax Deduction Scheme ... ..	305
2. The PAYE System... ..	309
3. Anti-Avoidance — Transfer of Assets Abroad... ..	312
4. Maintenance and Preservation of Records ... ..	315
5. Tax Offences and Penalties ... ..	321
6. Collection Procedures ... ..	327
7. Solicitor Enforcement ... ..	333
8. County Registrars and Sheriffs ... ..	336
9. VAT on Imports ... ..	339
10. Organisation and Procedures in Customs and Excise... ..	343
11. Customs and Excise Legislation ... ..	353
12. Customs and Excise Offences and Penalties ... ..	355
13. Revenue Effects of Our Proposals ... ..	358

**ANNEXES**

<i>Annex</i>	<i>Page</i>
To Appendix 6 Comparison of the History of Collection of VAT Periods, March/April, 1982, March/April, 1983 and March/April, 1984. ... ..	332
To Appendix 10 Periods of Deferment on Customs and Excise Duties ... ..	350
To Appendix 13 Personal Allowances and Tax Credits ... ..	371
To Appendix 13 Proposed Number of Taxpayers ... ..	372
To Appendix 13 Revenue Yield from Second Report ... ..	374

**INDEX**

(to the five reports of the Commission on Taxation)

<i>Index</i>	<i>Page</i>
First Report: Direct Taxation ... ..	377
Second Report: Direct Taxation, The Role of Incentives ... ..	386
Third Report: Indirect Taxation ... ..	391
Fourth Report: Special Taxation ... ..	397
Fifth Report: Tax Administration ... ..	399

**LIST OF TABLES**  
(in body of report)

<i>Table</i>	<i>Title</i>	<i>Page</i>
1.	Income Tax Appeals as at 31 December, 1984 ... ..	86
2.	Corporation Tax Appeals as at 31 December, 1984 ... ..	86
3.	Number of Appeals Heard by the Appeal Commissioners	87
4.	Distribution of Specified Amounts for Taxpayers Making Timely Appeals ... ..	93
5.	Normal Basis on which Income is Charged to Tax Under the Present System ... ..	96
6.	Complicating Factors in PAYE ... ..	117
7.	Indicators of Volume of Work in PAYE	118
8.	Complicating Factors in PAYE Compared with New System ... ..	120
9.	Parliamentary Questions in Individual Cases, 1984 ... ..	138
10.	Attitudes to Tax Evasion and Other Forms of Civic Dishonesty — Permissiveness Scores... ..	144
11.	Irish Attitudes to Tax Evasion and Other Forms of Civic Dishonesty — Permissiveness Scores ... ..	144
12.	Customs and Excise Offences ... ..	150
13.	Back-Duty Settlements for Income Tax and Corporation Tax ... ..	151
14.	PAYE Audits ... ..	152
15.	Yield from VAT Audits ... ..	152
16.	New Cases Identified by Special Enquiry Units ... ..	153
17.	Reporting Requirements of Financial Institutions... ..	181
18.	Penalty Proceedings: Failure by an Individual or a Company to Make a Return of Income ... ..	190
19.	Suggested Scales of Defaults and Tariffs ... ..	201
20.	Level of Compliance in Making Returns and Payments of VAT ... ..	212
21.	Level of Compliance in Making Returns and Payments of PAYE... ..	212
22.	Cases on Hands of County Registrars/Sheriffs, 1981 and 1983 ... ..	217
23.	Remissions and Amounts Irrecoverable ... ..	232
24.	Details of the Numbers of Companies Cases which Went into Liquidation/Receivership, 1981 to 1984 ... ..	235
25.	Assessment Form for Comprehensive Direct Expenditure Tax ... ..	247
26.	Value-Added Tax Registration Thresholds for Small Businesses in EEC Countries, October, 1983 ... ..	267
27.	Details of the Total Customs Seizures (Excluding Cars) for 1983 ... ..	280

<i>Table</i>	<i>Title</i>	<i>Page</i>
28.	Prosecutions for Motor Tax Offences 1974-1983 .... ..	289
29.	Number of On-the-Spot Fine Notices Issued for Non-Display of Tax Discs ... ..	290
30.	Convictions for Motor Tax Offences, June to November, 1984 ... ..	290
31.	Share of Total Taxation in Gross Domestic Product in Ireland ... ..	293
32.	Possible Tax Structures under Proposed New System	295

**LIST OF TABLES**  
(in Appendices)

<i>Table</i>	<i>Title</i>	<i>Page</i>
5.1	Income Tax and Capital Gains Tax Penalties ... ..	321
5.2	Corporation Tax Penalties ... ..	323
5.3	Value-Added Tax Penalties ... ..	324
5.4	Criminal Penalties ... ..	326
6.1	Collection of VAT — Taxable Period March/April, 1982	332
6.2	Collection of VAT — Taxable Period March/April, 1983	332
6.3	Collection of VAT — Taxable Period March/April, 1984	332
7.1	Cost of Enforcement by County Registrars/Sheriffs Compared with Solicitor Enforcement, 1983/84 ... ..	335
8.1	Number and Proportion of Certificates Issued by the Collector General in Respect of the Main Taxes to Sheriffs and County Registrars, 1980 to 1984 ... ..	337
8.2	Revenue Collected by County Registrars/Sheriffs as a Proportion of the Face Value of Certificates, 1980 to 1984	338
12.1	Customs and Excise Offences and Penalties ... ..	356
13.1	Revenue Effects of our Proposals, 1983/84, assuming Single Tax Rate 35 per cent, Tax Credits £385/£770, Single VAT Rate 13.4 per cent ... ..	359
13.2	Revenue Effects of our Proposals, 1983/84, assuming Single Tax Rate 35 per cent, Tax Credits £508/£1,016, Single VAT Rate 16 per cent... ..	360
13.3	Revenue Effects of our Proposals, 1983/84, assuming Single Tax Rate 38 per cent, Tax Credits £550/£1,100, Single VAT Rate 13.4 per cent ... ..	361
13.4	Revenue Effects of our Proposals, 1983/84, assuming Single Tax Rate 40 per cent, Tax Credits £580/£1,160, Single VAT Rate 11.75 per cent ... ..	362
13.5	Estimates of Tax Base and Net Produce of Tax, 1983/84	363
13.6	Extension to Income Tax Base, 1983/84 ... ..	364

<i>Table</i>	<i>Title</i>	<i>Page</i>
13.7	Net Produce of Tax at 35 per cent on the Adjusted Tax Base, 1983/84 ... ..	366
13.8	Net Produce of Income Tax at Various Rates on the Adjusted Income Tax Base, 1983/84 ... ..	366
13.9	Adjusted Corporation Tax Base, 1983/84 ... ..	367
13.10	Adjusted Capital Gains Tax Base, 1983/84... ..	369
13.11	Adjusted Capital Acquisitions Tax Base, 1983 ... ..	369
13.12	Value-Added Tax Base, 1983 ... ..	370
13.13	Social Security Tax Base ... ..	371
13.14	Personal Allowances and Equivalent Tax Credits, 1983/84 ... ..	372
13.15	Revenue Yield from Recommendations in the Second Report ... ..	375

## PREFACE

1. This is our fifth and final report based on the results of our examination of the Irish tax system under the terms of reference given to us when we were established in March, 1980. These were

“To enquire generally into the present system of taxation and to recommend such changes as appear desirable and practicable so as to achieve an equitable incidence of taxation, due attention being paid to the need to encourage development of the national economy and to maintain an adequate revenue yield; and to provide interim reports on such matters as the Commission considers desirable or as may be referred to it by the Minister for Finance for specific consideration.”

2. The first four reports contain our proposals for a comprehensive reform of the tax structure. This report gives our recommendations on the administration of the tax system. We concentrate on the advantages of our simplified tax system but many of our recommendations on administration can be read in the context of any tax structure.

3. The report is divided into six parts. The principles which should underpin the administration of a good tax system and our general approach to tax administration are discussed in part one. In part two we give our views on the way income should be assessed to tax. Part three deals with tax avoidance and tax evasion. In part four we consider the powers of the Revenue Commissioners to examine and verify tax returns, to assess statutory penalties and to collect and enforce payment of tax. Part five discusses the administration of specific taxes. Finally, part six contains estimates of the revenue effects and the income distribution effects of the reforms proposed in this and earlier reports.

### Meetings of the Commission

4. The Commission has met formally on seventy five occasions over a period of eighty four days.

### Format

5. The format and style of our first four reports has been followed to a large extent. The use of the pronoun ‘he’ has been made in the same context as before, embracing both male and female.

## Consultations

6. In preparing this report we received specialist advice to supplement the work by the secretariat. Mr John Avery Jones gave us the benefit of his experience as a member of the Keith Committee on Enforcement Powers of Revenue Departments in the United Kingdom. Professor Cedric Sandford of the University of Bath undertook a critical review of the final draft of this report. We are very grateful to them for the valuable contribution they made to our work.
7. During the production of this report, the Office of the Revenue Commissioners, in particular, officers dealing with income tax, corporation tax, customs and excise duties and value-added tax, gave us considerable assistance. We also consulted with the Departments of the Environment, Finance, Justice, the Public Service and Industry, Trade, Commerce and Tourism, the Appeal Commissioners, the Comptroller and Auditor General, the Ombudsman, the Chief State Solicitor, the Director of Public Prosecutions, the County Registrars and the Dublin County Sheriff. Bodies such as the Confederation of Irish Industry, the Consultative Committee of Accountancy Bodies — Ireland, the Institute of Taxation, the Civil Service Executive Union, the Irish Customs Union, the Irish Institute of Credit Management and many specialists involved in the areas which we studied gave us most valuable help.
8. Dr Miriam Hederman O'Brien (Chairman), Mr Derek Chambers, Mr Patrick P. O'Neill of the Commission and Mr Séamus P. Reic and Ms Deirdre Dowdall of the secretariat visited the Internal Revenue Service in Washington D.C. to discuss aspects of tax administration in the United States, including self-assessment. Discussions were also held in Washington D.C. with officials of the Department of the Treasury, chartered accountants and tax experts from Arthur Andersen & Co, Ernst & Whinney and a director of the tax preparing firm H. & R. Block. In addition, meetings were held with Professor Harvey Galper of the Brookings Institute, Dr Joseph J. Minarik of the Urban Institute, Dr Vito Tanzi and members of the International Monetary Fund and a number of public representatives.
9. The Chairman visited the EEC Commission in Brussels to discuss aspects of customs and excise duties and value-added tax. Discussions were also held in London with officials of H.M. Inland Revenue.

## Acknowledgements

10. In producing this report we have again benefitted from the generous help given by individuals and organisations involved in the areas under review. Many experts, both in Ireland and elsewhere, gave freely of their time to help us clarify the issues and understand their implications. Our thanks are due to officials connected with income tax administration in

Washington D.C. and to the others we met there for their open and frank discussion of tax administration in the United States. We are also grateful to the Revenue Commissioners, the officials of the Department of Foreign Affairs and Mr Graham Williams, President of the Institute of Taxation, for their help in organising the visit to Washington D.C.

11. We have been impressed by the continuing co-operation we received from H.M. Inland Revenue and Customs and Excise since we began our work five years ago and it is hoped that a special mention of Mr John Isaac C.B., Deputy Chairman of the Board of Inland Revenue will be taken as a gesture not only to him but to his colleagues who were of great assistance on many occasions.
12. The Directors and staff of the Irish Offices of the European Community and of the European Parliament and their counterparts in Brussels have been consistently helpful whenever we needed them.
13. As this is our final report we feel it is appropriate to acknowledge the generous response we have had from many organisations and people to requests for information and ideas. Some wish to remain anonymous, others have already been mentioned. We would like to put on record that our work has benefitted greatly as a result of their contribution.
14. Throughout our work we maintained a dialogue with those responsible for the operation of the existing tax structure. We are very conscious of the problems with which the Revenue Commissioners have to contend. We are grateful for their co-operation under difficult circumstances over the years. We consider that we share a common aim in improving the tax system for both taxpayer and administrator. We believe that despite the inconvenience which change inevitably causes, our proposals would achieve this aim.
15. The Commission has been serviced by staff seconded from the Department of Finance and the Revenue Commissioners. We wish to underline our previous tributes to their ability, dedication and hard work. The Secretary for the first four reports, Dr Donal de Buitléir, made an outstanding contribution to the Commission. Dr de Buitléir was promoted to the rank of Superintending Inspector of Taxes in March, 1985. He resigned as Secretary to take up his new position. His successor, Séamus P. Reic, has taken over the role of Secretary for this final report and continued the impressive record which he established when acting as Assistant Secretary for the second, third and fourth reports. Deirdre Dowdall, who has acted as Assistant Secretary for this report and Kealin Ireland, who has been our liaison with many outside groups, have supplied an exceptionally high level of service. The other officers who have been with us during the past five years maintained an excellent standard of work. We would also like to pay

tribute to the valuable assistance of Clodagh Brady and Linda Bergin and their predecessors who coped with the many demands which the Commission's work made upon them. Kathleen Morrissey and the typists in the Department of Finance were most co-operative in dealing with requests for urgent help in processing our considerable needs for revisions and final drafts.

16. We have received favourable comments on the quality and layout of our reports. This is largely due to the skill of Mr Frank Butler of Cahill Printers Ltd, who were responsible for printing our work and we would like to acknowledge his help and experience.

### Criticism

17. Finally, we wish to acknowledge the contribution made to our work by those who have challenged our proposals. Some of our critics have mistaken the terms of reference which we were given and to which we have been faithful. Some have tried to draw us into the arena which properly belongs to the politicians. Some, again, have ignored our contention that a tax system must be considered in its entirety rather than only in isolated parts. Others have given us an opportunity to explain more fully the reasons which led to our proposals. All have made us reflect on the task we have undertaken.

18. It is right that those who advocate change should be called upon to defend their thesis. There must, however, eventually be an end to debate and a decision taken whether or not to reform the tax system.

## THE KEY ELEMENTS OF PROPOSED REFORMS

1. Administration is an essential part of any tax system. Deficiencies in tax administration may themselves thwart the design of the legislature and the objectives of the system. The measures proposed in our first four reports would simplify taxation but our work as a Commission must include a review of the machinery of tax administration to make it complete. The administration of a tax system also contributes to its fairness, efficiency and simplicity.

2. The administration of taxation in Ireland has virtually broken down. Non-compliance is a major problem. The situation will get worse unless the evident problems are tackled quickly and with determination. Radical measures are needed.

3. The first priority is an immediate programme of simplification of the tax code. The importance of such a programme cannot be overstressed. Without it, the system is in danger of rapid disintegration. The changes in the tax structure outlined in our first four reports show how the system could be simplified.

- The large number of allowances, special deductions and reliefs in the income tax code should be phased out and the range as well as the level of tax rates reduced accordingly until a single rate of tax applies to all income.
- Further progress towards a single rate of value-added tax should be made.

4. The key elements of the system of administration we propose are
- (i) self-assessment for all sources of personal and corporate income (which come within our definition of income) except wages and salaries. The system of self-assessment would replace the existing Revenue-assessment and would take out of the hands of the Revenue Commissioners and place upon taxpayers the responsibility for calculating and paying on time their tax liabilities,
  - (ii) the retention of a cumulative system of PAYE which, together with our proposals for simplified taxation, would ensure accurate

deduction of tax for the vast majority of wage and salary earners throughout the year,

- (iii) a more general system of deduction of tax at source on other types of income,
- (iv) an integrated collection and enforcement system operated by the Revenue Commissioners with statutory powers to levy the income or financial assets of a taxpayer and to seize goods to satisfy a tax debt, and
- (v) a new penalty code with powers to enable the Revenue Commissioners to assess and collect statutory penalties for tax offences, subject to a right of appeal.

5. These proposals are designed to improve the level of compliance, to free the resources of the Revenue Commissioners to deal with non-compliance where it exists and to impose effective sanctions when obligations or tax liabilities are not met. A cumulative PAYE system in the context of the proposals for simplified taxation in our first report would ensure accurate deduction of tax for the vast majority of taxpayers throughout the year. Self-assessment for non-PAYE income tax, corporation tax, capital gains tax and capital acquisitions tax would relieve much of the day-to-day burden of administration, allowing the Revenue Commissioners to concentrate more on identifying, auditing and settling complex or suspect cases. The streamlining of the appeals, offences and penalties systems would provide an effective penalty code. Finally, the new collection and enforcement procedures would ensure the efficient collection of the revenue by the Revenue Commissioners. Overall, the simplification of the tax structure proposed in earlier reports, together with the administrative changes we recommend in this report, would reduce greatly the risk of breakdown in tax administration and would improve administration in general.

### **The Scope of Tax Administration**

6. Taxation is a practical matter; the tax code has to work. Administration involves several stages: drafting clear legislation; interpreting and implementing this legislation; keeping taxpayers and administrators abreast of new legislation and interpretation; identifying taxpayers, their income and wealth and on that basis assessing their tax liabilities; providing machinery which allows collectors and taxpayers to agree on assessments; operating appeal procedures in cases of dispute; ensuring timely payment of established liabilities and imposing penalties when liabilities are not met. Review procedures are needed to ensure that the law and the practice remain in line with the original intention of the legislation.

7. This report deals with these administrative issues, while investigating whether a good tax code can be kept fair, efficient and equitable in practice. We have not examined the organisational structure of the Revenue Commissioners. However, we consider that there is a *prima facie* case for closer integration of VAT, employers' liability to remit PAYE and PRSI, tax on directors' remuneration and corporation tax in the case of limited companies and corresponding tax heads for self-employed persons.

### **Legislation and Revenue Practice**

8. Generally speaking, the public service is satisfied with the present legislative processes and the procedures for consultation with interested parties and sees no need for change. Others are dissatisfied. We believe that legislation which is passed after proper consultation is better than legislation introduced without it. Lack of consultation over the past few years has contributed to defects in legislation. In our view, the argument is not about whether there should be more consultation but rather the form it should take. We make recommendations designed to improve the legislative process.

9. Even with full consultation and perfect drafting there will be certain 'grey' areas. These require interpretations by the Revenue Commissioners and give rise to a code of practice. Present Revenue practice has several unsatisfactory aspects:

- (i) the powers of the Revenue Commissioners are unclear,
- (ii) all taxpayers are not treated alike,
- (iii) no information on Revenue practice is published, and
- (iv) there is no independent review procedure.

These defects must be rectified. Our recommendations in this area are set out in Chapter 3.

### **Tax Assessment**

10. The present system of Revenue-assessment is not working efficiently. Initial assessments on an estimated basis are generally excessive; final tax collected is only about one-quarter of the tax charged in the original assessments. These high estimates seem to be made to elicit information from taxpayers. While they may have this effect, they also lead to large numbers of undetermined liabilities which can run over several years. We do not believe that the 1983 changes in the appeal procedures will improve the situation. The changes which might make the system work satisfactorily include an extension of the due dates for payment of tax by the self-

employed or choosing an earlier basis of assessment. These solutions are undesirable on equity grounds.

11. We examined the tax system of other countries and found that self-assessment in various forms operates in many different countries including Canada, Japan, New Zealand and Sweden. However, the best known example of full self-assessment is the United States system. We studied the United States system in detail and a delegation from the Commission visited Washington D.C. to investigate the administration and operation of self-assessment.

12. We recommend that the existing system of Revenue-assessment be replaced by self-assessment. The Revenue Commissioners would continue to have the power to make estimated assessments but, over time, this would become the exception and not, as now, the normal rule. Under self-assessment, taxpayers would be required to complete an annual return and to calculate their own liability. To secure compliance, the new system would rely on audit of a small proportion of cases and penalties which are both specific and automatic. Self-assessment would relieve inspectors of much of the routine work associated with the present assessment and appeal procedures. Examination of cases could then proceed in a way in which the skills of inspectors of taxes would be directed away from purely arithmetical computations into areas where they are most likely to achieve results by correctly bringing more profits into assessment. We are satisfied that self-assessment on this basis offers a means of securing greater rather than less compliance on the part of taxpayers. An outline of the self-assessment system we recommend is set out in Chapter 4.

13. This system of self-assessment would cover all sources of personal and corporate income which come within our definition of income, including capital gains and capital acquisitions. However, wages and salaries would be excluded where they are the only or main source of income of the taxpayer. PAYE on a cumulative basis would continue to operate. This would ensure that most wage and salary earners would have their tax liability worked out in full by their employers during the tax year. Withholding taxes at the single rate would satisfy any additional liability to tax on other income, such as deposit interest. Only those PAYE taxpayers with significant other untaxed income or more complex financial affairs would have to submit a self-assessment return. Gifts and inheritances received by PAYE taxpayers could be either self-assessed or directly assessed by the Revenue Commissioners.

14. Self-employed taxpayers and companies already have to comply with many of the requirements of self-assessment. The most important element of self-assessment incorporated in present administration of income tax and corporation tax is the onus placed on the taxpayer in appeal cases to specify

an amount of tax which he considers to be due. However, to facilitate the introduction of the new system and to give taxpayers and the Revenue Commissioners familiarity and confidence with self-assessment, we recommend in the first instance that it be introduced for corporation tax. Compliance for corporation tax is higher and a greater proportion of corporate taxpayers employs specialist tax advisers. Also, companies are already taxed on the basis of income arising in an accounting period and the complexities of different bases of assessment do not arise.

### Withholding Taxes

15. PAYE is the most important withholding tax in Ireland. Other withholding taxes in operation include tax credits on company distributions, deductions of tax from interest such as building society deposits and land bond interest and deduction of tax from payments to sub-contractors.

16. Deduction of tax at source can have many advantages. It reduces official administrative costs and the compliance costs of taxpayers. Withholding also curbs evasion. The more that people are liable at a single rate, the more will withholding at the single rate turn out to be an accurate assessment of liability. Thus, withholding becomes even more attractive to operate under the system of taxation we have proposed. It is particularly effective when operated in conjunction with a system of self-assessment because there is a greater tendency to declare income which has suffered tax and tax at the single rate would already have been paid.

17. We consider that deduction of tax at source should be extended as much as possible. We examine some existing schemes of deduction of tax at source (other than PAYE which is dealt with in Chapter 6) and we consider areas to which the system might be extended. Our recommendations are given in Chapter 5.

18. In our first report we recommended that the income from all interest-bearing deposits should be charged to tax to the extent only that the rate at which it accrues exceeds the rate of inflation during the period of accrual. In this report we consider how to implement this recommendation within a scheme of deduction of tax at source.

### Assessment under PAYE

19. In recent years the PAYE system, which seeks to withhold the correct tax due from an employee's income during the course of the tax year, has become more complicated. The operation of PAYE on a cumulative basis has run into so many problems under the existing tax code that it has lost many of the advantages over a non-cumulative system. The number of reviews imposes high costs on the Revenue Commissioners and employers,

there are delays and taxpayers get poor service. If this situation were to continue, we would recommend a change to a non-cumulative PAYE system and a final settlement after the end of the tax year. However, many of the complicating factors of the present code would disappear with the adoption of our previous recommendations on income taxation. In the context of the general scheme of taxation in our first report, we recommend that the present cumulative system should be retained. However, if our proposals are not adopted, the case is more finely balanced and we would recommend that the Revenue Commissioners should review and publish the arguments for and against a change to a non-cumulative system of PAYE.

### **Tax Appeals**

20. We have some recommendations to make on the appeal system but, generally, we feel that the present arrangements would work much better, given our other proposals on taxation and assessment. In particular, self-assessment would relieve much of the burden on the appeal machinery. As a result there would be more time to consider technical cases of interpretation of the law and to adjudicate in cases where there is a genuine dispute about the amounts of income assessed to tax.

### **Compliance Costs and Taxpayer Assistance**

21. Compliance costs are the amounts of money, time and effort imposed on the private sector in meeting its obligations under the tax code. Compliance costs may be borne by the taxpayer and/or by a third party acting as collector of the tax. We believe that there are good reasons for tipping the balance away from private compliance costs towards official administrative costs.

- Firstly, administrative costs are met from taxation, which can itself be determined with reference to fairness of the tax burden, whereas compliance costs fall on the private individual and may be distributed inequitably.
- Secondly, compliance costs are resented by taxpayers, particularly when they are incurred to show little or no liability to tax.
- Thirdly, it is much easier to ascertain the level of administrative costs than private compliance costs. If the former rises, there will be greater pressure on legislators and administrators to eliminate unnecessary work and to keep procedures as simple as possible.

22. Nonetheless, the most efficient way to collect VAT and PAYE is to use the private sector as an agent of the Revenue Commissioners. We do not favour compensation payments to offset compliance costs but the Revenue Commissioners have a responsibility to reduce compliance costs as much as possible. This should be done by simplifying the tax system,

providing adequate information to traders and improving forms and procedures. This would benefit both the public and private sectors.

23. The recommendations in our first four reports involve a considerable simplification of the tax system. This would reduce significantly the compliance costs of taxpayers, employers and VAT-registered traders. The improvements in tax administration, recommended in this report, would also contribute to a lessening in the burdens on the private sector. However, self-assessment could give rise to greater compliance costs for the small proportion of self-assessed taxpayers selected for investigation but overall compliance and administrative costs for self-assessed taxpayers would be reduced. The compliance expenses of PAYE taxpayers would be reduced to a minimum.

24. General assistance to taxpayers is usually provided in response to telephone calls, personal visits to tax offices and written enquiries. We make recommendations to improve the service to taxpayers.

### **Tax Evasion**

25. We share the public concern with tax evasion and we note the perception that it is widespread and increasing. It is difficult to gauge the exact extent of tax evasion but we are convinced by a number of partial indicators that it results in serious revenue losses. The evidence of the Revenue Commissioners shows it to be a problem in some areas. There is a clear need to increase the probability of detection.

26. The Revenue Commissioners have two methods of curbing evasion. The first is to use to the best advantage, in the routine examination of cases, all the information already in their possession. The second is to increase the proportion of their resources applied to investigative work and to deploy this as effectively as possible.

27. It seems to us that too great a proportion of the resources of the Revenue Commissioners is being devoted to the routine processing of the cases of those taxpayers who are generally compliant. Hence, too little attention can be devoted to persistent defaulters. A simplified tax code and self-assessment would help here. They would free resources and allow greater attention to be paid to critical examination of the affairs of a relatively small number of taxpayers. These critical examinations should be on an integrated basis, taking account of all aspects of a taxpayer's affairs, including PAYE and VAT liability. Improved audit arrangements, together with an extension of the powers of the Revenue Commissioners to get information and to visit premises, could increase the detection of evasion and hence control it more effectively. The new system of penalties and the streamlining of the procedures for imposing penalties proposed in Chapter 13 would ensure that effective sanctions are automatically imposed.

We are satisfied that these measures would lead to higher levels of detection and compliance.

28. We believe that it is in the public interest to establish the degree to which tax evasion is detectable and to measure it more accurately. This could be done along the lines of the Taxpayer Compliance Measurement Programme in the United States.

### **Tax Avoidance**

29. There are many views of what constitutes tax avoidance. For example, it is possible to reduce or remove tax liability by choosing among perfectly acceptable tax reliefs and incentives or even by refraining from consuming a taxed product. However, for purposes of this report we define avoidance as the minimisation of tax liability through taking advantage of some provision or lack of provision in the law, in circumstances other than those perceived to be intended by the legislature. We distinguish between tax avoidance and tax evasion. Since tax avoidance is taking advantage of opportunities provided by the law, it excludes fraud, concealment of income or other illegal measures which constitute tax evasion.

30. The present tax system creates the ideal environment for tax avoidance. This situation is likely to remain as long as marginal tax rates in Ireland are very high and taxes vary on different forms of income. Much simpler and comprehensive taxation seems the most obvious and effective solution. We have already made proposals along these lines. Piecemeal attempts to deal with tax avoidance are likely to end up merely as skirmishes between taxpayers, legislators and the Revenue Commissioners.

31. Nonetheless, even with simpler taxation, there will still be some scope for tax avoidance, albeit on a much smaller scale. General anti-avoidance provisions are very difficult to apply in practice and they give rise to great uncertainty. Furthermore, since avoidance is, by definition, compliance with the law, a general anti-avoidance provision would be in conflict with the general tax law. In the context of the system of taxation proposed in our first four reports we consider that appropriate specific provisions are the best means of dealing with tax avoidance.

### **Information Powers of the Revenue Commissioners**

32. The granting of powers to the Revenue Commissioners to compel individuals to supply information, either concerning their own affairs or the affairs of other taxpayers, results inevitably in taxpayers being put to inconvenience, trouble and expense. Therefore, any requirement to supply information should relate only to that which is strictly necessary to ascertain true liability. The information provided should be both useful and used. Otherwise it should not be sought. Regard should be had to the costs of supplying the information and a reasonable balance struck between these costs and the utility of the information to the Revenue Commissioners.

33. We see no merit in having draconian provisions on the statute book which are used rarely, if ever. Any powers given to the Revenue Commissioners should be operated and the Revenue Commissioners should be accountable for their use. Wide-ranging powers should not be provided on the grounds that they will be used only in a small number of serious cases unless the legislation specifically limits their use to such cases.

34. There are many inconsistencies between the powers available for different taxes and the obligations laid upon different sectors. There is a need for a review. We examine the existing powers of the Revenue Commissioners and we make some recommendations for change. We recommend that the powers of the Revenue Commissioners to visit traders' premises to verify tax returns should be harmonised over the direct taxes and VAT. We do not recommend any significant increase in the powers of the Revenue Commissioners but, in some instances, we envisage that the present powers should be more widely used. Any increase in powers should be matched by additional safeguards for the taxpayer. The aim of our proposals is to achieve a correct balance between the interests of the individual and the Exchequer and to improve the fairness and efficiency of tax administration.

### **Tax Offences and Penalties**

35. The main object of the system of taxation is to raise revenue. Accordingly, the effective, efficient and timely collection of that revenue is extremely important. Any delay in the payment of tax should therefore give rise to an interest charge on a commercial basis. Interest on late payment of tax liability should be treated separately from any penalty for non-compliance.

36. In principle, we favour the use of civil penalties rather than criminal sanctions for tax offences. Criminal sanctions should be reserved for the most serious cases of evasion involving fraud. We recommend civil penalties for a new range of tax offences, with clearer distinction between the minor inadvertent offences and serious cases of tax evasion. Our proposals also limit the scope of the Revenue Commissioners to mitigate penalties. Mitigation of penalties would continue in cases involving civil fraud in recognition of the degree of co-operation by the taxpayer. This would preserve the basis for negotiated settlements in such cases. The Revenue Commissioners should continue to have a general power to mitigate penalties at the collection stage but this should be confined to exceptional cases.

37. At present, penalties cannot be imposed by the Revenue Commissioners; they can be imposed only in proceedings before a court. In practice, however, most penalties relating to incorrect returns are collected following a settlement by agreement with the Revenue Commissioners. We believe that the Revenue Commissioners should be given the power to assess and collect statutory penalties, subject to a right of appeal.

38. Finally, we recommend that the names of tax evaders liable to penalties should be published, irrespective of whether the penalties are formally imposed or included as part of a negotiated settlement. The names of defaulters who, on their own initiative, make a voluntary disclosure of past defaults should not be published.

### Collection and Enforcement of Payment

39. Collection of the main taxes is centralised under the Collector-General. Collection activity involves issuing postal demands to taxpayers which are followed up by further postal demands until a stage is reached when the tax debt is passed to the county registrar/sheriff for enforcement. In recent years, the enforcement agencies, especially the county registrars, have been unable to cope with the volume of Revenue enforcement work. Court proceedings are initiated in only a small number of cases for the recovery of outstanding taxes and there is relatively little scope to extend the use of court proceedings.

40. The failure to collect revenue is a major defect of our tax system. Non-compliance in making returns and payments, especially VAT and PAYE/PRSI, is putting a severe strain on the collection and enforcement procedures to a point where there is near breakdown of the system. This in turn encourages further non-compliance because traders are put at a competitive disadvantage if they pay their taxes while others ignore the demands of the Collector General.

41. We recommend that the Revenue Commissioners should be directly responsible for all aspects of collection of tax and enforcement of payment. They should set up a formal and integrated system to collect and enforce revenue debts. The county registrars should be relieved of the responsibility for collection of revenue debts other than those resulting from court judgements.

42. The power of distraint is necessary to enable the Revenue Commissioners to maintain effective enforcement of payment but essentially it is a course of last resort. Other powers and changes in the collection procedures are necessary to establish an efficient and effective collection system.

43. We believe that local action would be much more effective in securing payment and in selecting cases for further enforcement action where taxes remain unpaid. Collection and enforcement systems based largely on postal demands are ineffective. A telephone call or a personal call from a local office can be more effective in securing payment than an anonymous computer demand. Traders respond to those creditors who exert most pressure. In many cases, reluctance rather than inability to pay is at the

root of non-compliance and a personal approach by a collector before enforcement proceedings are taken would be more successful, provided it is backed up with adequate enforcement powers. In addition, a local collection system would be in a position to communicate directly with the inspectors responsible for assessment of tax and would be more aware of the circumstances of the defaulting taxpayer. We, therefore, recommend that certain collection functions be decentralised. There is a number of ways in which decentralisation could be organised. The precise details of the organisation at local level is a matter for the Revenue Commissioners.

44. In the United States, the main collection activity involves the use of a levy on a defaulter's income or bank account. Under the levy procedure, the Internal Revenue Service may take all but a very small amount of a taxpayer's net income to meet his tax liability. Alternatively, they may require a bank to hand over the full balance on an account. The tracing of bank accounts is facilitated by a requirement that taxpayers list all bank accounts on their income tax return. Generally, court authorisation is not required but three legal requirements must be satisfied before levy action can be taken:

- (i) the tax must be owed,
- (ii) a notice and demand for payment must have been sent to the taxpayer's last known address, and
- (iii) if payment is not made, a notice of intent to levy must be given at least ten days in advance.

If collection is in jeopardy, the ten day waiting period and the notice of intent to levy are not required. While the use of this levy is controversial, it has not been successfully challenged in the courts.

45. We believe that this type of levy is the only effective answer to the problems of collecting outstanding taxes. The vast majority of taxpayers pays tax by deduction at source under PAYE. This ensures a high level of compliance. It also creates a demand for and lends support to revenue enforcement efforts in other sectors. Much of the tax outstanding has already been taken in the form of VAT and PAYE from other taxpayers. It is unacceptable that this should be used to finance the business or spending of those who hold it on behalf of the state. We recommend that the Revenue Commissioners be given the power to levy the income or financial assets of a taxpayer to satisfy a tax liability.

### Special Collection Arrangements

46. We have also examined a number of special collection arrangements to deal with difficult collection cases or to recover outstanding tax in certain situations. Our recommendations are set out in Chapter 16.

47. Section 285 of the Companies Act, 1963 puts the Revenue Commissioners in a favourable position in the event of receivership or liquidation of a company. In general, the Revenue Commissioners are preferential creditors in respect of one year's tax. This provision is criticised on the basis that it puts other less well informed creditors, particularly smaller creditors, at a disadvantage. We recommend that the preferential position of the Revenue Commissioners be abolished in relation to assessed income tax, corporation tax and capital gains tax. The preference of the local authorities in relation to rates and motor vehicle duties should also be removed.

48. Different considerations arise in relation to PAYE, employees' PRSI contributions, value-added tax and excise duties. In these cases, the Revenue Commissioners' claim is for money collected by the debtor as an agent rather than his liability as a taxpayer. Unless some measure of priority were accorded in these cases, taxes due would go to swell the insolvent's estate to the advantage of the general body of creditors. We do not think it right that statutory provisions enacted for the more convenient collection of the revenue should accrue to the benefit of private creditors. In these circumstances we believe that the retention of a measure of Revenue preference is justified. Our recommendations are given in Chapter 16.

#### **Administration of Direct Expenditure Tax**

49. Because this tax would be new to Ireland, we wanted to satisfy ourselves that the proposal was practicable so we dealt with a great many of the administrative issues in our first report. However, now that we are making recommendations on the administration of taxation, it is easier to see how the operation of the direct expenditure tax would fit into the general system.

50. Our proposals for the reform of the Irish tax system are designed to be implemented in three phases. The introduction of a direct expenditure tax is the final element in phase three. The existing income tax system needs to be greatly simplified before the direct expenditure tax stage is reached. In this report we amplify the guidelines for the administration of a direct expenditure tax set out in our first report.

51. Following the publication of the first report, there were criticisms that the proposal to introduce a progressive expenditure tax for a relatively small number of taxpayers at the top of the scale was impracticable on administrative grounds. We remain convinced that a progressive expenditure tax is desirable and feasible. The problems of transition may be solved in different ways.

#### **Value-Added Tax**

52. In our third report we examined the structure of VAT in detail. Many of our recommendations would have an impact on the administration of VAT. Here we examine a number of administrative issues:

- (i) the determination and settlement of VAT liabilities, including the appropriate taxable period,
- (ii) VAT on imports,
- (iii) registration for VAT, and
- (iv) VAT on second-hand goods.

Our recommendations are given in Chapter 18.

#### **Customs and Excise Duties**

53. Customs is now largely a European Community tax over which Ireland has little independent control. Excise duties were reviewed in our third report. Our discussion of these duties in this report is confined to some general issues of administration.

54. The administration of customs and excise duties is quite different from any other area of tax. The questions of assessment, collection and appeals arise in a different way to direct tax and there is a high degree of physical control. Much of the legislation and procedures which govern the administration of customs and excise duties is old and is not available in a consolidated form as in the case of income tax and value-added tax. We recommend that a review of legislation be undertaken in this area to update, simplify and consolidate the law.

55. We review the enforcement powers of the customs and excise authorities, in particular the power of seizure. We conclude that this power is necessary but should be operated under strict guidelines which are made known to the public. We also review customs clearance procedures. Such procedures may cause delays and increase costs for business. We conclude that there is a need for some rationalisation of the existing arrangements for checking and clearing goods. Computerisation of customs procedures would help to improve efficiency.

#### **Motor Vehicle Duties**

56. Motor vehicle duties are administered by local authorities and collected at twenty nine local offices throughout the country. Both the cost of administration and the level of evasion are high. In our third report we

made recommendations for the simplification of these duties. Such a simplification would reduce administrative costs and enable motor vehicle duties to be collected on an agency basis without the need for so many local offices. We consider a number of proposals and conclude that An Post is best suited to undertake this work.

57. We believe that there is a case for effective action to deal with the high level of evasion of these duties. We consider imposing a penalty of seizure of the vehicle in certain cases and the prescribing of statutory minimum penalties for all offences.

### **Re-Structuring the Tax System**

58. Finally, we draw together the implications of our proposals for the structure of taxation and give our view on the considerations which arise in allocating the overall burden of taxation between various taxes. We also set out the estimated revenue effects of the reforms we have proposed in this report and our earlier reports and we comment on certain aspects of the income distribution effects.

### **Conclusion**

59. In summary, the key elements in our proposals in this report are
- (i) self-assessment for non-PAYE income tax, corporation tax, capital gains and capital acquisitions tax should be introduced as quickly as possible,
  - (ii) the retention of a cumulative system of PAYE which, together with our proposals for simplified taxation, would ensure accurate deduction of tax for the vast majority of wage and salary earners throughout the year,
  - (iii) a more general system of deduction of tax at source on other types of income,
  - (iv) an integrated collection and enforcement system operated by the Revenue Commissioners with statutory powers to levy the income or financial assets of a taxpayer and to seize goods to satisfy a tax debt, and
  - (v) a new penalty code with powers to enable the Revenue Commissioners to assess and collect statutory penalties for tax offences, subject to a right of appeal.

## **LIST OF RECOMMENDATIONS**

### **Chapter 2: The Legislative Process**

1. Draft legislation on taxation should be published in advance to the greatest extent possible to allow more time for public evaluation of proposals.
2. A Standing Joint Oireachtas Committee on Fiscal Affairs should be established. This committee should deal with the committee stage of the finance bill and other fiscal matters and have powers to send for papers and records, hear witnesses and report the bill to the Dáil, with or without amendments.
3. A technical advisory committee representative of the main professional bodies in the taxation area should be established to assist the Revenue Commissioners and the Department of Finance in identifying aspects of taxation law and administration which need to be improved.
4. Temporary transfers of staff at middle-management level between the Office of the Revenue Commissioners and the Department of Finance should be instituted on a systematic basis.
5. Statutory consolidation of tax legislation should take place at regular intervals.

### **Chapter 3: Revenue Practice**

6. Revenue interpretations and rulings should be published regularly.
7. There should be no general extension of advance rulings by the Revenue Commissioners on the proposed treatment of particular situations.
8. The present range of extra-statutory concessions should be incorporated into legislation as far as possible. Where this cannot be done, it should be published at regular intervals in the form of practice notes.
9. It should be within the terms of reference of the Joint Oireachtas Committee on Fiscal Affairs, which we recommend in Chapter 2, to oversee and review Revenue practice and to ensure that it is properly published and consistently and fairly applied.

10. Given the size of the expenses' deductions allowed to members of the Oireachtas, these deductions should be allowed by the Revenue Commissioners on an individual basis subject to the rules applicable to other taxpayers.

11. The functions of the Minister for Finance in relation to determining the allowable expenses of the Judiciary for tax purposes should be transferred to the Revenue Commissioners.

#### **Chapter 4: Assessment Procedures**

12. Self-assessment should be introduced for non-PAYE income tax, corporation tax and all other direct-assessment cases. It should be introduced for corporation tax in the first instance.

13. The introduction of self-assessment for income tax purposes would be facilitated if tax for the current year were charged on the basis of the income of the accounting period ending in that year.

14. Self-assessed taxpayers should make three provisional payments of tax at four monthly intervals during the tax year. Interest at commercial rates should run from these dates on any underpayment found ultimately to be due. The balance of tax together with any interest due should be remitted with the tax return on the due date for the tax return. To avoid interest charges in every case, a *de minimis* provision or a tolerance factor should be built into the legislation.

15. There should be a requirement for self-assessment returns for companies, including supporting accounts, to be submitted within six months of the end of the relevant accounting year. Trading taxpayers should be required to submit self-assessed returns within nine months of the end of the relevant accounting year or within three months of the end of the tax year, whichever is the later. Non-trading taxpayers should be required, under a system of self-assessment, to submit their tax returns within three months of the end of the tax year.

16. There should be an automatic late filing penalty for returns not received by the new revised filing dates related to the amount of unpaid tax due and to the delay. There should also be a simple and automatic penalty for not making a return.

#### **Chapter 5: Withholding Taxes**

17. In principle, deduction of tax at source should be extended as much as possible.

18. Interest payable to Irish residents on all new government securities should be payable under deduction of tax once these securities have been made chargeable assets for capital gains tax purposes.

19. Inflation adjustment for tax purposes on all interest-bearing deposits by Irish residents with financial institutions should be made on an aggregate basis.

20. The existing construction industry scheme should be retained, subject to a right of appeal to the Appeal Commissioners and the courts against a refusal by the Revenue Commissioners to issue a certificate of exemption from deduction of tax for payments made under construction contracts.

21. The rate of deduction of tax from payments under construction contracts should be tied to the standard rate.

22. The extension to other areas of schemes of deduction of tax which meet the criteria set down in paragraph 5.43 should be kept under review.

#### **Chapter 6: PAYE**

23. In the context of the general scheme of taxation in our first report, the present cumulative system should be retained. However, if our proposals are not adopted, the case is more finely balanced and the Revenue Commissioners should review and publish the arguments for and against a change to a non-cumulative system of PAYE.

#### **Chapter 7: Tax Appeals**

24. Appointments as Appeal Commissioners should be made following an open public competition held by the Civil Service Commission.

25. Sufficient staff, including, if necessary, an additional Commissioner, should be appointed to enable the Commissioners to carry out their functions in a satisfactory manner.

26. The requirement to express dissatisfaction immediately after the determination of an appeal by the Appeal Commissioners or the Circuit Court Judge should be abolished. Any request made within twenty one days for the statement of a case for the High Court should be allowed.

27. Appeals to the High Court and the Supreme Court should be held *in camera*.

28. An inspector of taxes should be required to list a case for hearing before the Appeal Commissioners within three months of receiving a notice

from a taxpayer requiring him to do so. A similar provision should apply in cases of claims to relief by PAYE taxpayers.

### **Chapter 8: Compliance Costs and Taxpayer Assistance**

29. Every effort should be made to reduce compliance costs by simplifying the tax system, tax forms and procedures.

30. When devising forms, the Revenue Commissioners should take account of the needs of traders by presenting forms in a clear manner.

31. A range of specialist publications should be produced for small traders and people starting new businesses and for the classroom to prepare students for their tax responsibilities and to encourage voluntary compliance. These publications should be produced by expert writers, subject to the approval of the Revenue Commissioners.

32. The scope for accepting PAYE and VAT returns and other information in a computerised form should be extended and the obligations on traders to maintain supporting records, such as invoices, should be satisfied by records held in new forms, such as micro film.

33. A Central Enquiry Office (CEO) should be set up in Dublin. In the light of the experience of the operation of a CEO in Dublin, consideration should be given to opening similar offices in other large centres of population where the volume of demand would appear to justify such a course.

34. A 'freefone' system should be set up to enable taxpayers to contact the Revenue Commissioners from anywhere in the country for the price of a local call.

### **Chapter 10: Tax Evasion**

35. The Revenue Commissioners should undertake, as a matter of urgency, a valid statistical survey on the lines of the Taxpayer Compliance Measurement Programme in the United States to ascertain the level of detectable tax evasion and the characteristics of tax evaders. The results of this survey should be published.

36. The Revenue Commissioners should consider reorganising their structures to ensure closer integration of VAT, employers' PAYE and PRSI, taxation of directors' remuneration, capital gains tax and corporation tax in the case of limited companies and the corresponding tax heads in the case of self-employed persons.

### **Chapter 11: Tax Avoidance**

37. The system of taxation should be simplified as quickly and as widely as possible in line with our previous proposals. Simplified taxation is the best way to remove the conditions conducive to widespread tax avoidance.

38. In the context of the general system of taxation proposed in our earlier reports, tax avoidance should be dealt with by the enactment of appropriate specific provisions.

39. Anti-avoidance legislation should not apply before the date when the intention to legislate was announced.

### **Chapter 12: Information Powers of the Revenue Commissioners**

40. There should be a single power of entry to business premises, on notice, to ensure that returns are made for all businesses and to check the accuracy of returns of VAT, PAYE/PRSI and trading profits. All inspectors of taxes should be authorised to exercise this power.

41. A booklet setting out the rights and duties of traders should be prepared by the Revenue Commissioners and issued to all traders. The booklet should be re-issued before a checking visit begins.

42. The power to search premises should be available under warrant issued by a District Justice where there is reasonable ground for suspecting that an offence of fraud in relation to tax has been committed and where there is reasonable ground for suspecting that evidence of that offence is to be found on specified premises (whether or not the offence was committed there).

43. The existing VAT power to search premises should be brought into line with recommendation 42 above.

44. An officer of the Revenue Commissioners acting under the authority of a search warrant should have power to search persons whom there is reasonable cause to believe are in possession of evidence of an offence of fraud in relation to VAT or the direct taxes. The person executing the search warrant should also be empowered to take with him such other persons as appear to him to be necessary.

45. The powers of the Revenue Commissioners to seek independent information about a taxpayer's accounts and returns from his business suppliers and business customers, by virtue of Section 21 of the Finance Act, 1979, should be retained.

46. There should be an appropriate criminal penalty for any person who conceals, exports or destroys documents which are subject to a production notice.
47. Information regarding specific anti-avoidance transactions and connected operations should be required to be notified to the Revenue Commissioners on a current basis rather than retrospectively over long periods. Such obligations should be enacted in each situation when they are required. There should be substantial penalties for failure to comply. We do not favour a general power to enable the Revenue Commissioners to seek information about anti-avoidance.
48. All financial institutions, including building societies, should be subject to the same reporting requirements.
49. The automatic reporting limit for interest paid by financial institutions should be raised substantially. This should be done when interest paid by such institutions is subject to withholding tax on the basis recommended in Chapter 5. For the purposes of the return, an institution should aggregate all the accounts held by a single individual with that institution.
50. Insurance companies should be obliged to furnish information returns to the Revenue Commissioners in relation to certain policies.
51. The Revenue Commissioners should explore with information reporters improved means of matching information with taxpayers' files. In particular, the possibilities of requiring taxpayers to advise information reporters of their Revenue and Social Insurance number or the Revenue Commissioners supplying such information to the institutions appear desirable and should be investigated.
52. Any person or body who makes general information returns to the Revenue Commissioners concerning a taxpayer should be obliged to inform the taxpayer of the information reported.
53. The costs of complying with specific, as opposed to general, requests for information about the affairs of other taxpayers should be borne by the Revenue Commissioners where they are shown to be material.
54. Since international conventions for exchange of information provide that the Revenue Commissioners may refuse to make available information if to do so would, in their opinion, involve disclosure of an industrial, commercial or professional secret, they should be required to notify the taxpayer of a request for information. He should then have the opportunity to object to disclosure on the grounds that the information is commercially secret, with any dispute being adjudicated by the Appeal Commissioners.

55. The period of retention of business records for income tax, corporation tax, value-added tax and PAYE/PRSI should remain at six years. When the change to a system of self-assessment for all business recommended in Chapter 4 is made, the general time limit for assessments and repayment claims should be reduced to six years.

### Chapter 13: Tax Offences and Penalties

56. The Revenue Commissioners should be given power to assess and collect statutory penalties in the same way as tax, subject to a right of appeal by the taxpayer.
57. Details of all penalties and negotiated settlements should be published. The names of defaulters who, on their own initiative, make a voluntary disclosure of past defaults, should not be published.

### Chapter 14: A New Scheme of Offences and Penalties

58. Tax paid as a result of an understatement or undercharge should attract interest at a commercial rate for the period of the delay.
59. The existing scale of defaults should be abolished and replaced with three new categories:
- (i) civil fraud,
  - (ii) substantial misdeclarations, and
  - (iii) marginal errors or omissions.
60. The new code of offences might attract penalties of the following order:
- Civil Fraud:** 50 per cent of the evaded tax mitigable down to 30 per cent of the tax due for co-operation in the investigation. The minimum penalty should not be less than 30 per cent of the evaded tax.
- Substantial Misdeclaration:** 25 per cent of the tax lost. However, a default should not give rise to a penalty if there is a reasonable cause for the default or the taxpayer on his own initiative provides full information about the understatement.
- Marginal Cases:** There should be no penalty for minor errors or omissions. However, the more serious instances of these offences could be considered under the civil fraud provisions where they had been committed with an intent to deceive.
61. A system of surcharges should be introduced to deal with failure to submit PAYE and VAT returns or pay the tax due. The system would involve

- (i) a warning to any trader who failed to submit by the required dates two returns or payments within any period of one year,
  - (ii) an initial surcharge of 5 per cent of the tax due or £50, whichever is the greater, for the first default in the year following the issue of the warning,
  - (iii) an increased surcharge, rising in steps of 5 per cent for repeated failures to submit timely returns during the surcharge period.
  - (iv) late returns during the surcharge period would also extend the time during which the trader would be liable to surcharge, and
  - (v) liability to surcharge would only lapse after a period of one year's satisfactory compliance.
62. The penalty in respect of failure to notify chargeability to tax should be related to the amount of the tax unpaid in respect of each separate obligation.
63. The civil penalties should be imposed administratively but would be subject to appeal.
64. There should be a right of appeal to the Appeal Commissioners in respect of penalties and surcharges. The Appeal Commissioners should have powers to
- (i) mitigate the penalties, within the limits set out in recommendation 61 above, in cases of civil fraud,
  - (ii) waive the penalty for substantial misdeclaration but not to mitigate the penalty, and
  - (iii) determine the underpayment and the period of delay giving rise to interest charges but not to mitigate interest.
65. The Revenue Commissioners should continue to have a general power to mitigate penalties at the collection stage but the use of the power should be restricted to exceptional cases. The Revenue Commissioners should be required to report to the Comptroller and Auditor General upon the use made of mitigation.
66. There should be a set of specific criminal offences of dishonesty in respect of direct taxes and value-added tax. The criminal sanction should only apply where certain things are done or not done with an intent to deceive.
67. The Revenue Commissioners should explore with the Garda authorities the possibility of setting up a unit within the Fraud Squad to deal with criminal tax offences.

## Chapter 15: Collection and Enforcement of Payment

68. The Revenue Commissioners should be responsible for all aspects of collection and enforcement of tax. They should set up a formal and integrated system to carry out the enforcement of revenue debts. This would involve

- (i) the decentralisation of certain collection functions,
- (ii) greater use of legal action in local areas to enforce payment through the courts, and
- (iii) the appointment of local collectors on a full-time established basis with powers to seize goods.

69. County registrars should be relieved of the responsibility for collection of revenue debts other than those resulting from court judgements.

70. The Revenue Commissioners should be empowered to levy the income or financial assets of a taxpayer to satisfy a tax liability.

71. The doubts concerning Section 480 of the Income Tax Act, 1967 should be resolved without delay, either by further legislation or otherwise, so as to ensure that the Collector General has power to distrain and that other officers may distrain at his discretion on his behalf.

72. The power of seizure should be extended to enable the Revenue Commissioners and sheriffs to take 'walking possession' of goods.

73. The possibility of extending the power of distraint to real property, subject to court authorisation, should be examined.

74. The requirement that a *nulla bona* certificate must be returned by the sheriff before a judgement mortgage can be registered against a defaulter or before legal proceedings to petition for liquidation or bankruptcy can be initiated should be abolished as recommended by the Committee on Court Practice and Procedure.

75. The limits on Revenue debts which may be pursued in the lower courts should be increased substantially.

76. Collection of tax on gifts and inheritances should be the responsibility of the Collector General.

## Chapter 16: Special Collection Arrangements

77. The Public Accounts Committee should review the procedures to clear arrears of tax by instalments.

78. The Revenue Commissioners should have a general power to mitigate interest. The use of the power should be restricted to exceptional cases and the Comptroller and Auditor General should review the use made of mitigation in these cases.

79. In relation to PAYE, employees' PRSI contributions, value-added tax and excise duties, a measure of preference should be retained. In general, the period of preference should be twelve months. However, where returns have been made but the liabilities shown have not been discharged, the period of preference in relation to the established tax debt should be limited to three months.

80. The preferential position of the Revenue Commissioners in cases of insolvency should be abolished in relation to assessed income tax, corporation tax and capital gains tax. The preference of the local authorities in relation to rates and motor vehicle duties should also be removed.

81. The preferential position of the Revenue Commissioners in relation to interest on preferential tax debts should be abolished.

82. Consideration should be given to the possibility of requiring preparers of accounts to identify in financial statements amounts overdue in respect of these preferred debts.

83. Where the directors of a company which went into liquidation owing tax debts again set up business in any capacity, they should be obliged to notify the Revenue Commissioners.

84. The Revenue Commissioners should have power to request security for PAYE, employees' PRSI contributions and VAT payments where the promoters of a company/business which went into liquidation without discharging tax liabilities again set up in business. If satisfactory security is not given, it should be an offence to continue trading.

85. The Appeal Commissioners and the courts should have the power, on appeal, to waive any requirement for the provision of security if there is no culpability.

#### **Chapter 18: Administration of Value-Added Tax**

86. There should be no change in the length of the VAT accounting period or the timing of VAT payments.

87. VAT should continue to be charged on imports at the point of entry, subject to recommendations 88 and 89 below.

88. Firms primarily involved in manufacturing for export should continue to be allowed to import raw materials and components without payment of VAT. There should be no relaxation of the 75 per cent exporting condition.

89. The waiver of VAT on imports of up to £200 by registered traders should be retained but the operation of the scheme should be subject to regular monitoring. The limit should be increased only in line with inflation.

90. There should be a single registration limit for all businesses. This should set below the existing lower limit of £12,000. Some reduction in the existing exemption thresholds could be achieved during the transition to a single rate of VAT.

91. The anomaly in the treatment of hotels, guest houses and bed-and-breakfast establishments should be removed.

92. The exemption of the letting of immovable property should be confined to rented residential accommodation. All other activities involving the letting of immovable property should be chargeable to VAT, subject to the registration limits applying to other businesses.

93. In principle, we believe that second-hand goods sold by businesses registered for VAT should be charged to VAT and that the trader should be allowed a credit in respect of the residual VAT in the purchase price paid for second-hand goods. However, pending developments in the European Economic Community, we make no recommendation for change in the existing treatment of second-hand goods.

#### **Chapter 19: Administration of Customs and Excise Duties**

94. A review of customs and excise legislation should be undertaken to update, simplify and consolidate the law relating to customs and excise.

95. A small number of inland clearance depots should be set up with full time customs and excise staff and facilities available on site.

96. The power of seizure should be retained but a general code of practice for seized goods should be published and made available to persons concerned at the time of seizure.

97. Offences and penalties in the customs and excise area should be revised as part of the consolidation of legislation. This revision should take account of the general principles which we have laid down in respect of other tax offences.

98. Customs and excise offences and penalties should be banded and categorised.

99. Monetary penalties should be related to the duty evaded rather than to the duty paid value of the goods. In the case of prohibited goods, a fixed penalty or a penalty related to the value of the goods, whichever is more appropriate, should be imposed.

#### **Chapter 20: Motor Vehicle Duties**

100. The recommendations in our third report to simplify the rates of motor vehicle duties should be implemented.

101. An Post should be given the agency to collect motor vehicle duties.

102. The level of penalties imposed for non-payment of motor vehicle duties should be reviewed and seizure of the vehicle should be introduced as a penalty.

#### **GLOSSARY OF TERMS**

<i>Administrative Costs:</i>	The costs of assessment and collection of tax borne by the public sector.
<i>Advance Ruling:</i>	A statement by the Revenue Commissioners on how they will interpret legislative provisions in a given situation.
<i>Bonded Warehouse:</i>	Place used to store goods liable to customs and/or excise duty which is covered by a bond or security for the payment of duty.
<i>Cash Flow:</i>	The flow of money payments to or from a business.
<i>Compliance Costs:</i>	The costs to the private sector in money, time and effort of assessment and collection of tax.
<i>Consolidation:</i>	The combination of various parliamentary acts into one single act.
<i>Cumulative System:</i>	The cumulative system of PAYE is designed to calculate an employee's exact liability to income tax on any pay day. The tax liability on that date is the difference between the total net pay to date since the start of the income tax year and the total accumulated tax free allowance to date since the start of the income tax year.
<i>Customs Duties:</i>	Charges levied on imported goods from non-EEC countries.
<i>Customs Entry:</i>	A formal, signed declaration presented to the customs authorities by an importer or his agent to enable goods to be cleared for importation. It contains a description of the goods, gives the relevant tariff code number and relevant excise number which govern the rates

	of customs and excise duty chargeable. It is normally accompanied by an invoice showing the value of the goods.
<i>Direct Assessment:</i>	Assessment of one's tax liability by the Revenue Commissioners.
<i>Distrain:</i>	The legal seizure of goods and chattels in order to pay a debt.
<i>Double Taxation:</i>	The situation in which the same tax base is taxed more than once.
<i>Double Taxation Relief:</i>	Relief given against one country's tax charge for certain taxes paid in another country on the same income.
<i>Duty Paid Value:</i>	The retail price of an item inclusive of any duty or tax.
<i>Efficiency:</i>	Allocating economic resources so that optimal output is achieved.
<i>Effective Tax Incidence:</i>	Identification of where tax actually falls as a result of adjustments to economic behaviour after the tax is legally assessed.
<i>Equity, Tax:</i>	Standards of fairness. The tax payable should accord with ability to pay.
<i>Excise Duties:</i>	Selective taxes imposed on certain goods, the most common being on tobacco, alcohol and petrol.
<i>Extra-Statutory Concession:</i>	Relaxation which gives the taxpayer a reduction in tax liability to which he is not entitled under the strict letter of the law.
<i>Finance Act:</i>	An annual act which contains fiscal legislation.
<i>Income Distribution:</i>	The way in which total national income is divided among individuals or households.
<i>Insolvency:</i>	A situation where a person or organisation is unable to pay debts when they become due.

<i>Liquidation:</i>	The winding up of the affairs of a company when it ceases business.
<i>Mitigation:</i>	A reduction in the severity of punishment.
<i>Movements System:</i>	A system used when an employee changes job which ensures that all the relevant tax information is passed from one employer to the next. The system is operated by means of the form P.45
<i>Nulla Bona:</i>	Literally having no goods. The debtor has no assets which can be seized to settle a debt.
<i>PAYE:</i>	System of collecting income tax through regular deduction by the employer from earnings as they are paid.
<i>Phoenix Syndrome:</i>	This occurs when a company begins trading, builds up a significant tax debt, disposes of its assets and liquidates without payment of the tax due. Trading is then resumed by one or more of the directors of the previous company, often in the same premises and using the same equipment but under the protection of the limited liability of the new company.
<i>Receivership:</i>	Having one's property or business administered by a person appointed by the courts until debts are paid in full.
<i>Revenue Preference:</i>	In the event of the receivership or liquidation of a company, the Revenue Commissioners' claim for one year's tax is met before that of unsecured creditors.
<i>Revenue Practice:</i>	The way in which the Revenue Commissioners apply tax law.
<i>Schedules, Income Tax:</i>	For income tax purposes income is classified under certain heads or schedules. Schedule C covers income from interest (taxed at source) on certain government or other securities, Schedule D covers income from self-employment, rents or investments, Schedule E covers income from an office, employment or pen-

	sion and Schedule F covers income from distribution received on or after 6 April, 1976 from a resident company.
<i>Seizure:</i>	The legal confiscation of goods, documents etc.
<i>Self-assessment:</i>	A system which requires the taxpayer to complete an annual return and be responsible for calculating his own liability. There would be a thorough audit of a limited number of cases.
<i>Summary Powers:</i>	Powers which are exercised without all the formalities required by common law.
<i>Tax Avoidance:</i>	The minimisation of tax liability through taking advantage of some provision or lack of provision in the law, in circumstances other than that perceived to be intended by the legislature.
<i>Tax Base:</i>	The object to which the tax rate is to be applied, for example, income, wealth, consumption.
<i>Tax Code:</i>	The body of statutes and regulations which relates to tax.
<i>Tax Credit:</i>	An offset against tax liability.
<i>Tax Evasion:</i>	An illegal understatement of income or assets or overstatement of allowances, in an attempt to escape payment of tax. It ranges from deliberate errors or omissions to concealment, false declarations and major fraud.
<i>Tax Free Allowance, Certificate of:</i>	A statement issued to an employee and his employer showing the total amount of the tax-free allowances to which the employee is entitled together with the equivalent weekly and monthly figures.
<i>Tax-gearred Penalty:</i>	A penalty which distinguishes between larger and smaller cases by relating the penalty to the amount of tax involved.
<i>Tax Yield:</i>	The amount of revenue which is collected

	from a particular tax or the tax system as a whole.
<i>Time-gearred Penalty:</i>	A penalty which distinguishes between greater and lesser delay in complying with obligations.
<i>VAT Input Credit</i>	A credit which a VAT-registered trader receives for VAT paid by him to his suppliers or to the customs authorities at the point of importation.
<i>Withholding Tax:</i>	Deduction of tax at source, for example, PAYE.

Part I

**General Approach**

## CHAPTER 1

### GENERAL PRINCIPLES

#### Introduction

1.1 In this chapter we set down general principles which should underpin good administration of a tax system. We then outline our broad impressions of the administration of the present system and examine some of the administrative implications of the recommendations in our first four reports.

#### Basic Principles

1.2 The administration of a tax system must ensure that taxation is fair, efficient and simple. Equitable and efficient administration requires that all tax provisions can be administered with reasonable uniformity between taxpayers. Tax provisions which can only be enforced in some areas are unfair and result in distortions. Simplicity is achieved if the relationship between the taxpayer and the collecting authority is clear and unambiguous, if the administrative costs of tax collection are small and if the compliance costs for the taxpayer in terms of money, time and effort are also small.

1.3 Certainty about how much is due and when it is due requires clear and precise legislation. The scope for administrative discretion should be reduced to a minimum. In such circumstances, everyone is seen to be treated alike and grounds for complaint are minimised. Provisions which rely unduly on administrative discretion risk being applied arbitrarily, unfairly and selectively.

1.4 Clearly, the costs of collecting tax should be kept as low as possible. This requires some straightforward measures such as keeping tax forms and procedures as simple as possible, providing adequate information to taxpayers and proper staff training. However, collection costs include not only official administrative costs but also private compliance costs. In some cases, the cheapest method of collecting a tax may be to use companies or private individuals as agents. This is the case with PAYE, where the employer has the relevant information for a number of taxpayers in fairly

convenient form. However, this method should only be used when it is clearly the most efficient means available. There are good reasons for tipping the balance away from private compliance costs towards official administrative costs.

- Firstly, administrative costs are met from taxation, which can itself be determined with reference to fairness of the tax burden, whereas compliance costs fall on the private individual and may be distributed unequally.
- Secondly, compliance costs are resented by taxpayers, particularly when they are incurred to show little or no liability to tax.
- Thirdly, it is much easier to ascertain the level of administrative costs than private compliance costs. If the former rises, there will be greater pressure on legislators and administrators to eliminate unnecessary work and to keep procedures as simple as possible.

### The Existing System — Broad Impressions

1.5 Taxpayers often find it difficult to establish their correct liability and entitlements. Many reasons have been cited for this but it seems to us that the main administrative problems are rooted in the complexity of the present tax system. This has arisen from frequent changes in legislation, piecemeal additions to the existing system and increasing rates of tax on a shrinking tax base. We have also been struck by the low priority which problems of administration seem to be accorded in framing policy. Provisions have been passed by the Oireachtas which are not being enforced and may even be unenforceable.

1.6 The tax system which now operates in Ireland was designed to raise revenue in a fairly straightforward way. As recently as ten years ago the standard rate of income tax was the only rate which applied to 99 per cent of income taxpayers. When VAT was introduced in 1972 to replace turnover tax and wholesale tax, there were four rates of VAT but the zero rate covered a much narrower base and the 5.26 per cent rate applied to 88 per cent of all transactions. There was no capital gains tax until 1974 and the explosion in anti-avoidance legislation had not yet occurred. Each year since then has seen additions and changes. Computerisation has helped the system to operate but there is a limit to the burden which technology can carry. It has been argued to us<sup>1</sup> that the limit has now been reached and that the machinery is breaking down.

<sup>1</sup>Institute of Taxation in Ireland, Irish Federation of the Self-Employed Persons, Irish Tax Officials' Union.

1.7 The administration of PAYE is a good example of increasing complexity. New provisions over the last ten years have brought an increase in the number of amended certificates of tax-free allowances required in the course of the year, thereby creating more work for employers and the Revenue Commissioners. The number of complicating factors has also increased the number of end-of-year reviews of liability which the Revenue Commissioners have to undertake so that about half of all cases must be reviewed annually. As a result the PAYE system is strained and taxpayers are getting inadequate service.

1.8 Non-compliance is a major problem. Too many taxpayers do not send in their personal, PAYE and VAT returns on time or within a reasonable period of the due date. The assessment, appeals and enforcement systems are all used by the Revenue Commissioners to try to secure receipt of returns and accounts rather than the direct collection of revenue. Failure to send in a return will probably lead to receipt of a tax bill from the Revenue Commissioners: a bill which tends to be excessive rather than a good estimate of the true liability. This procedure is designed to provoke a response but the response generally comes in the form of an appeal only, rather than an appeal supported by sufficient information to enable the matter to be settled. Accounts and returns may be received eventually only after a number of appeal hearings. This is inefficient and wasteful. The natural answer is to set a realistic time limit for returns and accounts which is properly enforced and backed up with appropriate sanctions. Too often, unrealistic obligations are placed on taxpayers and they are not enforced when found to be unworkable. This brings tax administration into disrepute and encourages non-compliance.

1.9 To sum up, the compliance problem seems to be linked to high levels of taxation on a narrow base, the complexity of the system and the use of exaggerated assessments instead of an effective compliance code in an effort to obtain returns. As a result, the system is overwhelmed by appeals which are slow to clear. Tax finally collected is about 25 per cent of tax charged in assessments. The picture is one of a large administrative machine raising assessments which bear little relation to reality and then labouring mightily over the next two years to process the large number of appeals. One result is that too great a proportion of the resources of the Revenue Commissioners is devoted to routine processing of cases, leaving insufficient attention to persistent defaulters.

### CRITICISMS OF THE SYSTEM

1.10 We received many submissions which support our broad impressions of tax administration. The complexity of taxation came in for much criticism, giving rise to frustration among taxpayers, suspicion that they are not obtaining fair treatment, administrative delays and a heavy burden

in terms of money, effort and time, particularly on small businesses. A typical submission argued that

“there is a need to arrest recent trends in tax legislation which have increased complexity without significantly improving the tax yields and which have added to the difficulties, on the part of taxpayers and their advisers, in understanding the real intentions of the legislature.”

### Assessment

1.11 Most of the criticisms of the income tax system related to assessment procedures for the self-employed. Many of these criticisms apply also to PAYE. It was argued that taxpayers lack sufficient information and guidance in making tax returns. Although information and guidance is available from the Revenue Commissioners, the onus is on the taxpayer to seek this out. Many submissions instanced poor quality of service from the Revenue Commissioners in seeking the simplest of information; for example, long delays in dealing with postal correspondence, lack of privacy and inadequate facilities to deal with personal callers to tax offices also caused concern.

1.12 With regard to income from self-employment, some submissions were critical of the unrealistic assessments made by the Revenue Commissioners. Others criticised the mixture of present and preceding year bases of assessment. A number suggested that a system of self-assessment should be introduced for the self-employed, to be accompanied by stiffer penalties for tax evasion and more audit staff in the Revenue Commissioners. Others argued against the introduction of self-assessment, claiming that it was unlikely to succeed, given their view that the level of evasion was already high and non-compliance was widespread.

1.13 Many representations drew our attention to the compliance costs of the present tax system. The VAT system with many different rates<sup>2</sup> attracted particular criticism. Compliance costs are particularly high for the small business with a few employees. Such a business must cope with the complexity of the PAYE system. In addition, the owner, if self-employed, must deal with his own income tax. Finally, VAT returns must be made on the basis of purchases and sales at the various rates of VAT. All these obligations require the keeping of careful records. Some submissions favoured direct compensation for the costs involved in gathering taxes for the state. Others suggested that the costs could be reduced if the Revenue Commissioners simplified many forms and procedures and provided better information for employers and employees.

<sup>2</sup>The number of rates was reduced from six to four in March, 1985.

### Collection and Enforcement

1.14 A number of submissions expressed concern about a deterioration in collection and enforcement in recent years. This concern was particularly evident among the business community. When legitimate business is being taxed heavily, the ‘black economy’ escapes the net and enjoys a competitive advantage. Other submissions pointed out that ineffective collection and enforcement procedures only encouraged people to delay payment and, in some cases, to evade their tax liabilities.

### Appeals

1.15 Some submissions argued that the appeal procedure is inadequate to deal with the present complex tax system and suggested increasing the number of Appeal Commissioners. Others suggested that streamlining the administration of the tax system by introducing self-assessment for the self-employed, decentralising tax collection and strictly enforcing penalties would help clear the permanent backlog of appeals and allow time for consideration of complex cases.

### Consultation Procedures

1.16 A number of professional organisations expressed concern at poor communications with the Revenue Commissioners and the Department of Finance. Many were concerned that legislation was introduced without adequate consultation and/or passed by the Oireachtas with inadequate consideration. Most suggested, by way of improvement, that the Revenue Commissioners should publish statements of practice on interpretation of legislation and a list of concessions generally allowed.

## EFFECTS OF OUR PROPOSALS

1.17 The recommendations in our first four reports involve considerable simplification of the tax system arising from the following:

- (i) the replacement of multiple rates of income tax, separate capital gains and corporation taxes by a single rate of tax chargeable on all income,
- (ii) the abolition of exemptions, deductions and reliefs in the income tax system except for a single tax credit,
- (iii) the replacement of social insurance contributions by a social security tax fully integrated with income tax,
- (iv) the abolition of special income levies,

- (v) the reduction in the number of personal taxpayers liable to progressive rates of direct taxation,
- (vi) the ultimate replacement of different rates of value-added tax by a single rate on a wide base,
- (vii) the abolition of some excise duties,
- (viii) the rationalisation of motor vehicle duties (car tax), and
- (ix) the removal of many stamp duties and the eventual abolition of all stamp duties.

These simplifications, the broader income base, the abolition of deductions, allowances and reliefs, lower tax rates and the taxation of the majority of income taxpayers at a single rate would greatly lighten the administrative burden. We bear this in mind throughout this report.

### Conclusion

1.18 Tax administration should contain the following elements:

- (i) legislation which is precise and free from ambiguity. Loosely-worded or vague legislative provisions cause uncertainty as to what is taxed, when it is taxed and how much is due,
- (ii) adequate arrangements for identifying the taxpayer and obtaining other information necessary to impose the tax. Only as much information as can be processed efficiently should be gathered and there must be an efficient system for converting the selected information into a form usable for enforcement purposes,
- (iii) adequate control and enforcement in order to protect those who comply voluntarily. Otherwise compliance will deteriorate,
- (iv) a procedure for resolving disputes between the taxpayer and the administration. Ultimately judicial review is the only reliable and satisfactory check against arbitrary, erroneous or unfair administration,
- (v) a high level of collection of tax. A sure sign of ineffective tax administration is the existence of large default in tax payments, and
- (vi) effective sanctions available through the courts where there has been serious and deliberate fraud.

1.19 The present administration of taxation in Ireland falls too far short of these requirements. The measures proposed in our first four reports would simplify taxation so that the risk of breakdown is reduced and

administration in general is improved. However, reform of assessment, collection and enforcement procedures is also necessary.

## CHAPTER 2

### THE LEGISLATIVE PROCESS

#### Introduction

2.1 In this chapter we examine the legislative processes related to fiscal matters. In particular we discuss the need for consultation with interested parties. We conclude that the argument is not about whether there should be more consultation but rather the form this should take. Then we consider the options for improving the legislative process and maintaining a general review of tax legislation.

#### PRESENT SYSTEM

2.2 Proposed tax legislation first appears in a finance bill. This is usually published in the spring of each year. The Provisional Collection of Taxes Act, 1927 requires that a bill having the same effect as a financial resolution must receive its second reading in Dáil Éireann within the next thirty days on which the Dáil sits after the resolution is passed by the Dáil. The bill must be passed within four months from the date on which the resolution is expressed to take effect or, where no such date is expressed, from the passing of the resolution by the Dáil. This means, in effect, that the finance bill must be passed within four months of budget day each year.

2.3 Finance bills are debated in the Dáil. There is a discussion of general principles at second stage, a lengthy and detailed discussion of at least some of the provisions at committee stage, followed by a much shorter report stage. The bill is then passed to the Seanad which considers it but has no power of amendment. In theory, this enables each clause and schedule to be carefully scrutinised and debated before being enacted. However, in practice there is often intense pressure on time and many of the provisions appearing in a modern finance bill are of such complexity that they cannot be examined adequately in the time available.

#### A Range of Views

2.4 Dissatisfaction with existing procedures was clear from submissions.

One stated that:

"In recent years the debates have been brought to an end by the guillotine because Bills have been too long for full discussion in the time available. The 1980 Finance Bill of ninety-six sections was guillotined at Section 33. As the remaining sections were not debated in the Dáil, the necessary details for a proper understanding of the legislation could not be elicited."

2.5 Another submission summarised the criticisms of present arrangements:

"The delay in the publication of the bill after the budget; the hurried drafting of complicated provisions in the bill; the lack of consideration at committee stage of the bill in the Dáil. As a result the implications of many complex technical provisions were not fully appreciated or discussed before they were enacted."

2.6 We asked the Department of Finance and the Revenue Commissioners for their views on whether the present system could be improved. They

"cannot accept that the finance bill legislation is enacted without adequate consideration and consultation. The full resources of the budget section in the Department of Finance and the appropriate sections in the Office of the Revenue Commissioners are made available to deal with this work. Those employed in drafting legislation have considerable experience of doing so. While the bill is frequently amended after publication, the amendments are usually in response to representations or are additions to the bill of material that could not be finalised in time for the publication date."<sup>1</sup>

2.7 On the question of consultation, the Department of Finance told us that in their experience

"there is no shortage of professional advice available when a finance bill is being prepared. Indeed, once the budget proposals are announced, interest groups make representations in regard to virtually every proposal. When the Minister considers that a useful purpose would be served, it has been the practice to consult interested parties. Experience of both representations and consultation is, however, that generally the aim of the interest groups involved is to press for concessions rather than to offer impartial advice.

"The basic constraint on consultation with outside interests is created by the limited time available under present legal arrangements between the announcement of measures in the budget and the introduction of

<sup>1</sup>Letter of 2 November, 1984.

the finance bill. Because of budget confidentiality, it is not possible to consult interest groups before budget day on proposals affecting them. Once the budget is announced, the finance bill must be introduced as early as possible. The financial resolutions passed at budget time have only limited legal life and must be given full legal effect in a finance act before the expiry of four months from the date of the budget. In addition the tax changes announced in the budget are generally for implementation in the new tax year (i.e. from early April) so that they must also have early legal effect".<sup>2</sup>

2.8 We are faced with a clear conflict of evidence. Generally speaking, the public service is satisfied with the present legislative processes and the procedures for consultation with interested parties and sees no need for change. Others are dissatisfied.

2.9 The 1984 Finance Bill contained one hundred and sixteen clauses. In each of the years 1983 and 1982 there were over one hundred clauses. Some of the clauses enacted were not debated in Dáil Éireann because of pressure of time. This seems to us *prima facie* evidence of overburdened procedures.

2.10 There is evidence to suggest that some questions receive inadequate consideration by government before being included in the budget or finance bill. This is indicated by a number of instances of confusion and reversals of policy after matters have been announced. For example,

- (i) in 1973, it was announced in the Budget Statement that the tax-free margin accorded to certain bank deposits was being withdrawn. This proposal was dropped after further consideration,
- (ii) in 1979, it was announced in the Budget Statement that capital allowances on new plant and machinery would in future be given on the net cost after taking account of grants received. This proposal was later dropped,
- (iii) in 1984, there was confusion following the proposed measures against bond-washing announced in the 1984 Budget Statement,
- (iv) in 1984, the changes in proposals on tax-related lending during the 1984 Finance Bill suggest that the implications of the proposals announced in the Budget were not fully understood at the time, and
- (v) in 1985, Budget proposals on the taxation of building societies and value-added tax on the building industry were amended.

It is right and proper that changes should be made to policy and draft

<sup>2</sup>Letter of 2 November, 1984.

legislation in the course of debate where these are shown to be necessary and lobbying may also have played a role in the examples above. Nonetheless, we consider that some of the changes mentioned above were merely instances of inadequate consideration of the issues involved and hasty preparation of the legislation. The resulting confusion could have been reduced or avoided if consultation and debate had taken place in a calmer atmosphere, with more time than allowed by present procedures.

## THE OPTIONS

2.11 We have considered the following changes as a means of improving the legislative process and maintaining a general review of the legislation:

- (i) the enactment of a technical finance bill separate from the budgetary process,
- (ii) the publication of draft legislation in advance,
- (iii) the appointment of a Joint Oireachtas Committee on Fiscal Affairs,
- (iv) the creation of a technical advisory committee drawn from accountants, tax advisors and lawyers to assist the Department of Finance and the Revenue Commissioners,
- (v) the creation of a permanent review body to report to the government on different aspects of tax legislation and administration (as exists in France),
- (vi) greater mobility of staff between the Office of the Revenue Commissioners and the Department of Finance, and
- (vii) the consolidation of existing tax legislation.

### Technical Finance Bill

2.12 We asked the Revenue Commissioners about the possibility of enacting a significant amount of fiscal legislation in a technical finance bill separately from the budgetary process. They told us that

"we are opposed to having a separate finance bill to deal with technical matters. This would be impracticable due to

- (i) a shortage of skilled personnel to undertake the necessary work involved in two bills. Two finance bills would impose an impossible burden on the staff involved,
- (ii) the need to negotiate a large number of double taxation agreements. This important work has fallen into arrears and can only be tackled in the autumn of each year when finance bill pressures have eased,
- (iii) a separate technical bill which would not have to be passed within

four months as is required for the ordinary finance bill would take much longer to get through the Dáil; skilled staff would be involved for that much longer, and

(iv) in any event, the number of purely technical items is quite small”<sup>3</sup>

2.13 We do not favour the introduction of a second finance bill. It could be difficult to identify purely technical measures which have no other implications. We would prefer to see pressure on the finance bill being relieved by introducing new taxes in separate legislation. This would also allow more time for the drafting of legislation and for full consultation and debate. In the past, value-added tax, capital gains tax and corporation tax were introduced in separate legislation. The residential property tax could also have been introduced in this way.

#### **Advance Publication of Legislation**

2.14 Routine advance publication of legislation can never be a full solution since decisions on what is included in the budget statement are often taken only days beforehand and where there are budgetary implications, prior warning cannot be given. Nevertheless, it has happened on occasion in the past; for example, the proposals for value-added tax, corporation tax and new capital taxes were all the subject of white papers which provided, in some detail, advance information on the proposed legislation. The white papers did not incorporate draft legislation but they did provide an opportunity for consultation. There have been more recent occasions when advance publication of draft legislation would have been appropriate, the reduced rate of tax on manufacturing profits being a good example. This legislation did not take effect until 1 January, 1981. It was introduced in the 1980 Finance Bill but time-pressure prevented debate in the Dáil. The alternative of publishing the legislation in draft form and enacting the final legislation in the autumn of 1980 would have allowed much more time for consultation and debate. We recommend that draft legislation covering important policy changes be published well in advance, even if confidentiality requires keeping back some key details such as specific rates at which a new tax would be levied.

#### **Joint Oireachtas Committee**

2.15 Despite the relative priority given to fiscal legislation each year, it is clear that consideration of this by the Dáil is hopelessly inadequate. It is unrealistic to expect the Dáil itself to provide more time for this. Much of the legislation is complicated and few deputies have sufficient interest or knowledge to consider it fully. We recommend the establishment of a Joint

<sup>3</sup>Agreed note of meeting with the Revenue Commissioners, 12 December, 1984.

Oireachtas Committee on Fiscal Affairs. This Committee would have powers to investigate matters within its brief on its own initiative and would also deal with the committee stage of those parts of the annual finance bill which were referred to it by the Dáil. This Committee would function like the Joint Committee on Consolidation Bills which has powers to send for papers and records, hear witnesses and reports on the bill with or without amendments to both Houses.

#### **Advisory Committee**

2.16 It has been suggested to us that a technical advisory committee of accountants, tax advisors, lawyers and revenue law experts could advise the Department of Finance and the Revenue Commissioners on anomalies in legislation or aspects which hamper administration and suggest appropriate amendments or other legislation.

2.17 The Department of Finance advised us that

“We do not consider that an informal advisory committee would be an improvement but would merely add another layer to the administrative work needed for the finance bill. The value of a committee would also be limited by the fact that much of the preparatory work for the finance bill is of a confidential nature which could not be discussed with outside persons.”<sup>4</sup>

2.18 The Revenue Commissioners were also opposed to this. They told us there was no shortage of advice. All tax legislation and proposals for change are reviewed annually. Account is taken of anomalies identified in submissions and the views of representative bodies.

2.19 An advisory committee exists in the United Kingdom and appears to work satisfactorily. Our own experience during our work strongly endorses the value of discussion and consultation. We believe that the present unsatisfactory experience of consultation to which the Department of Finance and the Revenue Commissioners have referred arises because representative bodies feel their views are virtually ignored and no dialogue takes place. There is benefit to be gained from impartial advice on technical aspects of taxation law and administration. We see a distinction between making submissions and having consultations. There is also a difference between special pleading for sectoral interests and comment on the practical effects of technical measures.

2.20 We recommend the establishment of a technical advisory committee representative of the main professional bodies in the taxation area, to assist

<sup>4</sup>Letter of 2 November, 1984.

the Revenue Commissioners and the Department of Finance in identifying aspects of taxation law and administration which need to be improved.

### Permanent Review Body

2.21 We have considered whether or not it is desirable to establish a permanent review body to report to the government on different aspects of tax legislation and administration. This body could be organised on the lines of the *Conseil des Impôts* in France.

2.22 Such a body would function very much on the lines of a permanent Commission on Taxation. Our experience over the last five years confirms the value of such a body. However, we think this is likely to be far more effective if it is set up on a temporary basis when the need arises: perhaps once every thirty years.

### Staff Mobility

2.23 Under the existing system, the Revenue Commissioners advise the Department of Finance on technical changes to legislation. The Department of Finance is responsible for policy and the Revenue Commissioners for administration. The rigid division between the personnel involved in policy and administration leads to inadequacies in tax policy-making. The Department of the Public Service advised us that in relation to the technical shortcomings in legislation

“deployment of senior inspectors from the Revenue Commissioners to the Department of Finance would improve matters”.<sup>5</sup>

The Report of the Public Services Organisation Review Group (Devlin Report)<sup>6</sup> in 1969 also envisaged transfers between the Department of Finance and the Office of the Revenue Commissioners and vice versa.

2.24 We consider that both the Office of the Revenue Commissioners and the Department of Finance would benefit from staff mobility between them. We note that this is possible under the new arrangements for appointment to posts of principal and higher which were instituted in 1984 and 1985. However, we think that temporary transfers between the two bodies are desirable at middle-management level on a more systematic basis. We so recommend.

<sup>5</sup>Agreed note of meeting with the Department of the Public Service, 10 December, 1984.

<sup>6</sup>Prl 792 paragraph 33.4.9.

### Consolidation of Tax Legislation

2.25 Taxpayers and their advisors should find tax legislation easily accessible. The most recent consolidation of income tax law, the Income Tax Act, 1967, came into force on 6 April, 1967. This legislation has been amended by subsequent annual finance acts. Corporation tax was introduced by the Corporation Tax Act, 1976 and Capital Gains Tax by the Capital Gains Tax Act, 1975. These taxes have also been amended in annual finance acts and in addition the Capital Gains Tax (Amendment) Act was enacted in 1978. The volume of fiscal legislation relating to income tax, corporation tax and capital gains tax to be found outside the original enactments or the latest consolidation in the case of income tax is now almost equal to the legislation in the principal sources.

2.26 The law relating to value-added tax has been consolidated on a non-statutory basis by the Revenue Commissioners. The law relating to customs and excise is scattered through a series of acts (some of great antiquity) and statutory orders and regulations. Customs and excise legislation in the United Kingdom has been consolidated twice — firstly in 1952 which simplified and updated the legislation and secondly in 1979 which merely consolidated the 1952 legislation and the legislation enacted between 1952 and 1979 — without making any substantial changes.

2.27 Tax legislation is unique in its frequency. No other areas of law require the same degree of annual change. Thus, there is a special need to consolidate the enormous mass of such legislation at more frequent intervals than for most other forms of legislation. Statutory consolidation of tax legislation should take place at regular intervals, say every ten years.

### Recommendations

2.28 We believe that legislation that is passed after consultation is better than legislation introduced without it. In our view, the argument is not about whether there should be more consultation but rather the form this should take. Against this background, we make the following recommendations:

1. Draft legislation on taxation should be published in advance to the greatest extent possible to allow more time for public evaluation of proposals.
2. A Standing Joint Oireachtas Committee on Fiscal Affairs should be established. This committee should deal with the committee stage of the finance bill and other fiscal matters and have powers to send for papers and records, hear witnesses and report the bill to the Dáil, with or without amendments.

3. A technical advisory committee representative of the main professional bodies in the taxation area should be established to assist the Revenue Commissioners and the Department of Finance in identifying aspects of taxation law and administration which need to be improved.
4. Temporary transfers of staff at middle-management level between the Office of the Revenue Commissioners and the Department of Finance should be instituted on a systematic basis.
5. Statutory consolidation of tax legislation should take place at regular intervals.

## CHAPTER 3

### REVENUE PRACTICE

#### **Introduction**

3.1 In this chapter we consider the question of Revenue practice. By this we mean the way in which the Revenue Commissioners apply the tax system where

- (i) the legislation does not cover the case in question or is unclear,
- (ii) the legislation cannot be implemented strictly or in a cost-efficient manner.
- (iii) the legislative detail appears deficient, unjust or in conflict with the general spirit of the legislation in question, or
- (iv) the legislation confers some discretionary powers in its operation on the Revenue Commissioners.

In short, Revenue practice covers interpretation, concession and discretion. Among the issues which arise under this heading are advance rulings, extra-statutory concessions and the exercise of administrative discretion by the Revenue Commissioners.

#### **Present Position**

3.2 Revenue practice in Ireland is not directed by legislation. It is established by Revenue decision. When requested, the Revenue Commissioners may express their view of the interpretation or application of the tax system. There is, however, no general clearance or rulings procedure for transactions. The Revenue Commissioners told us that they do not, in general, provide advance rulings. An exception is made in the case of incentive reliefs for projects with which the Industrial Development Authority or another state agency is associated.<sup>1</sup> Apart from questions of interpretation of the law there are aspects of the law which are clear but which are considered to require alleviation in some way. This is done by

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<sup>1</sup>See also 'Industrial Policy', White Paper, July 1984. Pl. 2491, paragraph 8.5.

extra-statutory concession in individual cases. Finally, there are some instances where the legislation confers some discretion on the Revenue Commissioners in the operation of particular provisions.

3.3 A good example of Revenue practice in operation is the treatment of expenses incurred by employees charged to tax under Schedule E. In theory, the admissible expenses of all employees should be precisely determined. However, in certain instances the Revenue Commissioners allow certain groups of employees a flat-rate expenses allowance in cases in which experience suggests that large numbers of the employees in question incur much the same expenses during the course of the year. We think this is justifiable on grounds of administrative efficiency but should be confined to instances in which the amount of expenses does not vary much between particular employees in the group and the deduction is relatively small.

3.4 The decisions, interpretations and rulings which constitute Revenue practice are not published on a systematic basis. Occasionally the Revenue Commissioners issue a statement of their policy relating to particular tax provisions but this rarely happens.

#### **Criticisms of the Present Position**

3.5 A number of submissions suggested that the absence of official information concerning the existence and extent of Revenue practice and, in particular, extra-statutory concessions creates inequity between taxpayers and hinders decision-making. One submission argued that

“a trader who has a tax advantage of which a competitor, because of lack of information, is not aware, has received a hidden subsidy from the Revenue”.

Another submission contended that

“tax practitioners may not be aware of a concession in relation to a specific matter and an investment proposal which is postponed, or even abandoned, might be proceeded with if the Revenue concessions were known”.

3.6 Information on Revenue practice concerning extra-statutory concessions may not always be available even to the general body of inspectors of taxes. This anomaly arises because concessions are granted on an individual basis and the Revenue Commissioners are a decentralised organisation operating through a number of offices in Dublin and around the country. This in turn can lead to some inconsistency in the application of Revenue

practice. The present arrangements, while trying to introduce some flexibility into the tax code and to remove inequities, create others by the failure to provide information.

3.7 We consider that two basic principles should govern Revenue practice:

- (i) that it is known or easily available to those who need or wish to know, and
- (ii) that it is applied consistently between all those to whom it relates.

3.8 Better and more clearly drawn legislation would restrict the discretionary element in Revenue practice. Nevertheless, it is difficult to envisage a tax system in which executive discretion is absent. Revenue practice should be accepted as an essential part of our tax system and should be regulated properly. At the very least, the concessional element of Revenue practice should be recognised in legislation. Revenue interpretations and rulings should be published regularly and they should be subject to independent scrutiny.

#### **Advance Rulings**

3.9 The complexity of fiscal legislation is such that businessmen and their advisors find it necessary to approach the Revenue Commissioners for clarification of legislative provisions. Except in the cases noted in paragraph 3.2, the Revenue Commissioners do not give advance rulings which are binding on the inspector of taxes when the tax computations and liabilities come to be agreed. They told us that this is because

- (i) the volume of work to which this would give rise would be enormous,
- (ii) the facts put before the Revenue Commissioners are often inconsistent with the final position,
- (iii) the Revenue Commissioners could be liable for damages if the courts overturned their opinion, and
- (iv) they do not wish to facilitate tax avoidance.<sup>2</sup>

3.10 Advance rulings cannot replace tax advice. It is the tax advisor's function to advise and he should be able to do this in the light of the latest information available to him. A procedure for advance rulings may merely provide an excuse for the advisor not to give advice. In any case, where there is some reasonable doubt on the position such that the advisor finds it difficult to advise with any certainty, it is unlikely that the Revenue

<sup>2</sup>Agreed note of meeting with the Revenue Commissioners, 12 December, 1984.

Commissioners would prejudice their own position by giving a ruling favourable to the taxpayer.

3.11 We see no case for a general extension of advance rulings on the basis that the measures we propose later for more public information and scrutiny of Revenue practice will contribute to greater certainty in this area. We also believe that our proposals, by removing some of the curious distinctions that exist in the present tax code, will make the system much clearer and more certain and reduce the need for advance rulings.

### Revenue Discretion

3.12 As part of their duty to administer the tax system, the Revenue Commissioners must be free to take a view on the law which prescribes that system. The Revenue Commissioners have a power of interpretation but the final word on what the law means rests with the courts. The Revenue Commissioners' responsibility to administer the system also gives them authority to devise the best practice of dealing with particular situations under the legislation. There is a thin line between what amounts to a proper way to run the tax system and what is a concession to a taxpayer.

3.13 Some legislation confers specific discretionary powers on the Revenue Commissioners. For example, where the normal taxation provisions relating to resident employees who exercise their employment wholly abroad would give rise to hardship, the Revenue Commissioners are empowered to grant such relief as, in their opinion, is just.<sup>3</sup> In addition, the Revenue Commissioners are charged with the 'care and management' of all taxes and duties (except rates and excise duties on mechanically propelled vehicles). The extent of the discretion conferred on the Revenue Commissioners by this general provision has never been clearly defined and recently has been called into question.

3.14 In evidence before the Public Accounts Committee, the Accounting Officer for the Revenue Commissioners stated that

"while the Revenue Commissioners have no precise statutory discretion to remit such interest (that is, interest on overdue VAT and PAYE/PRSI deducted by employers), they regard themselves as having general discretion under the 'care and management' provisions."<sup>4</sup>

<sup>3</sup>Section 76 (4) Income Tax Act, 1967.

<sup>4</sup>Committee of Public Accounts, Interim and Final Reports 1977. (Pr. 8562), page 49.

3.15 The Public Accounts Committee had difficulty in accepting unreservedly the view that the 'care and management' provisions allowed the Revenue Commissioners discretion not to pursue the collection of statutory interest on overdue PAYE and VAT. It felt that there must be some limits to what those provisions could comprehend. It did not seem reasonable that the Revenue Commissioners could ignore the requirement of tax legislation on administrative grounds. The Committee called for

"clarification by the Attorney General as to whether the 'Care and Management' provisions allow the Revenue Commissioners to adopt a policy of not pursuing the statutory interest charge on overdue PAYE and VAT."

3.16 The issue of the extent of the Revenue Commissioners' discretion under the 'care and management' provisions has not yet been clarified by the Attorney General. However, we asked the Revenue Commissioners for their view on the powers conferred on them by the 'care and management' provisions. They replied that

"the care and management provisions have not as far as we are aware ever been legally interpreted. However, these provisions place on the Revenue Commissioners the responsibility for administering the law in relation to taxes, subject to the general direction of the Minister for Finance and subject to a right of appeal to the Appeal Commissioners and the courts. The management provision enables us to exercise administrative discretion in allocating the resources available to us. We are not required to implement the letter of the law in all cases, regardless of cost. Under the care provision, we mitigate the application of the law if its literal interpretation would not be in accord with the intention of the Oireachtas or if it would result in hardship.

"In general, the care and management provisions in Ireland are more limited than in the United Kingdom, due to the constraints imposed by a written Constitution. The operation of 'care and management' is subject to the supervision of the Comptroller and Auditor General and the Public Accounts Committee. There are strict rules to be followed before tax would be written off.

"There is a major difference in relation to extra-statutory concessions between Ireland and the United Kingdom. In Ireland, the Revenue Commissioners are bound by both legislation and the Constitution. This precludes us from making general extra-statutory concessions. Any such concessions would have to be provided for in legislation. We could apply an extra-statutory concession in an individual case under the care provisions. Since general extra-statutory concessions are not allowed, they do not exist and cannot be published.

"The care and management powers are rather slight. Their application

varies as different problems arise. In practice, more discretion is needed in relation to assessment than to collection. We do not have to account to the Comptroller and Auditor General in relation to assessment but, against this, assessments are subject to appeal. As far as assessment is concerned, individual inspectors of taxes must enjoy a degree of autonomy but they are subject to close supervision by the Superintending Inspectors of Taxes. The most that can be said is that, under the care and management provisions, we are allowed to fail to collect tax but not to give an exemption.<sup>15</sup>

3.17 The whole area of tax concessions is a difficult one. On the one hand, the tax code is practically unworkable without the flexibility of some tax concessions. On the other hand, to grant too much power to the Revenue Commissioners to make concessions could lead to widespread legislation by bureaucracy.

3.18 The views of the Revenue Commissioners quoted in paragraph 3.16 that

“since general extra-statutory concessions are not allowed, they do not exist and cannot be published.”

are disingenuous. The way certain legislation is interpreted in a given situation may amount in practice to an extra-statutory concession. It should follow that the Revenue Commissioners apply the same interpretation in all similar situations, in which case there can be no objection to its being published. It is entirely reasonable that this interpretation or practice should be available to the public in a readily accessible way. This is the only defence against administration which may become arbitrary and against suspicion which may be unfounded.

3.19 We recommend that concessions embodied in present practice should, as far as possible, be incorporated into the general body of legislation. Where practice results in interpretations of general application in particular circumstances and there is reason not to include them in legislation, they should be published at regular intervals in the form of practice notes. It is essential that changes in Revenue practice should be brought to the attention of the public. This includes any decision by the Revenue Commissioners to use provisions in the law which have remained dormant or fallen into disuse. While the Revenue Commissioners are entitled to use any provisions in tax law, the public should be notified of any change in Revenue practice. However, we recognise that some provisions in tax law are rarely used but are nonetheless necessary from time to time.

<sup>15</sup>Agreed note of meeting with the Revenue Commissioners, 12 December, 1984.

3.20 As we noted in paragraph 3.8, it is desirable that in all questions of interpretation and concession, some form of independent public scrutiny should operate. We recommend that it should be within the terms of reference of the Joint Committee on Fiscal Affairs, which we recommended in Chapter 2, to oversee and review the operation of Revenue practice. The Committee should be charged with seeing that Revenue practice is published in a form that is easily available to those who wish to know or need to know. The Committee should also see that Revenue practice is consistently and fairly applied.

### Specific Aspects of Revenue Practice

3.21 One aspect of Revenue practice which has given rise to criticism in submissions is the treatment for tax purposes of Schedule E expenses incurred by members of the Dáil and Seanad. There is public concern that these taxpayers are not on an equal footing with all others. For this reason we propose to deal with this issue.

3.22 The current position may be summarised as follows:

- (i) a flat rate deduction equivalent to 50 per cent of the parliamentary allowance as at April, 1983 is allowed to members of the Oireachtas,
- (ii) office holders, in addition to the deduction at (i), get a further deduction of 12½ per cent of their salary, and
- (iii) in addition to the combined deductions at (i) and (ii) above, a dual abode deduction may be claimed by any Minister (including Ministers of State) but not by other office holders, in respect of expenses incurred on the provision of a second place of residence. The deduction is granted for expenditure up to a maximum of one-half of a Minister's salary.

3.23 We think the existing treatment of the expenses of Dáil Deputies and Senators is inappropriate for the following reasons:

- (i) the amounts involved are too large to be passed on a rule of thumb basis,
- (ii) the amounts appear generous, given the restrictions on the allowability of expenses which are applied to other Schedule E taxpayers and the very large element of reimbursement of expenses which is allowed,
- (iii) in no circumstances should expenses be allowed as a percentage of salary,
- (iv) the basis for the dual abode allowance to certain Ministers is questionable, and

(v) the expenses incurred by members of the Oireachtas vary considerably.<sup>6</sup>

3.24 We recommend that salaries payable to Dáil Deputies, Senators, Ministers and other office holders be subject to PAYE in the normal way. Given the size of the expenses' allowances, we recommend that they be assessed on an individual basis under the rules applicable to other taxpayers.

3.25 The expenses for tax purposes of members of the Judiciary are set by the Minister for Finance. We think it is inappropriate for the Minister for Finance to set the expenses allowable for any group of taxpayers. We recommend that this function be transferred to the Revenue Commissioners.

3.26. We are conscious that there may be an element of remuneration in the existing deductions for expenses allowed to Dáil Deputies and others. It may be that increases in remuneration may be justified if our recommendations are put into effect. We think this would be a much better way of remunerating our politicians than paying them inadequate salaries and trying to compensate for this by mitigating the taxation arrangements which apply to other taxpayers. It is desirable, in principle, that our legislators face the same tax regime as other taxpayers.

### **The Board of the Revenue Commissioners**

3.27 One general feeling coming through from submissions and the discussions we had with various representative bodies was that there should be more communication between the Revenue Commissioners, the business community and its professional advisors. The perception is that the Revenue Commissioners do not appreciate many of the problems of business and trading since, generally speaking, they have little or no direct experience of business.

3.28 At present, the Board of the Revenue Commissioners consists of three members appointed by the Taoiseach. Invariably these are career civil servants drawn from the Office of the Revenue Commissioners. The Chairman is appointed by the Minister for Finance and is head of the Revenue Department and accounting officer for the Revenue Vote. The two Commissioners are ex-officio Secretaries to the Department. In practice, one normally acts as Secretary for customs and excise and the other as Secretary for inland revenue.

<sup>6</sup>Review Body on Higher Remuneration in the Public Sector'. Report No. 20, October, 1979. Pl. 8148, paragraph 12.34.

3.29 The Board of the Revenue Commissioners does not function as a Board in the conventional sense. It

“does not have regular meetings or act as a committee but does consider matters which affect the office as a whole such as planning, internal policy, finance, organisation and personnel. Board functions may be exercised ‘jointly and severally’. Therefore, each member of the Board may exercise the functions of any other member.”<sup>7</sup>

3.30 We discussed with the Department of the Public Service a suggestion that non-executive directors be appointed to the Board of the Revenue Commissioners. They

“do not favour the appointment of Board members from the private sector as conflicts of interest could arise . . . such a Board could not operate within the existing structure”.<sup>8</sup>

3.31 Conflicts of interest arise in all walks of life and there are well established procedures for dealing with them. Conflicts of interest may also arise even when Board members are civil servants. The problem of non-executive members lies more in the difficulties of finding a method of appointment which would ensure that the appointments would be seen to be made solely in the public interest, than in the principle itself. However, in the interests of public perception of the impartiality of the Board we do not recommend such appointments. Other ways of bridging the gap between the Revenue Commissioners and the taxpayer must be found. We believe that our proposals in this chapter and the proposals in Chapter 2 to improve consultation procedures will make a significant contribution in this area.

### **Conclusion**

3.32 There are various unsatisfactory aspects of Revenue practice. The powers of the Revenue Commissioners are unclear. There is a lack of uniformity in the treatment of taxpayers because information on Revenue practice is not published and there is no independent review procedure. It is essential that these defects are rectified.

### **Recommendations**

3.33 We make the following recommendations:

1. Revenue interpretations and rulings should be published regularly.
2. There should be no general extension of advance rulings by the

<sup>7</sup>Agreed note of meeting with the Revenue Commissioners, 12 December, 1984.

<sup>8</sup>Agreed note of meeting, 10 December, 1984.

Revenue Commissioners on the proposed treatment of particular situations.

3. The present range of extra-statutory concessions should be incorporated into legislation as far as possible. Where this cannot be done, it should be published at regular intervals in the form of practice notes.
4. It should be within the terms of reference of the Joint Oireachtas Committee on Fiscal Affairs, which we recommend in Chapter 2, to oversee and review Revenue practice and to ensure that it is properly published and consistently and fairly applied.
5. Given the size of the expenses' deductions allowed to members of the Oireachtas, these deductions should be allowed by the Revenue Commissioners on an individual basis subject to the rules applicable to other taxpayers.
6. The functions of the Minister for Finance in relation to determining the allowable expenses of the Judiciary for tax purposes should be transferred to the Revenue Commissioners.

## Part II

### **Tax Assessment**

## CHAPTER 4

### ASSESSMENT PROCEDURES

#### Introduction

4.1 In this chapter we consider the general procedures for assessing income tax and corporation tax liabilities. The present system of assessment by the Revenue Commissioners has become cumbersome and inefficient. Initial assessments on an estimated basis are generally excessive; tax finally collected is only about one-quarter of the tax in the original assessments. These high estimates seem to be made to elicit information from taxpayers. While they may have this effect, they also lead to appeals in almost all cases. The large number of appeals then overloads the machinery and leaves very many liabilities undetermined, sometimes for several years. We conclude that a system of self-assessment should be introduced where taxpayers would complete an annual return and be responsible for calculating their own liability. The onus to comply is shifted directly onto the taxpayer and is reinforced by an effective penalty code in respect of returns and accounts and late payment of tax. There would be a thorough audit of a limited number of cases. We are satisfied that self-assessment on this basis offers a means of securing greater rather than less compliance on the part of taxpayers.

4.2 This system of self-assessment would cover all sources of personal and corporate income which come within our definition of income, including capital gains and capital acquisitions. However, wages and salaries would be excluded where they are the only or main source of income of the taxpayer. PAYE on a cumulative basis would continue to operate to ensure that most wage and salary earners would have their tax liability worked out in full by their employers during the tax year. Withholding taxes at the single rate would satisfy any additional liability to tax on other income, such as deposit interest. Only those PAYE taxpayers with significant other untaxed income or more complex financial affairs would have to submit a self-assessment return. We consider the administration of PAYE in Chapter 6 and we examine the scope for extending withholding taxes in Chapter 5.

## EXISTING PROCEDURES

4.3 Every taxpayer directly assessable to income tax should receive a tax return each year in early April. By law he is required to complete and return this to his inspector of taxes within twenty-one days. The return requires him to disclose his income from all sources for the previous tax year (ending 5 April) and details of disposals and acquisitions of certain assets for capital gains tax purposes. The inspector should receive the completed return in early May to enable him to issue an assessment in June or July setting out his estimate of the taxpayer's income and the tax payable. This is intended to allow taxpayers sufficient time to lodge appeals before demands are issued by the Collector General. In most cases the tax is payable in one instalment by the following 1 October. If a taxpayer appeals (and he must take the initiative if the appeal machinery is to operate), he can postpone payment of tax which he thinks is not due. The elaborate provisions dealing with interest on overdue tax apply at a later stage. These are set out in Chapter 31 of our first report.

4.4 Appeals must be made within thirty days of the date of the notice of assessment but there are provisions for late appeals in certain circumstances. When a taxpayer appeals an assessment he is required to specify the amount of tax, if any, which he considers will be payable on determination of the appeal. This amount is payable on demand and collection of the excess of the tax charged over this specified amount is suspended. In order to avoid interest charges on any balance of tax due, the specified amount must turn out to be at least 85 per cent<sup>1</sup> of the taxpayer's final liability. Thus, a taxpayer must make a rough assessment of his own liability before making the initial tax payment or else pay the amount assessed.

4.5 If the inspector of taxes and taxpayer cannot agree the tax liability, the appeal is listed for determination by the Appeal Commissioners. If the taxpayer is not satisfied with the Commissioner's determination he may request a rehearing by the Circuit Court. In that event the amount of tax determined by the Appeal Commissioners becomes payable pending the Circuit Court decision. The taxpayer may appeal on a point of law to the High Court against a decision of the Appeal Commissioners or of the Circuit Court Judge.

4.6 The determination of the appeal can take a considerable length of time because of delays in submitting accounts and other information required by the inspector and because of disagreements as to the tax liability. The

<sup>1</sup>The requirement that the specified amount should be 85 per cent of the final liability applies to assessments to income tax. In the case of any other assessment to tax the requirement is 80 per cent of the tax found to be due.

process can involve a number of listings before the Appeal Commissioners and in some cases also before the Circuit Court, before agreement is reached.

## Large Number of Appeals

4.7 The Revenue Commissioners told us that appeals are made against a very high percentage of assessments.

"Timely appeals are made in about 70 per cent of income tax cases judging by the fact that out of 165,146 income tax assessments made for the year 1984/85 in July, 1984, 116,514 (71 per cent) had been appealed in August. Late appeals will increase the percentage considerably.

"Precise information of a similar kind is not available for corporation tax or capital gains tax but in the case of corporation tax, the proportion of assessments appealed is probably higher than in the case of income tax.

"The total number of incoming appeals recorded on the computer collection files for income tax, corporation tax and capital gains tax in the twelve months to mid-November, 1984 was 207,900, which is about 80 per cent of the number of assessments made annually under these three taxheads (approximately 260,000). This suggests that the proportion of assessments appealed must be somewhere near 90 per cent allowing that the numbers of assessments made annually have been increasing and that many of the appeals made in a year relate to assessments made in earlier years."<sup>2</sup>

## Backlog of Appeals

4.8 Table 1 shows figures for income tax appeals on hand during the year 1984. At 31 December, 1984 a total of 71,851 assessments made in the year ended 5 April, 1984 which gave rise to a tax charge was under appeal. The due date for payment of the tax in relation to most of these assessments was 1 October, 1983. In any event, a substantial payment on account was due on that date. Therefore, fifteen months after the due date for payment of the tax, 71,851 assessments had not been finalised even though a substantial part of the ultimate liability may have been paid. In addition, there were 42,086 cases in which assessments for earlier years had not been finalised. In any one of those cases a number of earlier years could have been under appeal. At the rate appeals were settled in 1984, it would take fourteen months to clear this backlog.

<sup>2</sup>Material supplied at meeting with the Revenue Commissioners, 12 December, 1984.

**TABLE 1**

**Income Tax Appeals<sup>1</sup> as at 31 December, 1984**

Income Tax (Schedules D and E)	Year of Account* 1983/1984 <sup>2</sup>	All Years of Account to 1982/1983 <sup>3</sup>
Number unsettled at 1 January, 1984	107,925	87,208
Number received in year	13,777	6,803
Number settled in year	49,851	51,925
Number unsettled at 31 December, 1984	71,851	42,086

Source: Revenue Commissioners

Notes:

<sup>1</sup>The figures relate to ordinary appeals to the Appeal Commissioners. Circuit Court appeals are not included.

<sup>2</sup>Represents assessments appealed.

<sup>3</sup>Represents cases in which one or more years of assessment are under appeal.

\*Year of account refers to assessments actually made in that year regardless of whether or not they relate to that year of assessment.

4.9 A similar position emerges in Table 2 in relation to corporation tax assessments. However, the number of corporation tax appeals outstanding was less serious than for income tax. A greater proportion of assessments under appeal was finalised during the year. The arrears constituted about nine months work. In addition to the income tax and corporation tax appeals there was a total of 11,562 unsettled appeals relating to VAT, capital gains tax and PAYE estimates on employers.

**TABLE 2**

**Corporation Tax Appeals<sup>1</sup> as at 31 December, 1984**

Corporation Tax	Accounting Periods ending 6/4/82 to 5/4/83 <sup>2</sup>	All Accounting Periods ending prior to 6/4/82 <sup>3</sup>
Number unsettled at 1 January, 1984	22,841	14,073
Number received in year	2,775	1,782
Number settled in year	13,569	10,206
Number unsettled at 31 December, 1984	12,047	5,647

Source: Revenue Commissioners.

Notes:

<sup>1</sup>The figures relate to ordinary appeals to the Appeal Commissioners. Circuit Court appeals are not included.

<sup>2</sup>Represents assessments appealed.

<sup>3</sup>Represents cases in which one or more accounting periods are under appeal.

4.10 The growth in appeals is partly due to increases in the numbers of taxpayers subject to direct assessment. Self-employed people at work in

the non-agricultural sector increased by 28,000 or over 38 per cent between 1971 and 1981<sup>3</sup>. In addition some 44,000 farmers have been assessed.

4.11 Table 3 shows that the number of appeal hearings more than doubled in the period between 1975 and 1983. The drop in the number of hearings in 1984 was due to the fact that only two Commissioners were available during the first half of that year. The difference between the number of hearings and determinations is explained by the fact that some cases are settled by agreement after they are adjourned at initial hearing before the Appeal Commissioners.

**TABLE 3**

**Numbers of Appeals Heard by the Appeal Commissioners**

Year	No. of hearings	No. of Determinations
1964	5,571	1,825
1970	11,492	5,252
1975	20,150	5,901
1979	11,618	4,314
1983	42,692	19,192
1984	36,532	17,866

Source: Appeal Commissioners.

**The 1985 Legislation**

4.12 Major changes were made in the appeal procedures for assessments made after 8 June, 1983. These changes were designed to reduce delays in settlement of appeals and to counteract abuses of the appeals system.

4.13 An application for adjournment of the hearing of an appeal by the Appeal Commissioners may not be refused if made

- (i) within nine months of the end of the tax year to which the assessment relates, or
- (ii) within nine months of the date on which the notice of assessment was given to appellant,

whichever of these dates is the earlier. Where such an application has been refused by the Appeal Commissioners, and

- (i) the appellant has not made a return of income, or
- (ii) the appellant has made a return of income but all the statements of profits and gains, schedules and other evidence relating to such a return have not been furnished by the appellant.

<sup>3</sup>Census of Population 1971 and 1981. The Census figures have been adjusted as in Sexton (1981).

the Commissioners shall make an order dismissing the appeal. They may, however, determine the appeal if they are satisfied that sufficient information has been furnished to enable them to do this. The distinction between dismissal and determination is of the utmost importance as the right of re-hearing of appeals by the Circuit Court is now confined to those which have been determined by the Appeal Commissioners. Late appeals are not admitted more than twelve months after the date of the notice of assessment unless the taxpayer has made a return of income and furnished such other information as the inspector of taxes may require and has paid the tax charged together with accrued interest.

4.14 The Revenue Commissioners told us that they

"are expecting a big improvement in the working of the appeals procedure following the changes introduced in 1983. It is too early to say how these will work but it is hoped that they will result in appeals being made earlier and will reduce duplication between the Circuit Court and the Appeal Commissioners."<sup>4</sup>

4.15 The Appeal Commissioners were less optimistic about the effects of the 1983 legislation. They told us that

"the appeal process will have to be taken much more slowly in dismissal cases because the Commissioners are now the final arbiters. We would be very reluctant to dismiss massive estimated assessments now that there is no further appeal to the Circuit Court. We do not see ourselves dismissing appeals automatically. One of the problems we face is dismissing an appeal in the absence of the taxpayer who might be represented by his agent. We would like the Revenue Commissioners to advise the taxpayer in the notice of the appeal hearing that they are seeking dismissal. It would also help if the inspectors of taxes were in a position to give details of tax paid for the current and previous years at appeal hearings. While we have no option but to dismiss appeals in certain circumstances under the 1983 legislation, we are not precluded from adjourning the appeal to allow the taxpayer time to comply. We may also determine an appeal if we consider that we have sufficient information to do so. We envisage that we will make some determinations on the basis of information for previous years. The determination of the appeal as opposed to its dismissal preserves the right of appeal to the Circuit Court. The 1983 legislation will not affect the majority of tax assessments until the middle of 1985 and it will be

<sup>4</sup>Agreed note of meeting with the Revenue Commissioners. 12 December, 1984.

some time after that before any judgement could be made about the effectiveness of the provisions. However, it is already clear that taxpayers and their agents are trying to circumvent the legislation. This is being done by exploring other legal remedies and by various ploys such as not attending the appeal hearing when there is a danger that the appeal will be dismissed. The taxpayer then has an opportunity to seek re-admission of the appeal. In 1978 there were 782 applications for re-admission to the Appeal Commissioners. This increased to 1,650 in 1984. The vast majority of these appeals are re-admitted."<sup>5</sup>

4.16 It is no exaggeration to say that the existing system of assessment and appeals has virtually broken down. Because of the time constraints involved under the present system, virtually all assessments must be made on an estimated basis in the absence of completed returns. The requirement that a tax return has to be filed within twenty one days of it being delivered to the taxpayer is totally unrealistic and is never enforced. Not surprisingly, the present system has fallen largely into disrepute. The existing return is, in any event, not itself a particularly helpful document for the Revenue Commissioners to have even when it is fully completed. The raw material which the inspector needs to make an assessment consists of a set of accounts and supporting tax computations, yet there is no statutory requirement for the submission of accounts. If they are not submitted, the elaborate and inefficient process of estimated assessments, appeals and postponements has to be activated to ensure that they are. As a result, the whole system is deluged with a huge number of appeals which is slow to clear so that it is overwhelmed by a large backlog of work. The picture is one of a large administrative machine raising assessments which bear little relation to reality and then labouring mightily over the next two years to reduce them to realistic levels. We do not believe that the 1983 changes in the appeal procedures will lead to a significant improvement. The only realistic prospect of solving the existing problems is to change to a system of self-assessment. We consider the case for this in the next section.

## SELF-ASSESSMENT

4.17 In this section we consider whether the present system of assessment by the Revenue Commissioners could be replaced by a system which would put the responsibility on the taxpayer to assess his own liability. This assessment would be subject to routine arithmetical check in all cases and critical examination in a small minority of cases.

<sup>5</sup>Agreed note of meeting. 4 January, 1985.

4.18 The term 'self-assessment' causes some confusion and misunderstanding. Self-assessment does not allow a taxpayer to determine his own level of taxation and there is no reason to believe that self-assessment would fail to collect large sums of revenue due from taxpayers. The level of surveillance of incomes would be at least comparable to that exercised at present and inspectors of taxes would have more time to carry out effective examinations of tax returns selected for audit. The prospect of being subjected to tax audit would in itself be a strong inducement to voluntary compliance. Automatic penalties for failure to submit a return and for understatement of income in returns, by showing taxpayers the penalties they would face if caught evading, would maintain high levels of compliance.

4.19 We examined the tax systems of other countries and found that self-assessment in various forms operates in many different countries including Canada, Japan, New Zealand and Sweden. However, the best known example of full self-assessment is the United States system. We studied the United States system in detail and a delegation from the Commission visited Washington D.C. to investigate the operation of self-assessment.

4.20 Our discussions with the United States Internal Revenue, the Department of the Treasury, public representatives, tax practitioners, accountants, lawyers, economists and members of the largest commercial 'tax preparing' firm in the United States, gave us a very full picture of the operation of self-assessment. We raised the arguments which had been made to us concerning the system and we investigated all aspects of the self-assessment procedures.

4.21 One of the questions in which we were interested, for example, was whether the system of self-assessment was responsible for the problems currently agitating tax-reformers in the U.S. If it was, was this due to an inherent defect in the system or not? The answer, from all sides, is that difficulties have arisen mainly because of frequent changes in legislation in recent years which resulted in complexities and anomalies in the U.S. tax structure and, to a lesser extent, the level of taxation. Self-assessment is not seen as the villain. Another fundamental question is whether self-assessment would work without the system of draconian penalties and armed revenue officials enforcing collection. Detection is seen as the most important weapon and self-assessment frees resources for work on examination, leading to detection. Freedom to freeze assets and levy bank accounts and powers to seize real and personal property subject to court authorisation are much more useful than the power to look for jail sentences since, except in cases of aggravated fraud (and where other criminal activities are involved), the courts are reluctant to impose imprisonment.

## Main Features

4.22 The objective of self-assessment is to take out of the hands of the Revenue Commissioners and place upon taxpayers as much responsibility as possible for calculating and paying on time their own tax liabilities. In outline, a self-assessment system would work as follows:

- (i) taxpayers would be required to calculate their own tax liability and remit the tax.
- (ii) every taxpayer would be responsible for obtaining and completing a return form annually. In practice, the Revenue Commissioners would continue to issue return forms to taxpayers for whom records were held, as a matter of convenience to taxpayers and their accountants. But non-delivery of a form would not relieve a taxpayer of his obligation to obtain and submit a statutory return.
- (iii) the return form would require a taxpayer to provide
  - (a) a full report of his taxable income and gains,
  - (b) a calculation of the tax payable (or repayable), and
  - (c) supporting schedules to show how the figures of income and gains arose,
- (iv) traders would make provisional payments of tax during the accounting year,
- (v) the return would have to be filed and the balance of tax paid by a specified date,
- (vi) all tax that was due but not paid by the payment date would be liable to an interest charge. Overpayment of tax would be repaid with interest, subject to a suitable interval to enable the Revenue Commissioners to make the repayment,
- (vii) late filing of a return would attract a penalty,
- (viii) inaccurate returns as a result of fraud or substantial misdeclaration of income would attract a penalty,
- (ix) in certain closely defined circumstances, taxpayers would be able to meet their filing obligations by making a provisional return. This would allow subsequent adjustments to be made in the light of claims, for example, for group relief, where longer time limits apply,
- (x) the Revenue Commissioners would continue to make assessments in certain circumstances, for example, where no return was filed, or where a return was subsequently amended following examination by the Revenue Commissioners.

(xi) the Revenue Commissioners would subject all returns to an initial check, probably for arithmetic and other straightforward completion errors, and to ensure that the tax paid was in accordance with the returns and in time, and

(xii) some returns would be selected for more detailed examination.

4.23 In Ireland, virtually all of the elements of self-assessment are present for self-employed taxpayers and for companies, except that the auditing function is critically deficient. However, superimposed on this self-assessment process there is a system of Revenue-assessment and an appeals procedure which are used largely to compel taxpayers to submit their returns and accounts. This is very inefficient. The key to greater efficiency in tax administration is to have a system of full self-assessment with an effective compliance code.

#### **Experience with Self-Assessment in Ireland**

4.24 Experience with self-assessment in Ireland is limited but there are examples within the tax system where responsibility has been placed on persons to estimate their own liability to certain taxes and remit the amounts due to the Revenue Commissioners.

4.25 Value-added tax is a self-assessed tax; traders must compute and pay their VAT liability every two months. In addition, the 1975 wealth tax contained a genuine element of self-assessment since sufficient information was not available to identify assessable persons. Although it was provided that details of taxable wealth should be returned on a prescribed form and that assessments would be made by the Revenue Commissioners, in practice, most taxpayers made a payment of tax on the basis of their own estimations.

4.26 The Revenue Commissioners regard their experience with wealth tax to be unsatisfactory in that they had great difficulty in obtaining returns. The amounts paid by self-assessment proved to be only about one-half of the true liability and considerable effort had to be expended by the Revenue Commissioners over many years to obtain payment of the unpaid one-half of the liability.

4.27 The residential property tax which was introduced in 1983 requires assessable persons to submit returns to the Revenue Commissioners estimating the market value of their property on 5 April each year. Returns must be submitted on or before 1 October after each valuation date and tax is payable on 1 October without the making of an assessment.

4.28 We asked the Revenue Commissioners for their experience with this tax. They replied that

“The level of compliance can be gauged to some extent by the fact that the estimated yield from the tax for 1983 was £3 million. While actual payments in that year totalled £1.04 million only. Up to 31 August, 1984, only a further £0.3 million was added to that total despite the issue of estimated assessments (selected on the basis of rateable valuations) by the Revenue from early 1984. (The picture as regards residential property tax is, of course, considerably distorted because of the legal proceedings taken to test the constitutionality of the tax).”<sup>6</sup>

The low return in relation to the estimate could also indicate that the estimate was over optimistic.

4.29 The experience with the residential property tax should not be used as a basis to reject the concept of self-assessed taxes. The residential property tax was a new tax whose constitutional validity was challenged in the courts. This had an adverse effect on compliance. In addition, many of those liable for tax were PAYE taxpayers who had no experience of self-assessment beforehand, unlike self-employed taxpayers who already have to comply with virtually all the requirements of self-assessment.

4.30 The most important element of self-assessment already incorporated into the administration of income tax and corporation tax relates to the onus placed on the taxpayer in appeal cases to specify an amount of tax which he considers to be due, as noted in paragraph 4.4.

4.31 The Revenue Commissioners' experience in relation to specified amounts in recent years is shown in Table 4.

4.32 The Revenue Commissioners told us that

“in general the number of taxpayers specifying is becoming satisfactory while the amounts specified appear to be reasonably accurate.”<sup>7</sup>

#### **Advantages and Disadvantages of Self-Assessment**

4.33 The existing procedures for assessment and collection of tax operate in a most unsatisfactory manner. At times the assessment is no more than a reminder to the taxpayer to self-assess the amount of tax which he considers to be due, that is, the specified amount and a reminder to the inspector that the taxpayer is on record but has not yet submitted a return and accounts. The system places too much emphasis on the issuing of estimated assessments and on the routine processing of the response these generate at the expense of auditing the liability of taxpayers. As a result,

<sup>6</sup>Material supplied at meeting with the Revenue Commissioners, 12 December, 1984.

<sup>7</sup>Material supplied at meeting with the Revenue Commissioners, 12 December, 1984.

inspectors of taxes spend far too much time looking at the affairs of compliant taxpayers and too little time examining the affairs of defaulters. Self-assessment would relieve the Revenue Commissioners of the burden of assessing all taxpayers. Large backlogs of appeals would not arise. Self-assessment offers the only prospect of restoring an effective system of assessment of tax on income other than wages and salaries.

TABLE 4

Distribution of Specified Amounts for Taxpayers making Timely Appeals

Specified Amount	Income Tax 1984/85 %	Corporation Tax Recent Years %
Nil	37	60
Positive Amounts	57	30
Did not Specify <sup>2</sup>	6	6

Source: Revenue Commissioners.

Notes:

<sup>1</sup>The specified amount is the amount of tax which the taxpayer is prepared to pay pending determination of his appeal. Inadequate specified amounts give rise to interest charges.

<sup>2</sup>Taxpayers in this category either neglected to specify an amount of tax due when appealing or were satisfied to have the amount assessed remain payable despite the appeal.

<sup>3</sup>The information available on the adequacy of specified amounts is very limited. A 1983 study to gauge the adequacy of amounts specified in cases where appeals had been settled concentrated on cases where the amount specified was more than nil and less than the tax assessed. 150 income tax cases and 150 corporation tax cases were examined for the years 1979/80 and 1980/81 (later years were not considered as they would not have been settled in a sufficiently high proportion of cases when the study was being done). The specified amounts as a proportion of the actual liability averaged 74 per cent in the case of income tax and 99 per cent in the case of corporation tax.

4.34 Given the inefficient operation of the existing procedures with regard to tax returns, assessments, payments on account and the duplication of work for inspectors of taxes, taxpayers and their professional advisors, self-assessment would result in a reduction in the overall cost of tax administration for taxpayers and companies.

4.35 Any proposal for self-assessment has to confront the inertia argument that in Ireland people have traditionally had their assessments issued by tax offices. Why change the existing system which is familiar and works reasonably well for a new system with unknown pitfalls? However, as we have seen, the present system does not work well and has been deteriorating steadily. Also, a change to self-assessment for Schedule D taxpayers does not require the institution of a radical new procedure with which taxpayers are unfamiliar. Following the introduction of specified amounts in 1976, Schedule D taxpayers already have to perform most of the tasks which are required to operate under self-assessment. Indeed, it could be argued that the present system gives us the worst of both worlds. Taxpayers already

suffer most of the compliance costs of self-assessment and revenue assessment and the Revenue Commissioners receive none of the benefits which self-assessment would allow.

4.36 We raised with a number of professional bodies the issue of self-assessment for income tax and corporation tax. The Institute of Taxation considered that such a system was feasible and

“favoured a system whereby the taxpayer paid quarterly instalments on an actual basis so that by the fourth quarter 80 or 85 per cent of the liability would be met. The balance should be due after review at the end of the year when accounts had been submitted and agreed. Underpayments and overpayments should attract interest at normal commercial rates. This system cannot be adopted now because of the mixture of present and preceding year bases of assessment.”<sup>8</sup>

4.37 The Consultative Committee of Accountancy Bodies — Ireland favoured self-assessment but said that it

“is feasible only if it is operated intelligently by the Revenue Commissioners and in a spirit of co-operation. Initial compliance costs would be high. It would have to be clear that these would be offset by the administrative savings which would arise in later years.”<sup>9</sup>

4.38 The Irish Tax Officials' Union, while recognising that any proposal to implement self-assessment would require considerable study, went on to say that

“there could be some benefits if aspects of the United States system were used for the self-employed here. It would be a pre-requisite for any change to self-assessment to have a simplified income tax system and to assess all incomes on a current year basis.”

4.39 We have concluded that a system of self-assessment is desirable for all persons liable to income tax and corporation tax who are, at present, subject to direct assessment. We now deal with certain issues which need to be resolved before such a system could be introduced. These are

- (i) the basis of assessment,
- (ii) a new style of return form,
- (iii) filing of returns and a compliance code,
- (iv) the arrangements for payment of tax,

<sup>8</sup>Agreed note of meeting with the Institute of Taxation, 12 June, 1984.

<sup>9</sup>Agreed note of meeting with the Consultative Committee of Accountancy Bodies—Ireland, 12 November, 1984.

- (v) the checking and auditing of returns,
- (vi) enforcement,
- (vii) revenue implications, and
- (viii) treatment of capital gains and capital acquisitions.

### Basis of Assessment

4.40. While self-assessment can, in principle, be operated on any basis of assessment, some rationalisation of the existing system would facilitate its introduction. The present position in relation to the assessment of income is particularly confusing. This is clear from Table 5. Some forms of income are assessed on a current year basis while others are assessed on the basis of the income of the preceding year. There are special provisions in relation to commencements and cessations of particular sources of income. Most deductions are on a current basis but some are not.

TABLE 5

#### Normal Basis on which Income is Charged to Income Tax Under the Present System

Income	Normal Basis of Assessment
Profits (Case I and Case II)	Income of accounting period ending in preceding income tax year
Interest and Dividends (Case III)	Income of preceding year ended 5 April
Other Income (Case IV)	Income of current year
Rents (Case V)	Income of preceding year ended 5 April
Schedule E	
PAYE including Pensions	Income of current year
Other Schedule E including Non-Contributory Social Welfare Pensions	Income of preceding year ended 5 April
Schedule F (Irish Company Dividends)	Income of current year
Building Society Interest	Income of current year

4.41 In our first report we recommended the abolition of many of the existing deductions and reliefs. We also recommended<sup>10</sup> that all income should be charged on the basis of the income arising in the current fiscal year. Where accounts are not made up to the end of the fiscal year (5 April or 31 March), apportionments would be required. However, the introduction of self-assessment would be facilitated if the taxation of self-employed persons for the current tax year were charged on the basis of the income of the accounting period ending in that year. Companies are already taxed on the basis of income arising in an accounting period.

<sup>10</sup>Paragraph 31.11.

### A New Style Return Form

4.42 A standardised return form is an essential ingredient of a self-assessment system to allow processing of the information by the Revenue Commissioners. Just as important is general acceptability, since widespread public resistance to the use of the form could result in a high failure rate in completing the form accurately. This would jeopardise the administration and undermine confidence in the implementation of self-assessment.

4.43 Only experience can provide a firm basis on which to judge the most suitable format for a new style return form. However, the new form would be essentially a tax working sheet. It would enable the taxpayer to compute his tax liability and would allow routine checking by the Revenue Commissioners. Considerable effort would have to be put into designing an experimental return and it would have to be field-tested under realistic conditions. Consultations with accountants, tax practitioners and trade associations would be essential to gain general acceptability. Separate forms would be necessary for companies and sole traders.

4.44 In the United Kingdom, a field test of an experimental return for corporation tax was carried out in 1983 in co-operation with the Confederation of British Industry and the accountancy bodies to see if the way could be prepared for self-assessment. The exercise proved very successful. Starting in the autumn of 1985, the Inland Revenue will send out a new document with corporation tax returns. This new form is for companies or their accountants to use when sending accounts and computations to their inspector of taxes. To begin with, its use will be optional, although in time it may become part of the formal tax return. No decision has yet been taken to move to self-assessment. The intention for the moment is to ensure greater compliance and more efficient use of Revenue resources.

### Filing of Returns

4.45 In most self-assessment systems, the filing date is the same as the date for payment of tax. In Ireland, all corporation tax for companies is due for payment six months<sup>11</sup> after the end of the accounting period. Income tax on trading profits is due for payment between six and eighteen months after the end of the accounting year. This arises because there is a single due date for payment of income tax, that is 1 October, even though the accounting periods of traders vary. Thus, to link the filing date with

<sup>11</sup>The Finance Act, 1985 sets the due date for payment of all corporation tax six months after the end of the accounting period. At present, corporation tax is payable in two instalments. The new provision will apply to all companies by 1987 at the latest.

the existing due dates for payment would mean that companies would have to file a return and accounts six months after the end of the accounting period and sole traders would have between six and eighteen months, depending on the accounting period used.

4.46 We believe that a filing date six months after the accounting period would be reasonable for all companies. However, there would need to be a facility for exercising options to revise certain entries on the return, such as group relief, where the statutory time limit for a claim to relief was longer than that allowed for filing. Safeguards would be needed to prevent abuse of these options. We are confident that a reasonably secure and workable framework could be constructed.

4.47 In the case of sole traders, a standard time limit for the submission of accounts and returns is necessary. Any time limit should relate to the end of the relevant accounting year. We consider that, with a reasonable transition period, a time limit of nine months after the trader's accounting year is realistic.

4.48 We recommend that there should be a requirement for self-assessment returns for companies, including supporting accounts, to be submitted within six months of the end of the relevant accounting year. Trading taxpayers should be required to submit self-assessed returns nine months after the end of the relevant accounting year or within three months of the end of tax year, whichever is the later. There should be a similar requirement for companies, with a time limit of six months. Non-trading taxpayers should be required under a system of self-assessment to submit their tax returns within three months of the end of the tax year.

### Compliance Code

4.49 To secure compliance, any system of assessment requires a regime of penalties or surcharges which are enforced. The main special requirement under a system of self-assessment is the effective imposition of a penalty for failure to make a return or for the late submission of a return. We consider that there should be an automatic late filing penalty for returns not received by the new revised filing dates, related to the amount of tax payable but not paid by the due date and to the degree of lateness. This could be supplemented by a simple and automatic non-filing penalty which would be initiated by the tax office and be of particular value in cases where the late filing penalty proved to be an ineffective sanction, for example, where the tax return showed a loss. The existing penalties for failure to submit income tax returns do not distinguish enough between greater and lesser delay and they are not related to the tax underpaid.

4.50 We envisage that if a self-assessed return is not submitted by the due date

- (i) the penalty would be, say, 5 per cent of the tax unpaid for each month, or part of a month, that the return is late unless the taxpayer can show reasonable cause for the delay,
- (ii) the maximum penalty would be limited to, say, 30 per cent of the tax unpaid, and
- (iii) there would be a fixed penalty of not less than, say, £100, if a return is more than two months late.

Interest should apply to late payments arising as a result of delays in submitting tax returns.

4.51 At present, penalties for failure to submit returns are imposed by the High Court by means of formal proceedings. The cumbersome nature of the proceedings is part of the reason why penalties are not used to enforce compliance. In Chapter 13 we recommend that the Revenue Commissioners should be given the power to assess and collect statutory penalties in the same way as tax, subject to a right of appeal.

4.52 A simple and streamlined approach along those lines would move the emphasis very firmly away from the use of estimated assessments as a means of obtaining basic information. The Revenue Commissioners would continue to have the power to make estimated assessments but, over time, this would become the exception and not, as now, the normal rule. The new system would rely on penalties which are both specific and automatic to secure compliance.

### Arrangements for Payment of Tax

4.53. In our first report, we recommended that Schedule D taxpayers should make four equal payments of provisional tax on or before 5 July, 5 October, 5 January and 5 April in the year of assessment. On the basis that self-employed persons paid 80 per cent of the liability ultimately found to be due, no interest should be payable. We suggested that the requirement of four equal instalments could be relaxed in the case of taxpayers, for example farmers, who can show that the bulk of their income accrues in the second half of the fiscal year.

4.54 Under a system of self-assessment, we consider that some changes are necessary to these arrangements. There should be three provisional payments during the tax year on 5 August, 5 December and 5 April. Interest at commercial rates should run from these dates on any underpayment (or overpayment) found ultimately to be due. The balance of tax together with any interest due should be remitted with the tax return on the due date for

the tax return. To avoid interest charges arising in every case, a *de minimis* provision or a tolerance factor should be built into the legislation.

### Checking and Auditing of Returns

4.55 An essential feature of self-assessment is a routine check of all returns and an in-depth audit of a sample of cases. The basis for such a system of checking and auditing already exists in Ireland. Because of the pressures on the assessing system and some doubts about the benefits of examining all cases in detail, the Revenue Commissioners in recent years have moved away from the traditional system of checking every entry in every account submitted. In 1977, instructions were issued to inspectors of taxes about a new system of examination of accounts of traders, partnerships and professionals. It was envisaged that there would be

- (i) a basic examination in all cases, and
- (ii) a critical examination where the basic examination indicated a need for a critical examination.

A critical examination would be carried out in any case where the basic examination revealed that the receipts had been understated, or the purchases overstated, or significant amounts in respect of cash introduced, or new loans received had not been satisfactorily explained.

4.56 So far, the Revenue Commissioners have not succeeded in implementing this scheme in full. The main reason why the scheme has not been fully implemented is that the volume of routine work generated by the assessing and appeal procedures has made it difficult to set up a programme of critical examinations. The latest attempt to launch the long-delayed second phase of the programme of examinations was made in June 1984. However, as long as inspectors of taxes are required to meet the twin targets of maintaining a programme of critical examination and assessing all taxpayers, this system is unlikely to be very effective.

4.57 Self-assessment would relieve inspectors of the routine work associated with the assessing and appeals procedures. The new system of examination of accounts could then proceed in a way in which the skills of inspectors of taxes would be directed away from purely computational matters into areas where they are most likely to achieve worthwhile results in terms of additions to profits brought into assessment.

### Enforcement

4.58 The Revenue Commissioners expressed the view that to counter the opportunities which self-assessment would provide to underpay tax, substantial deterrents would be necessary.

“In the United States the tax authorities have been given powers which, it may be thought, would not be acceptable here. Such powers include the imposition of severe and automatic penalties for not filing returns and by way of interest charges in respect of underpayments, free access to private homes, business premises and bank accounts (without the necessity for intervention by a Court) and, ultimately, imprisonment. The fear of penalties has such an impact in the United States that many taxpayers feel it necessary to have their tax affairs handled by agents, making the United States a ‘tax consultants’ paradise’ according to a United Kingdom observer when the introduction of self-assessment was last being considered in Britain.”<sup>12</sup>

4.59 The Revenue Commissioners concluded that, given the level of non-compliance in Ireland in the making of returns, the furnishing of information and the payment of tax, the introduction of a system of self-assessment of tax would, to be successful, need to be supported by draconian enforcement powers, most of which would have to be capable of being applied automatically without the intervention of the courts. If the Revenue Commissioners were not accorded such powers they argued, any system of self-assessment would undoubtedly adversely affect the tax yield from the self-employed.

4.60 Any system of assessment and collection requires that the authorities have effective methods of enforcement. We consider in Chapter 12 the enforcement powers of the Revenue Commissioners to enter premises, check taxpayers records and verify tax returns. It is not obvious from our review that a change to a system of full self-assessment would require any enforcement powers beyond those which are already largely in place. The changes we recommend in the powers of the Revenue Commissioners to collect outstanding taxes are necessary, irrespective of any change to self-assessment. As we noted earlier, the emphasis in the United States system is on detection and collection of the revenue and not on putting people in jail.

### Revenue Implications

4.61 There may be concern that any change to self-assessment for self-employed persons would result in a drop in revenue from this sector, unless and until penalties for non-compliance were shown to be effective. In 1983, Schedule D taxpayers (mainly the self-employed) paid £237 million in tax. Of this, £57 million was paid by building societies under the composite rate arrangement leaving a net £180 million paid by self-employed persons

<sup>12</sup>Material supplied at meeting with the Revenue Commissioners, 12 December, 1984.

as normally understood. This amounts to about 3 per cent of total tax revenue (including social insurance contributions).

4.62 The administrative costs of assessing and collecting this tax are very high. The staff involved contains a disproportionate number of the most highly trained revenue officials. We are confident that if these were redeployed from largely routine examination of the affairs of compliant taxpayers to a more critical examination of the affairs of defaulters, the odds are that tax collected from the self-employed sector would increase.

### **Treatment of Capital Gains and Capital Acquisitions**

4.63 The administration of capital gains tax is fully integrated with income tax administration. Taxpayers are required to include details of disposals and acquisitions on their income tax returns and the assessments are made by the local inspector of taxes.

4.64 The administration of capital acquisitions tax is centralised in the Capital Taxes Branch of the Revenue Commissioners and is located in Dublin. Centralised and separate assessment for capital acquisitions tax exists entirely as an historical accident. This system was suitable for assessment and collection of death duties. Following the change to the donee-based capital acquisitions tax, the existing system was let stand. A further major change was made in 1984. Lifetime cumulation of gifts and inheritances received on or after 2 June, 1982 by a donee from all sources is now aggregated to determine the amount of tax payable on the latest taxable gift or inheritance.

4.65 Our proposals take the integration of taxation of gifts and inheritances with other taxes even further. They come within our definition of income. Following the introduction of lifetime cumulation of gifts and inheritances, the administration of these taxes should no longer be divorced from the administration of income tax and capital gains tax. We consider that the work of the Capital Taxes Branch should be transferred to the Superintending Inspectors of Taxes. In addition to leading to a more rational organisation structure this change would strengthen the skill and experience of the Superintending Inspectors Branch in areas such as the administration of capital gains tax when our proposal to make death a disposal is implemented.

4.66 The donee of a gift or the successor to an inheritance is liable to deliver a return within three months of the gift or inheritance. No return is required where 80 per cent of the exemption threshold has not been exceeded. A return must be made on request by the Revenue Commissioners.

4.67 We recommend that individuals should be required to include gifts and inheritances received in their income tax return. Such receipts would then be subject to self-assessment by taxpayers who are within the ambit of self-assessment for income tax. Gifts and inheritances received by PAYE taxpayers could either be self-assessed or directly assessed by the Revenue Commissioners.

### **Conclusion**

4.68 The present system of Revenue-assessment is not working. Because of the time constraints involved, virtually all assessments must be made on an estimated basis in the absence of completed returns. Caution requires these estimates to be high. As a result, the system is deluged with appeals which are slow to clear. We do not believe that the 1983 changes in the appeals procedure will improve the situation. The changes which would make the system work satisfactorily include an extension of the due dates for payment of tax by the self-employed or choosing an earlier basis of assessment. These solutions are unacceptable on equity grounds.

4.69 We recommend that the existing system of Revenue-assessment be replaced by self-assessment. The Revenue Commissioners would continue to have the power to make estimated assessments but, over time, this would become the exception and not, as now, the rule. The new system would rely on audit of a small proportion of cases and on penalties which are both specific and automatic to secure compliance.

4.70 Self-employed taxpayers and companies already have to comply with many of the requirements of self-assessment. The most important element of self-assessment already incorporated into the administration of income tax and corporation tax is the onus placed on the taxpayer in appeal cases to specify an amount of tax which he considers to be due. However, to facilitate the introduction of the new system and to give taxpayers and the Revenue Commissioners familiarity and confidence with it, we recommend in the first instance that it be introduced for corporation tax. Compliance for corporation tax is higher and a greater proportion of corporate taxpayers employs specialist tax advisors. Also, companies are already taxed on the basis of income arising in an accounting period and the complexities of different bases of assessment do not arise.

### **Recommendations**

4.71 We make the following recommendations:

1. Self-assessment should be introduced for non-PAYE income tax, corporation tax and all other direct-assessment cases. It should be introduced for corporation tax in the first instance.

2. The introduction of self-assessment for income tax purposes would be facilitated if tax for the current year were charged on the basis of the income of the accounting period ending in that year.
3. Self-assessed taxpayers should make three provisional payments of tax at four monthly intervals during the tax year. Interest at commercial rates should run from these dates on any underpayment found ultimately to be due. The balance of tax together with any interest due should be remitted with the tax return on the due date for the tax return. To avoid interest charges in every case, a *de minimis* provision or a tolerance factor should be built into the legislation.
4. There should be a requirement for self-assessment returns for companies, including supporting accounts, to be submitted within six months of the end of the relevant accounting year. Trading taxpayers should be required to submit self-assessed returns within nine months of the end of the relevant accounting year or within three months of the end of the tax year, whichever is the later. Non-trading taxpayers should be required, under a system of self-assessment, to submit their tax returns within three months of the end of the tax year.
5. There should be an automatic late filing penalty for returns not received by the new revised filing dates, related to the amount of unpaid tax due and to the delay. There should also be a simple and automatic penalty for not making a return.

## CHAPTER 5

### WITHHOLDING TAXES

#### Introduction

5.1 In this chapter we consider the question of withholding taxes or deduction of taxes at source. PAYE, the most important withholding tax in Ireland, is dealt with separately in Chapter 6. However, there are other forms of withholding taxes and other income to which withholding taxes could be extended and these are examined.

#### The Issue in General

5.2 Deduction of tax at source has a long history. It was the essential element in Addington's scheme of 1803 which ensured the success of his income tax system over the earlier failures. The principle is now accepted and widely operated and includes PAYE, advance corporation tax, deduction of tax from interest on, for example, building society deposits and land bonds and deduction of tax from payments to sub-contractors.

5.3 Deduction of tax at source can have many advantages. For instance, it is a relatively simple matter for a company distributing income (wages and salaries, interest on bonds or dividends on shares) to deduct a standard rate of tax from all the payments. Although this involves the company in some compliance costs, the overall collection costs, both administrative and compliance are reduced. In other words, the costs to the company of acting as the tax collecting agent are smaller than would be the costs to the revenue service and individuals if they were to follow up each distribution. Withholding also reduces evasion.

5.4 Deduction of tax at source works best when applied under a single-rate tax system. This means that the number of calculations by individual taxpayers is greatly reduced, as is the number of settlements between the revenue authorities and taxpayers. In other words, the more that people are liable at a single rate, the more will withholding at the single rate turn out to be an accurate assessment of liability.

5.5 Hence, withholding is a very attractive principle under the system of taxation we have proposed, reducing overall costs and relieving most taxpayers of the drudgery associated with meeting their tax liability. It is particularly effective when operated in conjunction with a system of self-assessment. Under these circumstances, most taxpayers would have little or no compliance costs. Only those in more complex tax positions (for example, liable for income tax on capital gains or liable for expenditure tax) would have to go into detail about their liability and make a balancing settlement with the tax authorities after the close of the fiscal year. Even in these cases, the tax withheld and the details of income would be easily accommodated in the final calculation and settlement.

5.6 We also feel that wide-scale deduction of tax at source has the important side-effect of establishing public support for revenue enforcement efforts. Compliant taxpayers tend to demand efforts to ensure compliance from other taxpayers. There are some administrative implications, notably, resources must be devoted to ensuring that those who are charged with deducting tax at source do so and promptly remit tax deducted to the Revenue Commissioners. Another critical element in any system of deduction at source is that excess amounts withheld are refunded quickly.

5.7 We consider that deduction of tax at source should be extended as much as possible. In the rest of this chapter we examine some existing schemes of deduction at source (other than PAYE, which is dealt with in Chapter 6) and consider areas to which the system might be extended.

#### **Withholding by Income Source — An Overview**

5.8 The main types of income (other than wages and salaries) which are at present subject to deduction of tax at source are the following:

- (i) income chargeable under Schedule C, that is, interest and dividends out of any public revenue payable in Ireland and certain foreign dividends,
- (ii) building society interest,
- (iii) dividends paid by Irish resident companies,
- (iv) sums paid for the purchase of a capital asset where the vendor does not have a capital gains tax clearance certificate issued by the Revenue Commissioners, and
- (v) monies paid to certain subcontractors in the construction industry.

All of these schemes for withholding tax on income could be integrated into a general system of withholding at the single rate under our proposals. The scope of some of the schemes could be extended to other similar income.

#### **Government Securities**

5.9 Income tax is charged at the standard rate under Schedule C on persons entrusted with the payment of 'public revenue dividends' and certain foreign dividends. Such persons are usually banks or paying agents. 'Public revenue dividends' include dividends, interest and annuities payable out of the public revenue of any government and the revenue of any foreign public authority or institution.

5.10 The paying agent or bank at which the dividend is presented for encashment generally deducts tax at the standard rate from the amount of the dividend or interest received in Ireland. For example, in the case of foreign dividends the paying agent will generally deduct tax at 35 per cent on the amount of the dividend, net of foreign tax. However, British treasury stock is an exception as the tax is deducted on the gross amount.

5.11 Interest on Irish government securities issued under the authority of the Minister for Finance is excluded from the charging provisions of Schedule C and is thus paid in full. Interest on securities of certain state-sponsored bodies including Aer Lingus, the Agricultural Credit Corporation, the Electricity Supply Board and Córas Iompair Éireann are also exempt from withholding.

5.12 The existing arrangements for taxation of income from Irish government and certain other securities are unsatisfactory and should be changed. Holders of these securities do not have the effects of inflation taken into account for income tax purposes. Problems arise in making changes in the tax treatment of existing securities due to undertakings in prospectuses, even where these would favour certain holders. In our first report, we recommended<sup>1</sup> that allowance be made for inflation by making all new government securities chargeable assets for capital gains tax purposes. The annual returns from the asset should therefore be charged to tax in full as they arise. We recommend that interest payable to Irish residents on all new government securities be payable under deduction of tax.

#### **Deposit Interest**

5.13 In our first report, we recommended<sup>2</sup> that the income from all interest-bearing deposits should be charged to tax to the extent only that the rate at which it accrues exceeds the rate of inflation during the period of accrual. In so far as the interest earned is insufficient to compensate for the erosion of the capital value of the deposit, the shortfall should be

<sup>1</sup>Paragraph 13.54.

<sup>2</sup>Paragraph 11.15.

allowed against other income. In this report we consider how to implement this recommendation within a scheme of deduction of tax at source.

5.14 At present, tax on interest payable by building societies is collected under an arrangement between the societies and the Revenue Commissioners under Section 31 of the Corporation Tax Act, 1976. In our first report, we referred<sup>3</sup> to certain unsatisfactory features of the composite rate arrangement and we recommended that it should be terminated and the tax treatment of interest on building society deposits be aligned with that accorded to other interest-bearing deposits.

5.15 We recommend that the inflation adjustment on all interest bearing deposits with financial institutions be made on an aggregate basis. This is the only effective and efficient method of doing so. The method we envisage for doing this is best illustrated by an example.

#### Example

Assuming an average rate of interest of 6.25 per cent by the Associated Banks on deposits under £5,000 and average inflation of 5 per cent, the real income from deposits would be 1.25 per cent on average. The tax on this at the single rate, say 30 per cent, would amount to 0.375 per cent. Therefore, the Associated Banks would pay to the Revenue Commissioners 0.375 per cent of the value of deposits under £5,000. No further tax liability would arise on this interest for the vast majority of taxpayers.

5.16 The position in relation to building societies would be as follows. The average rate of interest on share accounts in building societies in 1984/85 was 7.4 per cent net which is equivalent to 11.4 per cent gross. With average inflation at 7.6 per cent in 1984/85 the tax properly due on this income is 3.8 per cent at, say, 30 per cent or 1.14 per cent. Therefore, the building societies would pay to the Revenue Commissioners 1.14 per cent of the value of their shares and no further income tax would be due on building society interest. At the rates of interest and inflation in 1984/85, this would result in a substantial reduction in taxation on building society interest which could be reflected in lending rates.

5.17 The issue arises how non-liable taxpayers should be treated under this procedure. We consider that the Revenue Commissioners should repay the tax deducted to persons not liable for tax.

5.18 Another issue which arises is whether or not this procedure should apply to non-resident accounts. Under double taxation agreements, deposit

<sup>3</sup>Paragraph 11.39.

interest is generally taxed only in the country of residence of the depositor and under the existing reporting arrangements, the Associated Banks and other deposit taking institutions are not obliged to make returns of interest payable to non-resident account holders. In principle, we think that non-residents should be excluded, since if tax were deducted it would have to be repaid in certain instances, which would only increase administrative costs. At a practical level, if non-residents are not excluded they are unlikely to invest their money in Ireland anyway, unless the real rate of return is exceptionally high.

5.19 There is concern that the exclusion of non-resident accounts from existing reporting requirements is being abused by residents masquerading as non-residents. We do not think that bringing non-resident accounts within the scope of deduction of tax at source is the solution to any problem of abuse. Firstly, the application of the deduction of tax to the real gain reduces substantially the incentive for residents to try to achieve non-resident status for their holdings. Secondly, the depositor must now sign an affidavit as to his residence if the bank is not satisfied with the *bona fides* of a declaration of non-residence. Thirdly, we consider that rules, properly made, should be enforced rather than replaced, thus avoiding the penalisation of legitimate non-resident investors whose funds could be useful for Irish business and employment. For these reasons we recommend that no change should be made in the treatment of non-resident accounts.

#### Distributions

5.20 Distributions (usually of dividends) made by a resident company are not subject to deduction of tax at source but do qualify for appropriate tax credits. However, the 1983 advance corporation tax will ensure, at the end of the transitional period, that there is effective deduction of tax at source by the company.

5.21 Where a dividend is paid by a resident company, part of the corporation tax on the income underlying the distribution is imputed to the recipient by way of a tax credit. The tax credit normally amounts to 35/65ths of the distribution. Special arrangements relate to companies liable to tax at the rate of 10 per cent applicable to manufacturing companies.

5.22 An individual resident in Ireland is liable to income tax (under Schedule F) on any distributions received from a resident company. This liability is on the aggregate of the distribution and the tax credit but the tax credit is set against the income tax due. Where the shareholder is liable to income tax at a higher rate than the amount of the credit, the tax credit is deducted from the tax payable. A shareholder who is not liable to tax or is liable at a rate less than the amount of the credit may claim payment of all or part of the tax credit as appropriate.

5.23 Where a resident company makes a distribution on or after 9 February, 1983, it is liable to pay advance corporation tax (ACT). The amount of the ACT is, subject to transitional relief, equal to the tax credit attaching to the distribution.<sup>4</sup> ACT on distributions made on or before 31 December, 1985 will be reduced to 50 per cent. The example below illustrates the operation of ACT.

#### Example

If a company pays a dividend of £6,500, the tax credit attaching to the dividend is 35/65ths, which amounts to £3,500. The company will as a result have a liability to ACT of £3,500.

5.24 ACT paid by a company can be set off, in so far as is possible, against the company's corporation tax liability for the accounting period in which the distribution is made. It can, however, only be set off against corporation tax on the company's income and not against corporation tax arising on the company's capital gains. Any surplus ACT may be set off against corporation tax on the company's income of an earlier accounting period (ending within the previous twelve months) or carried forward and set against corporation tax on future income.

5.25 Under our proposals the single rate of tax would apply to personal and corporate income, including capital gains. The rate of imputation would be 100 per cent of the underlying corporation tax. In these circumstances, ACT would be an effective withholding tax on all company distributions which would meet the tax liability on dividend income for all shareholders not liable to expenditure tax.

#### Capital Gains

5.26 On the sale of certain assets after 5 April, 1978, the person by or through whom the payment is made is obliged to withhold capital gains tax at 30 per cent on half the sale proceeds and pay it over to the Revenue Commissioners. The obligation to deduct tax applies only on the disposal of certain specified assets, such as land and buildings and there is no need to deduct tax unless the sale price exceeds £50,000. The scheme is basically designed to collect tax in the case of a non-resident where later collection may be impossible. Irish residents may apply to the Revenue Commissioners for a clearance certificate which will enable the proceeds to be paid without deduction of capital gains tax. The certificate is normally issued solely on the grounds of Irish residence. Non-residents may apply

<sup>4</sup>There is also provision to set off tax credits on distributions received by the company against the ACT due on distributions made.

for a clearance certificate on the grounds that there is no liability or that the tax has been paid.

5.27 It is obvious that this is not a general scheme of withholding but a means of dealing with a particular collection problem. The sale price of an asset does not give any indication of the gain or indeed the loss arising on the disposal of the asset. Indexation is a further complication in arriving at the chargeable gains. These difficulties would continue to exist under our proposals. We do not therefore envisage any general scheme of withholding on the sale proceeds of assets to meet income tax liabilities on possible gains.

#### Gifts and Inheritances

5.28 We recommended in our first report that gifts and inheritances should be subject to the single rate of tax. We hold different views on whether there should be an exemption threshold for tax purposes and if so how much it should be. We agree, however, that the existing threshold for immediate relatives should be substantially reduced in the context of our proposals and the number of classes of consanguinity reliefs should be reduced. We also recommended that the problem of financing payment of tax where the amount of liquid assets is relatively low, or where the assets are not readily realisable, should be dealt with through insurance schemes and more liberal arrangements for payment of tax by instalments.

5.29 In principle, we favour a withholding tax on gifts and inheritances since these would form an important new part of income as we define it. Taking, first, inheritances which are likely to give rise to fewer difficulties, executors could be accountable for payment of tax before inheritances are distributed. Inheritance thresholds could be dealt with as repayment claims by the beneficiary on the Revenue, except in cases where it would be onerous to pay the tax by deduction. In these cases it should be possible to have the beneficiary and the executor agree an assessment with the Revenue Commissioners.

5.30 Where the beneficiary would wish to receive the inheritance and to be accountable himself for the taxation, for example, in the case of an inheritance of a farm or business, it seems possible to us that the Revenue Commissioners' consent could be obtained in cases where deferred payment arrangements were acceptable or beneficiaries could provide the executors with cheques in settlement for forwarding by the executors to the Revenue Commissioners.

5.31 In so far as gifts are concerned, we believe that the same procedures could be pursued substantially, except where the gift could not be transmitted to the donee without the donor having to use other financial resources

to make the payment. A withholding tax on gifts is not likely to reduce the number of persons accountable for payment of tax but the donor is more likely to ensure that tax is paid.

5.32 We conclude that withholding tax on gifts and inheritances should operate as widely as possible. The difficulties which arise could be resolved by treating the issues of thresholds as a matter for monetary settlement between the Revenue Commissioners and the beneficiary and by separating the treatment of assets which are not readily realisable so that these are dealt with by exception. Special treatment may also have to apply to certain gifts.

### CONSTRUCTION INDUSTRY SCHEME

5.33 There are special rules relating to deduction of tax from payments made to self-employed sub-contractors in the building industry. Principal contractors must deduct tax at the rate of 35 per cent from such payments and remit this tax to the Collector General, unless the sub-contractor produces a certificate issued by the Revenue Commissioners authorising the receipt of the amount without deduction of tax. This scheme is designed to deal with the particular problems of collecting tax and controlling evasion in the construction industry. Full details of the tax deduction scheme are in Appendix 1.

5.34 A submission from the Construction Industry Federation referred to "the extremely complex requirements of the sub-contractor's legislation. The amount of detail which must be recorded and checked with regard to each sub-contractor is astonishing when multiplied by many hundreds of sub-contractors. Due to the structuring of the legislation even a small error can involve a contractor in substantial penalties or tax liabilities. Even though the sub-contractor involved may have accounted for the tax already the company is still liable for the penalties or tax. Simplification of this complex system would boost the efficiency of the industry and would reduce the amount of money spent by the government in administering the system."

5.35 Other issues which arise in considering the tax deduction scheme in the construction industry are

- (i) whether there should be an appeal against a refusal by the Revenue Commissioners to issue a certificate,
- (ii) the rate at which tax should be deducted under the scheme, and
- (iii) whether the deduction scheme should be extended to other sectors.

5.36 We asked the Revenue Commissioners for their views on the operation of the scheme and particularly whether the scheme could be simplified to reduce compliance costs. They replied that

"the scheme of tax deduction from sub-contractors in the construction industry was introduced in 1971 to deal with large-scale evasion of tax. It was revised in 1976 with some further minor revisions in 1981. The scheme operates satisfactorily. It is reasonably simple and there are adequate explanatory leaflets. Further simplification could only be at the risk of increasing evasion. The deduction of tax is only at the standard rate so there is no question of it being a penal system".<sup>5</sup>

5.37 Prior to the introduction of the scheme, there was widespread tax evasion in the construction industry. Experience prior to 1976 suggests that this can only be controlled by using very stringent controls. For this reason, we cannot recommend any relaxation in the existing arrangements.

### Appeals

5.38 As we noted earlier, there is no appeal from a decision by the Revenue Commissioners to refuse to issue a certificate to a sub-contractor entitling him to receive payment in full.

5.39 The Revenue Commissioners said that

"there should be no appeal against this refusal to issue a certificate allowing payment without deduction of tax. This would be inappropriate since there is no appeal against deductions under PAYE and the sub-contractors' scheme is, like PAYE, a system of payment of tax".<sup>6</sup>

5.40 The lack of an appeal procedure may perhaps be justified on the basis that it is very difficult for an independent tribunal to assess whether the Revenue Commissioners are correct in believing that there is good reason to expect that the applicant will not keep proper records in the future. This can only be objectively determined with hindsight.

5.41 As against this, the powers conferred on the Revenue Commissioners under this legislation are very wide. An individual's livelihood may depend on whether he qualifies for a certificate or not. It is important, therefore, to have procedures to ensure that these powers are exercised in a reasonable way. We recommend that provision be introduced to enable appeals to be made to the Appeal Commissioners and the courts against a refusal by the Revenue Commissioners to issue an exemption certificate under the scheme.

<sup>5</sup>Agreed note of meeting with the Revenue Commissioners, 12 December, 1984.

<sup>6</sup>Agreed note of meeting with the Revenue Commissioners, 12 December, 1984.

## Rate of Tax

5.42 The effective rate of tax due on any gross payment to a sub-contractor varies widely and is difficult to estimate with precision in advance. It will depend, for example, on whether the sub-contractor supplies materials or not, whether or not he has employees and the level of taxation generally, both income tax and value-added tax. Clearly, any single rate of tax deduction will give rise to some underpayments of tax and substantial overpayments in certain cases. It is imperative in these circumstances that refunds be made promptly. The existing arrangements for monthly refunds are reasonable and we recommend no change. In the context of our general scheme of taxation, tax should be deducted at the single rate. In the meantime, we recommend that the rate of tax deduction be tied to the standard rate.

## OTHER SECTORS

5.43 Before a deduction scheme could be extended, in whole or in part, to other sectors, the following conditions should be satisfied:

- (i) assessment and collection of tax from that sector should be operating unsatisfactorily under existing arrangements,
- (ii) the ratio of value-added to gross turnover should be reasonably high,
- (iii) accountable persons should already be required to keep records and be reliable, and
- (iv) there should be fewer accountable persons than taxpayers.

5.44 The Revenue Commissioners said that

“while collection of tax in the entertainment and other industries is very unsatisfactory, there are very few areas in which deduction schemes could be introduced in practice. One possible area is payment to non-residents in connection with sporting or entertainment events.<sup>7</sup>”

5.45 We recommend that the extension of deduction schemes to areas which meet the criteria in paragraph 5.43 be kept under review. However, we make no specific recommendations.

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<sup>7</sup>Agreed note of meeting with the Revenue Commissioners, 12 December, 1984.

## Recommendations

5.46 We make the following recommendations:

1. In principle, deduction of tax at source should be extended as much as possible.
2. Interest payable to Irish residents on all new government securities should be payable under deduction of tax once these securities have been made chargeable assets for capital gains tax purposes.
3. Inflation adjustment for tax purposes on all interest-bearing deposits by Irish residents with financial institutions should be made on an aggregate basis.
4. The existing construction industry scheme should be retained, subject to a right of appeal to the Appeal Commissioners and the courts against a refusal by the Revenue Commissioners to issue a certificate of exemption from deduction of tax for payments made under construction contracts.
5. The rate of deduction of tax from payments under construction contracts should be tied to the standard rate.
6. The extension to other areas of schemes of deduction of tax which meet the criteria set down in paragraph 5.43 should be kept under review.

## CHAPTER 6

### PAYE

#### Introduction

6.1 In this chapter we consider withholding of tax on wages and salaries under PAYE. In recent years, the system has become more complicated. This has increased the burdens on employers and on the Revenue Commissioners as well as reducing the quality of service to taxpayers. There is a great need to simplify the system and this would be possible under our proposals. In these circumstances we believe there is a strong case for continuing PAYE on a cumulative basis. This would ensure that most wage and salary earners would have their tax liability collected in full by their employers during the tax year without the need for a review and a final settlement after the end of the tax year. The historical background to the introduction of PAYE in Ireland and the main features of the system are in Appendix 2.

#### Main Features of Present System

6.2 The distinguishing characteristics of the PAYE system are

- (i) a 'cumulative' system of deductions designed to ensure that the employee's tax is calculated on each pay day on the basis that his income will be received until the end of the tax year at the same rate as it has been received since the start of the tax year and taking account of total tax deducted already in the year, and
- (ii) the main responsibility for operating the scheme falls on employers and the Revenue Commissioners.

6.3 The Irish PAYE system incorporates three important features for deducting tax from wages and salaries which tend to distinguish it from systems in other countries (except that of the United Kingdom). Firstly, in many cases an end of the year adjustment of liability is unnecessary and is not carried out. Secondly, the need to amend certificates of tax-free allowances, to keep current tax deductions tuned to the individual taxpayer's circumstances as they develop, calls for frequent contact between

the tax office and the employer. In general, the employees of a particular employer are dealt with by the same tax office, irrespective of where they live or work. It follows that when an employee changes his job, he more often than not changes his tax office too. Thirdly, the system tends to be more expensive for employers to administer than other systems and, for the same reasons, cheaper in terms of compliance costs for employees.

6.4 Over the last ten years the administration of PAYE has become more complex. Table 6 shows that the number of complicating factors per case more than doubled between 1973 and 1980 and has risen by a further 15 per cent since then.

TABLE 6  
Complicating Factors in PAYE

	1973	1980	1984
	000s	000s	000s
Total Live Employments	901.2	1,190.3	1,146.8
Reliefs Granted <sup>1</sup>	989.6	1,468.4	1,444.8
Non-PAYE Income Coded <sup>2</sup>	55.4	137.1	164.4
Table Allowances and Exemptions	119.8	585.7	415.5
PAYE and PRSI Allowances	Nil	1,014.7	1,523.3
Total Complicating Factors	1,164.8	3,205.9	3,548.0
Complicating Factors per Case	1.18	2.69	3.09

Source: Revenue Commissioners.

#### Notes:

<sup>1</sup>Reliefs include interest, expenses, life assurance etc.

<sup>2</sup>Income assessed under Schedule E, investment income, farm profits etc.

As a result of these complicating factors there has been an increase in the number of amended certificates of tax-free allowances required in the course of the year, thereby creating more work for employers and the Revenue Commissioners. The number of complicating factors has also increased the number of end-of-year reviews of liability which the Revenue Commissioners have to undertake. This has increased compliance costs for a rising number of PAYE taxpayers who find that the correct amount of tax is not deducted from them.

6.5 The net result of this is shown in Table 7 which indicates the growth in the volume of work generated by changing circumstances and added complexity.

**TABLE 7**  
**Indicators of Volume of Work in PAYE**

Year ended April	1973	1980	1984
	000s	000s	000s
Unemployment Repayments	31.3	52.8	72.3
Reviews (Underpayments and Overpayments)	149.3	335.3	333.9
Total	180.6	338.1	406.2

6.6 The volume of work can also be judged from the fact that it is necessary to send out over 768,000 amended certificates of tax-free allowances to employees and over one million copy certificates and amended tax deduction cards to employers each year. In the year to April 1984, 333,899 reviews of liability represented 35 per cent of live main employment cases. These reviews covered 474,076 tax years, as some reviews covered more than one year. This suggests that about 50 per cent of PAYE cases in any year require adjustment.

6.7 The increasing inability of the PAYE system to ensure that the correct deductions are made is shown by the rise in the average repayment of tax from £19.70 in 1973 to £102.30 in 1980 — an increase of 50.1 per cent in real terms.

6.8 The Revenue Commissioners told us<sup>1</sup> that on the basis of an examination which was last done on 1979/80 figures, it would be advisable from the revenue standpoint to review about 50 per cent of cases. In the district check computer programme, which is a type of review by computer process done twelve to fourteen months after the end of the tax year, lists are produced categorising cases under different headings. Of these, four types are regarded as meriting review of liability:

- (i) suspected undercharges greater than £20,
- (ii) cessations and changes of job,
- (iii) subsidiary employment cases where the tax-free allowances are allocated between employments, and
- (iv) cases in which the deductions were not wholly cumulative (week 1/month 1 basis).

All these cases are the subject of monthly reports by each district to the Superintending Inspectors of Taxes.

6.9 Many taxpayers request that their liability be reviewed. While separate

<sup>1</sup>Letter of 30 November, 1984.

statistics are not kept for each of the two types of review, that is, those initiated by the inspector of taxes and the taxpayer, it is estimated that about 30 per cent of the reviews being done are initiated by the inspector of taxes.

6.10 The Revenue Commissioners summarised the position for us as follows:

“When PAYE was introduced on 6 October, 1960 it was intended that each case would be reviewed annually. There was far less need to do a review in those earlier years as PAYE deductions in many cases equated with true liability due to the single rate of tax applicable and the less complex system of allowances and reliefs. While the district list computer programme highlights the cases which should be reviewed in the Revenue interest, the bulk of reviews actually done are not those initiated by the Inspectors because of the increasing number of requests for a review received from taxpayers, in the context of diminishing staff resources”.<sup>2</sup>

### Effects of Our Proposals

6.11 Implementation of the recommendations in our first report would greatly simplify the administration of PAYE. Simplification would result in particular from the following proposals:

- (i) the application of a single rate of income tax to all income arising in the personal and corporate sectors,
- (ii) the removal of nearly all exemptions and deductions from income for tax purposes,
- (iii) the replacement of social insurance contributions by a social security tax which has the same tax base as income tax and would work in the same way, and
- (iv) the imputation in full of tax paid at the company level to the shareholder when distributions are made out of company profits.

6.12 The new scheme would consist only of allowances in respect of Schedule E expenses and personal allowances in the form of a tax credit. Under such a new system the tax-free allowance could be determined at the beginning of the year. Changes in the flat rate expenses agreed with the Revenue Commissioners and changes in tax credits by reference to indexation or budget changes could be handled automatically by computer.

6.13 In Table 8 we estimate the complicating factors in PAYE under the

<sup>2</sup>Letter of 30 November, 1984.

new system compared with that in the year ended April, 1984. The effect would be to reduce these to one quarter of their present level.

**TABLE 8**

**Complicating Factors in PAYE compared with Proposed System**

	1984	Proposed System
	000s	000s
Reliefs Granted	1,445	636
Non-PAYE Income Coded	164	155
PAYE and PRSI Allowance	1,523	Nil
Table Allowances	400	94
Exemptions (incl Marginal Relief)	16	Nil
Total PAYE Allowances, Reliefs and Coded Income.	3,548	885

Source: The 1984 figures were supplied by the Revenue Commissioners.

It is clear that the effects would be

- (i) reduced administrative and compliance costs arising from routine operation of PAYE,
- (ii) improved standards of service, and
- (iii) scope for redeployment of official resources to tackle evasion.

**OTHER ISSUES**

6.14 We now turn to examine a number of other issues in relation to PAYE. These are

- (i) the introduction of a non-cumulative system of PAYE, and
- (ii) self-assessment for PAYE taxpayers.

**Non-cumulative System**

6.15 The system of PAYE operated in Ireland (and the United Kingdom) is cumulative. Under the cumulative system, the employee's liability to income tax on any pay-day is calculated on the difference at that date between

- (i) total net pay to date since the start of the income tax year (cumulative pay), and
- (ii) total accumulated tax-free allowances to date since the start of the income tax year (cumulative tax-free allowances).

Other countries operate a non-cumulative system under which there is no carry-forward of pay or allowances from one period to another. However,

the cumulative PAYE system is more than just a means of spreading allowances; it is designed to withhold the correct tax on wages and salaries during the tax year.

6.16 In theory, a cumulative system is fairer because it should succeed in collecting the correct tax in the vast majority of cases. However, as we have already seen, the present cumulative system meets this test very badly in that it is necessary to adjust the liability in half the cases at the end of the year and ideally the Revenue Commissioners would like to review more. Thus, the number of cases requiring adjustment under a non-cumulative system is unlikely to be very much greater than is required now, so the loss in equity would not be significant. If we were considering the administration of the existing tax system only, a cumulative PAYE system would not have significant advantages on equity grounds over a non-cumulative system.

6.17 Our proposals for reform of income tax involve considerable simplification of the system. As noted in paragraph 6.13, these would bring a big reduction in the number of cases requiring end of the year adjustment under a cumulative system. The number of adjustments under a non-cumulative system would also be less than is required now but a cumulative system would have a bigger advantage than under present arrangements. There is one complication, however. Even under our proposals, it is always going to be difficult to include short-term social welfare benefits in the tax base under a cumulative system, eroding the equity advantages of this system over non-cumulation.

6.18 A non-cumulative system would be simpler and cheaper to operate during the course of the year for the Revenue Commissioners. One great advantage would be that there would be no further need for the 'movements system'. The present system of movements is a very cumbersome procedure required when an employee changes jobs. It revolves around the cessation certificate (form P45) which has four parts containing information (in quadruplicate) about the pay and tax deducted to date in the tax year and the tax-free allowances to which the employee is entitled.<sup>3</sup> If the former employer, the employee, the new employer or either tax office fails to play its part on time the movements system breaks down and the employee is charged to tax on the emergency basis until his affairs are put in order.

6.19 The number of cessations of employment each year varies with the level of economic activity. In the year ended April, 1984 it was almost

<sup>3</sup>Part 1 is a notification to the inspector of taxes. Parts 2 and 3 are in most cases given by an employee to a new employer who retains part 2 and sends part 3 to the tax office as a request for a certificate of tax-free allowances or tax deduction card. Part 4 is for use in claiming unemployment benefit from the Department of Social Welfare.

287,000 compared with over 438,000 four years earlier. In a tax district dealing with PAYE, the work on the movements system alone occupies a significant percentage of total staff resources. Also, the difficulties of the movements system has been the principal administrative problem in relation to any proposal to include short-term social welfare benefits in the tax base. Unemployment would be regarded as a commencement and cessation under the PAYE regulations. The abolition of the movements system would greatly simplify the operation of PAYE and would considerably lessen the administrative problems in relation to the inclusion of short-term social welfare benefits in the tax base.

6.20 Under a non-cumulative system, the link between employers and the Revenue Commissioners would be broken. The Revenue Commissioners would notify employees of their tax-free allowances and employees would have to notify their employer. This would require a system like the old social welfare cards which were surrendered to employees when they left an employment. Non-cumulation would eliminate the need to restore cumulation after a breakdown in the P45 series of procedures, which is expensive to put right. Employers, particularly those with computerised payrolls, would not welcome receiving instructions from employees in a haphazard fashion, compared with the present system where they receive them *en bloc* from the tax office and in a readily transcribable form.

6.21 A non-cumulative system would mean considerable re-organisation of work for the Revenue Commissioners at the end of the year. Under the present system the employer's end of the year return of what he has paid his employees and the amount of tax he has in each case deducted are linked with the employees' files and, where necessary, compared with the employees' tax returns. In Ireland, because the employer's tax office in the majority of cases deals also with the affairs of all his staff, this job of 'matching' is relatively easy. In other countries which do not have this link between the employer and the tax office, the 'matching' is often a considerable problem.

6.22 To summarise, a cumulative system is more complicated to operate than a non-cumulative system. However, it should result in the correct amount of tax being deducted in a greater number of cases than a non-cumulative system. A non-cumulative system would tend to result in overpayments of tax in the following cases:

- (i) those who commenced employment for the first time after the start of the tax year, or permanently ceased employment before the end of the year,
- (ii) those who qualified for additional deductions during the course of the tax year, and

- (iii) those whose income fluctuated considerably over the tax year.

The number of overpayments would be very much reduced under a system with relatively low tax thresholds, a long band of income chargeable at a standard rate and relatively few reliefs and deductions such as the system we proposed in our first report. Nonetheless, end-of-year reviews and final settlements would be necessary.

6.23 The choice between the cumulative and non-cumulative systems of PAYE is finely balanced. The closer the system approaches that outlined in our first report, the greater is the advantage of the cumulative system. We have now the worst of both worlds; all the extra costs and complexity of a cumulative system and little of the benefits of fewer end of the year adjustments of liability. The greater the weight that is attached to the need to bring short-term social welfare benefits into the PAYE system the stronger is the case for a non-cumulative system.

#### **Self-Assessment for PAYE Taxpayers**

6.24 Self-assessment for PAYE taxpayers could take a number of forms but the most sensible and efficient would involve provisional deductions from wages or salary on a non-cumulative basis during the year, with a settling up with the Revenue Commissioners after the end of the tax year. The essential features of self-assessment would therefore be

- (i) determination of tax-free allowances by taxpayers themselves and notification of tax-free allowances to employers by taxpayers,
- (ii) employer deductions during the year on a non-cumulative basis, and
- (iii) completion of annual returns by all taxpayers together with payments of final instalments of taxes due or claims for refunds. Employers would also be required to submit to the Revenue Commissioners details of pay and tax deducted for all employees.

6.25 Under a system of self-assessment, the Revenue Commissioners would cease to be involved with taxpayers and employers during the tax year. Instead, they would concentrate on the one million or so self-assessment returns. This operation would involve some relatively simple checks on arithmetical accuracy (preferably by computer), the internal consistency of the information supplied and the correct enclosure of supporting documents. There would also be an in-depth audit of a small number of cases at a later stage.

6.26 Self-assessment may provide a way of achieving significant cost savings in the administration of the tax system by allowing the Revenue Commissioners to withdraw from the day to day administration of the

PAYE system and to concentrate its resources mainly on the end-of-year adjustments and audits. Advocates of self-assessment point to the comparisons which have been made between the relative costs of collection of income tax in the United States and in the United Kingdom where the income tax system closely resembles the Irish system. The relative administrative costs of collection in the United States with a self-assessment system have been estimated to be under half the costs in the United Kingdom and Ireland.

6.27 The scope for cost savings within a self-assessment system derives not from the self-assessment process itself (which would, in fact, create greater end-of-year work) but from the other changes in the PAYE system which would reduce the Revenue Commissioners' involvement with taxpayers and employers to low levels during the course of the year. However, our proposed simplified system of direct taxation would provide most of these savings independently of a change to self-assessment.

6.28 Traditionally, PAYE taxpayers have had little involvement in the calculation of their tax liabilities. Most of the work is done either by the Revenue Commissioners or by the employers. In practice, the vast majority of PAYE taxpayers no longer has to complete an annual return of income, though the legal obligation to do so remains. The degree of active participation by the individual taxpayer is limited to keeping the Revenue Commissioners informed of changes in circumstances affecting his tax-free allowances. His role is thus, largely, a passive one. Any move towards self-assessment would involve the taxpayer in the calculation of his own liability and would increase the compliance costs of PAYE taxpayers.

6.29 The case of self-assessment for PAYE taxpayers in Ireland must be judged on the scope for a reduction in the overall cost of administration of the tax system, including the compliance costs of taxpayers and their employers. The scope for such a reduction in costs must be measured against the costs under our proposed system of direct taxation and not against existing costs. Under our proposals, major benefits would flow from increased simplicity. The integration of income tax and social security tax would reduce compliance costs, particularly for small businesses. The collection of PAYE would be a simple and straightforward matter with no need for end-of-year reviews, save in exceptional cases. Against this background, a move towards self-assessment is unlikely to lead to further significant costs savings. Indeed it is possible that self-assessment would result in a higher overall cost. The overriding consideration in deciding the nature of the tax administration is that the total cost of the system, including private compliance costs, should be kept to a minimum. Where a choice has to be made between two systems of equal overall cost, we would favour the system which places the lower burden in terms of private compliance costs on taxpayers and their employers. In the circumstances,

we do not recommend the introduction of self-assessment for PAYE taxpayers but this should be kept under review. Any decision to change to a non-cumulative PAYE system would change the balance of the argument in favour of self assessment.

6.30 Under the general system of self-assessment we recommended in Chapter 4, some wage and salary earners with income from other sources would be obliged to complete a self-assessment return form. These would be taxpayers with income not subject to withholding at the single rate. Sources of income such as deposit interest would be subject to a withholding tax which would satisfy the liability in most cases. Tax on small amounts of untaxed non-PAYE income could be collected through the PAYE system by reducing the personal allowances by the amount of income. Self-assessed PAYE taxpayers would be obliged to include capital gains and capital acquisitions in their returns and calculate their own liability: gifts and inheritances received by other PAYE taxpayers and capital gains could either be self-assessed or directly assessed by the Revenue Commissioners.

### Conclusion

6.31 The present system of PAYE on a cumulative basis has run into so many problems under the existing tax code that it has lost many of the advantages over a non-cumulative system. The number of reviews imposes high costs on the Revenue Commissioners and employers, there are delays and taxpayers get poor service. If this situation were to continue we would recommend a change to a non-cumulative PAYE system, with a final settlement after the end of the tax year.

6.32 However, many of the complicating factors of the present code would disappear with the adoption of our previous recommendations on income taxation. In these circumstances we feel there would be a strong case for continuing PAYE assessment on a cumulative basis. The compliance costs for many individual taxpayers would be reduced, in fact most wage and salary earners would have their tax liability collected in full by their employers. For wage and salary earners with other sources of income than those recorded through the PAYE system, the same PAYE record would fit in well as part of their income tax return under the general self-assessment system we recommend.

### Recommendation

6.33 We make the following recommendation in relation to the operation of PAYE:

1. In the context of the general scheme of taxation in our first report, the present cumulative system should be retained. However, if our

proposals are not adopted, the case is more finely balanced and the Revenue Commissioners should review and publish the arguments for and against a change to a non-cumulative system of PAYE.

## CHAPTER 7

### TAX APPEALS

#### Introduction

7.1 In Chapter 4 we described the present appeal procedure and we noted that the system is overburdened by cases concerning delay in the submission of returns and accounts. This makes it difficult to allocate sufficient time to hear technical argument appeals. In this chapter we consider the operation of the appeals system under self-assessment. We also examine certain aspects of the machinery for dealing with appeals and we make recommendations for change.

#### Appeals under Self-assessment

7.2 At present almost 90 per cent of assessments are appealed and in 1984 more than 36,000 appeals were considered by the Appeal Commissioners. Self-assessment would greatly relieve the pressure on the appeals system. Most self-assessment returns would be accepted by the Revenue Commissioners after a routine check only; appeals would not arise in such cases. The Revenue Commissioners would continue to have the power to make estimated assessments but, over time, this would become the exception and not, as now, the normal rule. Under self-assessment, appeals would be largely confined to cases selected for investigation where there is a dispute between the inspector of taxes and the taxpayer about the tax liability. The appeal process would then become a proper dispute procedure under which the taxpayer could complain to an independent tribunal and the Appeal Commissioners would have the time to consider fully the arguments presented.

#### Appointment of Appeal Commissioners

7.3 Appeal Commissioners are appointed by the Minister for Finance. The practice has been to appoint civil servants from the Office of the Revenue Commissioners or members of the accountancy or legal professions. The Appeal Commissioners perform a very important function.

We recommend that any vacancies be filled following an open public competition to be organised by the Civil Service Commission.

7.4 We noted in Chapter 4 (Table 3) that the number of appeals heard by the Appeal Commissioners in 1984 was almost seven times the number in 1964 and the number of hearings has more than doubled in the past ten years. While the number of hearings increased dramatically during this period the number of Appeal Commissioners increased by only one in 1980 (from two Commissioners to three as at present). We expect a reduction in the number of hearings as a result of our proposals for changes in the assessment procedures. However, undue delays are bad for both taxpayers and the administration and ineffective operation brings any system into disrepute. We recommend that sufficient staff, including, if necessary, an additional Commissioner, should be appointed to enable the Commissioners carry out their functions in a satisfactory manner.

### **Circuit Court Appeals**

7.5 One general aspect of the appeal procedures is whether the taxpayer should in all cases be entitled to a re-hearing by the Circuit Court. With regard to all assessments made on or before 8 June, 1983, the taxpayer has the right to request a rehearing by the Circuit Court Judge if he is dissatisfied with the decision of the Appeal Commissioners. New provisions introduced in 1983 ensure, in relation to assessments made after 8 June, 1983, that the taxpayer has no right to a rehearing by the Circuit Court Judge if the appeal to the Appeal Commissioners has been dismissed on the grounds that no accounts have been furnished. The new provisions are an attempt to stop taxpayers using the appeal procedures to delay the submission of returns and accounts and payment of any balance of tax. At 31 December, 1984 there was a total of 10,924 income tax and corporation tax assessments under appeal to the Circuit Court.

7.6 While it is too early to say how the new provisions will work, the Revenue Commissioners hope that they will result in appeals being made earlier and will reduce duplication between the Circuit Court and the Appeal Commissioners. We take a less optimistic view. It may be that the 1983 provisions will reduce the pressure on the appeal system but they will only do so at the cost of confirming as due and payable amounts of tax which in many cases are hopelessly unrealistic. The already overburdened collection system will have to cope with this, either by running up even greater amounts of uncollectable tax due for collection or, alternatively, liberalising the arrangements for writing off tax which has been assessed.

7.7 The Circuit Court hearing is a full re-hearing of the appeal without reference to what has gone before. There is no transmission to the judge of evidence, arguments or the reasons for the decision of the Appeal

Commissioners. All that the judge knows is that the taxpayer has been unsuccessful before the Commissioners. Since the Circuit Court is a rehearing of the appeal, issues not raised or even hinted at before the Appeal Commissioners may be taken. There is, however, an obvious need for an informal hearing on tax matters. Disputes arise and should be resolved every year and most cases should be capable of settlement without recourse to a court of law. In principle, the Appeal Commissioners serve this function well.

7.8 A taxpayer should have a right of appeal to the Circuit Court but we considered whether the rehearing should be only on the basis of evidence presented before the Appeal Commissioners. This restriction would undermine the traditional informality of hearings before the Appeal Commissioners and impose additional costs and delays. We do not think that the Appeal Commissioners, as currently constituted, would be in a position to produce written arguments and decisions incorporating a record of the evidence presented to them in every case. Nevertheless, if abuse arises, steps may have to be taken to confine hearings in the Circuit Court to matters raised in evidence before the Appeal Commissioners, except, of course, with the express permission of the Court.

### **Appeal to High Court**

7.9 A taxpayer or the inspector of taxes may appeal to the High Court by way of a case stated. The procedure is that on determination of the appeal by the Appeal Commissioners or the Circuit Court Judge the aggrieved party must immediately express dissatisfaction with the determination as being erroneous on a point of law. Having done this he then has twenty one days within which he must give notice in writing to the clerk to the Appeal Commissioners requiring the Commissioners to state and sign a case for the opinion of the High Court. A fee of £20 must be paid.

7.10 The requirement that either party to an appeal must express dissatisfaction immediately in order to secure the right to have a case stated for the High Court can give rise to difficulties and could deprive the taxpayer or the Revenue Commissioners of the right of appeal. As a separate procedural step, the expression of dissatisfaction does serve as a warning to preserve a note of the evidence for incorporation in the stated case. We do not think there is great force in this argument, particularly as the request for the statement of case must be made within twenty one days and it would therefore be reasonable for any party or Appeal Commissioner or Circuit Court Judge to retain his notes for at least this long. Furthermore, in practice there is considerable discussion among the parties about the content of the case and it is only when agreement is reached that the case is forwarded to the High Court. We therefore, recommend the abolition

of the requirement to declare dissatisfaction 'immediately' after the determination of an appeal.

### ***In Camera* Appeals**

7.11 There is no specific provision for hearings before the Appeal Commissioners to be held *in camera*. No provisions are necessary as the hearings are in private rather than in open court. However, provision is made for the rehearing of an appeal by the Circuit Court to be held *in camera*. Until recently tax appeals to the High Court and the Supreme Court were held *in camera* if the taxpayer so desired. This option was withdrawn in 1983 and such appeals are now held in open court. Circuit Court appeals are still held *in camera*.

7.12 The taxpayer's right of appeal to the High Court lies only on a point of law. Such cases generally relate to the interpretation of some aspect of legislation or documents in support of a claim to a particular tax treatment. The matter at issue may be one which would have implications for other taxpayers in similar circumstances and for that reason it is important that the facts and the decision should be made known. However, we are not convinced that there is a need to identify the taxpayer involved in the appeal. We recommend that tax appeals to the High Court and the Supreme Court should be held *in camera*.

### **Taxpayers Right to have Appeal Heard**

7.13 Under existing law the taxpayer cannot force the inspector of taxes to have his case heard before the Appeal Commissioners. An aggrieved taxpayer cannot hasten the hearing of his appeal without the co-operation of the inspector of taxes. If an inspector, for whatever reason, is not disposed to list an appeal for hearing, the taxpayer appears to have no right of access to the Appeal Commissioners. A taxpayer may proceed by way of a Writ of Mandamus which would ask the High Court to direct the hearing of the appeal but this procedure is expensive and should not be necessary for such matters.

7.14 We raised this issue with the Revenue Commissioners who favoured no change in this area. In their experience

"taxpayers can get their cases heard when they want to. The main problem is the large volume of cases which sometimes leads to delay."<sup>1</sup>

We see no compelling reasons why taxpayers should not have the right to have their cases heard by the Appeal Commissioners if the inspector of

<sup>1</sup>Agreed noted of meeting, 12 December, 1984.

taxes is delaying unduly the settlement of an appeal. We recommend that an inspector of taxes be required to list a case for hearing before the Appeal Commissioners within three months of receiving a notice from a taxpayer requiring him to do so. A similar provision should apply in the case of claims to relief by PAYE taxpayers.

### **Recommendations**

7.15 We make the following recommendations:

1. Appointments as Appeal Commissioners should be made following an open public competition held by the Civil Service Commission.
2. Sufficient staff, including, if necessary, an additional Commissioner, should be appointed to enable the Commissioners to carry out their functions in a satisfactory manner.
3. The requirement to express dissatisfaction immediately after the determination of an appeal by the Appeal Commissioners or the Circuit Court Judge should be abolished. Any request made within twenty one days for the statement of a case for the High Court should be allowed.
4. Appeals to the High Court and the Supreme Court should be held *in camera*.
5. An inspector of taxes should be required to list a case for hearing before the Appeal Commissioners within three months of receiving a notice from a taxpayer requiring him to do so. A similar provision should apply in cases of claims to relief by PAYE taxpayers.

## CHAPTER 8

### COMPLIANCE COSTS AND TAXPAYER ASSISTANCE

#### Introduction

8.1 In this chapter we examine the effects on the compliance costs of taxpayers of our proposals for simplification of the tax system and of proposed changes in administration. We discuss the question of compensation for compliance costs, particularly those incurred by the business community, and we consider the extent to which the Revenue Commissioners could alleviate compliance costs by providing general assistance to taxpayers.

#### COMPLIANCE COSTS

8.2 The costs of the tax system include the administrative costs of assessment and collection of tax in the public sector and the compliance costs of the private sector. Compliance costs are the amounts of money, time and effort imposed on the private sector in meeting its obligations under the tax code. Compliance costs may be borne by the taxpayer and/or by a third party acting as collector of the tax. In the case of PAYE some compliance costs are borne by PAYE taxpayers but it seems probable that most of the expense of compliance with the PAYE system is borne by employers. The compliance costs of VAT fall on the business community. Compliance costs of PAYE and VAT may be offset by gains in the form of managerial and cash flow benefits. These benefits may even result in actual gains for the very large employers and businesses.

8.3 The recommendations in our first four reports involve a considerable simplification of the tax system. This would reduce significantly the compliance costs of taxpayers. The improvements in tax administration, recommended in this report, would also contribute to a lessening of the burdens on the private sector. However, self-assessment could give rise to greater compliance costs for the small proportion of self-assessed taxpayers selected for investigation but overall compliance and administration costs

for self-assessed taxpayers would be reduced. The Revenue Commissioners would accept most returns after an arithmetical check only.

8.4 Our proposals for reform of direct personal taxation and the replacement of social insurance contributions by a social security tax fully integrated with income tax would reduce significantly the compliance costs of operating the PAYE system for employers. The compliance expenses of PAYE taxpayers would then be reduced to a minimum.

8.5 The recommendation in our third report to move towards a single rate of VAT applicable to all goods and services, save exports and a few agricultural inputs, would bring a dramatic reduction in the compliance and administrative costs of VAT. A value-added tax applied at a uniform rate is a relatively simple tax to operate; most of the complications and hence the compliance costs of VAT result from exemptions and the existence of several rates. Records of purchases and sales would be streamlined. There would no longer be a need for special schemes for retailers to enable them to apportion their sales at the various rates of VAT. The completion of VAT returns would be simplified by a dramatic reduction in the number of entries to be made.

8.6 Against this background we consider the claims made in submissions for compensation for compliance costs and the need for more assistance for taxpayers and traders.

#### Compensation for Compliance Costs

8.7 A large number of submissions complained of the excessive burden placed on businesses to keep detailed records and to account for monies collected under the PAYE and VAT systems. This burden is deeply resented by small traders in particular who pressed the case that they should be compensated for acting as 'unpaid tax collectors'.

8.8 A recent Irish study<sup>1</sup> estimated that the compliance costs of PAYE for employers amounted to almost 6 per cent of net PAYE receipts in 1984. Managerial and cash-flow benefits reduced the gross costs for all firms and resulted in actual gains for the very large employers. The vast majority of firms, that is, those employing twenty people or less, incurred a net cost per employee of around £60 whereas firms employing one hundred or more received a net benefit of up to £35 per employee. Another important finding to emerge from the study was that compliance costs in the private

<sup>1</sup>Robert J. Leonard and John N. O'Hagan, 'PAYE, Costs of Compliance and Administration'.

sector were more than three times the administrative costs in the public sector.<sup>2</sup>

8.9 We have no information on the size of VAT compliance costs in Ireland. However, we have examined the results of a study<sup>3</sup> of the costs and benefits of VAT in the United Kingdom. This concluded that the total administrative and compliance costs of operating VAT<sup>4</sup> in 1977/78 were just over 11 per cent of VAT revenue in that year. Private sector costs were roughly five times greater than public sector costs. The compliance costs and benefits of VAT in Ireland may well be of the same order, given the similarities in the VAT system in the United Kingdom and Ireland. The same study showed a clear pattern in the distribution of compliance costs across firms of different sizes. Expressed in relation to turnover, the average compliance costs of small traders was some thirty to forty times that of very large traders.

8.10 The most efficient way to collect VAT and PAYE is to use the private sector as agents of the Revenue Commissioners despite the high compliance costs. Nevertheless, we recognise that the effect of the much higher net compliance costs of small firms *vis-à-vis* large firms is to put small firms at a competitive disadvantage whenever large and small firms compete in the same market. This is a state-created disadvantage and the state has a responsibility to offset it or to alleviate it. We do not favour compensation payments to offset compliance costs because we cannot envisage any tailor-made method of compensation that would be both fair and simple. The government and the Revenue Commissioners therefore have a responsibility to reduce compliance costs as far as possible. This should be done by simplifying the tax system, providing adequate information to traders and simplifying forms and procedures. These measures would enhance the efficiency of both the public and private sectors.

8.11 Many taxpayers, employers and VAT-registered traders find it

<sup>2</sup>A United Kingdom study on the compliance costs of PAYE relating to 1981-82 ('PAYE: Costs v. Benefits' Michael Godwin, Peter Hardwick and Cedric Sandford, Accountancy, November, 1983) estimated that for the United Kingdom total operating costs of collecting PAYE and National Insurance contributions combined was under 3 per cent, with compliance costs being slightly more than administrative costs. This total operating cost is much lower than the 8 per cent of the Irish study. In other respects the conclusions were similar, for example, the much higher burden on small firms, the cash flow benefits exceeding the compliance costs of large employers.

<sup>3</sup>Cedric Sandford, Michael Godwin, Peter Hardwick and Ian Butterworth, 'Costs and Benefits of VAT', Heinemann Educational Books, 1981. An up-dating of this study to 1983-84 due to be published shortly shows combined administrative and compliance costs at around 8 per cent, with administrative costs down to 1.1 per cent and compliance costs at 6-7 per cent of VAT revenue. This reduction is partly a product of the abolition of the higher rate of VAT (the United Kingdom now has only one positive rate but widespread zero rating) but mainly a result of a much higher standard rate of VAT than in 1977-78 (15 per cent as against 8 per cent). The differentials between large and small firms remain.

<sup>4</sup>In the United Kingdom in 1977/78, there were two positive rates of VAT.

necessary to telephone tax offices for tax information or the Collector General's Office about tax payments. Very often this means that taxpayers must make trunk calls and the costs increase when taxpayers experience difficulty in finding officers who can deal with their queries. To alleviate the costs imposed on the private sector we recommend that a 'freefone' system should be established to enable taxpayers to contact the Revenue Commissioners for the price of a local telephone call. This would shift costs to the administration and would be more equitable.

## TAXPAYER ASSISTANCE

### Direct Assistance to Taxpayers

8.12 Direct assistance to taxpayers is usually provided in response to queries by telephone, personal visits to tax offices and written enquiries.

8.13 Under present arrangements, most Schedule D taxpayers engage the assistance of qualified accountants or tax specialists. Nevertheless, some directly-assessed taxpayers with low incomes (particularly pensioners with low investment incomes) rely to a great extent on the Revenue Commissioners to finalise their tax affairs. The advice has traditionally been available locally for most directly-assessed taxpayers because in the main their affairs have been dealt with at the local offices. It would be essential that such assistance would continue to be available under a system of self-assessment.

8.14 The operation of the PAYE system requires close links between the Revenue Commissioners and employers. Because of this, taxpayers' records are generally organised to bring together details of all employees of a particular employer in the tax office which deals with the employer. Thus, although the Revenue Commissioners is a decentralised organisation with offices around the country, the local tax offices do not handle the affairs of all local employees. Many employees around the country find that their affairs are dealt with in Dublin.

8.15 The Dublin PAYE districts are organised by vocation or employment and are housed in offices at a number of different locations. When a taxpayer has a query about his tax liability which he wishes to have answered directly, he must find out which district deals with his affairs and its location. This causes confusion and often results in a taxpayer having to spend a considerable time locating the relevant office.

8.16 The Department of the Public Service recently examined a proposal for a Central Enquiry Office (CEO) for the Dublin area. The proposal for a CEO was originally submitted to the Revenue Commissioners by the

Irish Tax Officials' Union. The idea was inspired by the British model which established an Enquiry Office in each tax district and Principal Local Enquiry Offices in centre city locations.

8.17 The CEO, as proposed, would provide a convenient location where taxpayers could have their queries answered, whatever their tax district. Staff would have considerable experience of taxation and be specially trained to handle queries from the public and back-up services in the form of telephones, visual display units and microfilm would be available. The CEO would therefore provide a better service to the public while reducing the disruption caused by callers in tax offices.

8.18 The CEO, as proposed, is primarily aimed at PAYE taxpayers who make the greatest number of enquiries to tax offices. Under our proposals for simplification of the tax system, complicated allowances and reliefs would be removed and the vast majority of PAYE taxpayers would pay tax at the single rate. Hence, the number of callers would be reduced but some taxpayers would still need assistance. The CEO would provide a readily accessible office for PAYE callers and self-assessed taxpayers needing help to complete their returns.

8.19 We endorse the proposal to establish a Central Enquiry Office in Dublin. In the light of the experience of the operation of a CEO in Dublin, consideration should be given to opening similar offices in other large centres of population, where the volume of demand would appear to justify such a course.

### **Forms and Publications**

8.20 We have seen that our proposals for reform of the tax system, especially VAT, offer scope for a simplification of the information required in returns. A lot more could be achieved by consistent uncluttered presentation, clearer form description and titles, the use of standard type face and paper and improved layout to allow completion by typewriter or small computer. Too often, forms are designed to meet the requirements of the Revenue Commissioners and not the needs of the traders. The material issued to an employer when he registers initially for PAYE is intimidating in its volume and complexity. Some progress has been made in this area but further improvement would meet a real need. Consultation with business and trade associations is necessary. We consider that this is best done on an informal basis with the accountancy bodies, tax practitioners and the business community generally.

8.21 Tax forms and explanatory leaflets should be available in Post Offices. We also think tax forms should be issued in duplicate to enable

the taxpayer to keep more easily a copy of any return made to the Revenue Commissioners.

8.22 A simplification of the booklets and guides published by the Revenue Commissioners would also be very helpful. There is the problem of accurately expressing complex legal provisions in simple terms; we recognise that a balance has to be maintained between being simple and being accurate but it seems to us that simplicity is accorded too low a priority. Greater clarity is attainable and could be best achieved by employing expert writers rather than tax experts to produce tax guides. Taxpayers and traders understand that the guides are not intended to be a substitute for legislation or statutory regulations.

8.23 The Revenue Commissioners produce one comprehensive guide for each tax and some additional publications are available. We see merit in having a comprehensive guide to PAYE and VAT but there is a need for more specialist publications aimed at the small trader or entrepreneur setting up a new business.<sup>5</sup>

8.24 It would also be useful to have specialist publications to help educators to prepare students for their tax responsibilities through a programme in schools. Such a programme could examine not only the mechanics of preparing a tax return but also the theory and foundations of the concept of taxation with a view to improving voluntary compliance.

8.25 Finally, in their dealings with taxpayers and in particular with the business community, the Revenue Commissioners should continue to be aware of the changes which are occurring in commercial and accounting procedures and practices because of new technology. Already, some PAYE returns are accepted by the Revenue Commissioners in a computerised form. The facilities for accepting returns in this way should be extended. The obligation to keep certain records, for example, invoices or other supporting records, should be satisfied by microfilm records or records in other new technology forms.

### **Parliamentary Questions**

8.26 In relation to their dealings with the Revenue Commissioners, some taxpayers seek the assistance of Dáil Deputies. These in consequence may put down parliamentary questions. The extent to which this arises is shown in Table 9 which gives the total number of parliamentary questions answered on individual cases in 1984.

<sup>5</sup>A very good example of what can be done in this area is 'Your Own Business — a guide to setting up and running a small firm', published by the Industrial Development Authority.

TABLE 9

## Parliamentary Questions in Individual Cases, 1984

Tax	No. of Questions
Income tax	178
Value-added tax	29
Customs and excise duties	18
Stamp duties	2
Capital gains tax	1
Capital acquisitions tax	1
Total	229

Source: Department of Finance and the Revenue Commissioners

The total number of questions put down in individual cases is increasing rapidly. The estimated number of such questions in 1981 was only seventy.

8.27 The procedures which must be followed in preparing replies to parliamentary questions are cumbersome and involve considerable administrative effort, particularly for questions which require oral answers. The Revenue Commissioners told us that

“the cost of preparing answers varies considerably from question to question depending on the matters raised. A rough estimate of the cost would suggest a range of £30 to £70”.<sup>6</sup>

8.28 We consider that there are undesirable aspects to raising questions in the Dáil regarding the affairs of individual taxpayers. It is inappropriate for the following reasons. Firstly, the Minister for Finance has no responsibility for individual cases as this is devolved on the Revenue Commissioners under the ‘care and management’ provisions. He should not be held accountable in these cases. Secondly, there are adequate procedures designed to safeguard taxpayers from maladministration. The taxpayer can appeal to the Appeal Commissioners and the courts on questions of law and fact or to the Ombudsman where maladministration is concerned. Thirdly, under rules of confidentiality, the Revenue Commissioners should not disclose the taxpayer’s affairs to the Minister for Finance and officials of his Department.

### Recommendations

8.29 We make the following recommendations:

1. Every effort should be made to reduce compliance costs by simplifying the tax system, tax forms and procedures.

<sup>6</sup>Memorandum of 16 April, 1985.

2. When devising forms, the Revenue Commissioners should take account of the needs of traders by presenting forms in a clear manner.
3. A range of specialist publications should be produced for small traders and people starting new businesses and for the classroom to prepare students for their tax responsibilities and to encourage voluntary compliance. These publications should be produced by expert writers, subject to the approval of the Revenue Commissioners.
4. The scope for accepting PAYE and VAT returns and other information in a computerised form should be extended and the obligations on traders to maintain supporting records, such as invoices, should be satisfied by records held in new forms, such as micro film.
5. A Central Enquiry Office should be set up in Dublin. In the light of the experience of the operation of a CEO in Dublin, consideration should be given to opening similar offices in other large centres of population where the volume of demand would appear to justify such a course.
6. A ‘freefone’ system should be set up to enable taxpayers to contact the Revenue Commissioners from anywhere in the country for the price of a local call.

Part III

**Tax Evasion and Avoidance**

## CHAPTER 9

# PUBLIC PERCEPTIONS OF TAX EVASION

### Introduction

9.1 In our discussions we have frequently come across the problems of tax evasion (illegal understatement of tax liability, for example, by not declaring all income) and tax avoidance (legal reduction of tax liability, for example, by arranging to receive income in those forms which are least taxed). These are vexed problems, sometimes confused, by no means unique to Ireland and there seems to be a widespread impression that they are getting more severe. We wish to distinguish between avoidance and evasion, so we deal with them separately in the following two chapters.

### Public Perceptions

9.2 In many of our submissions and discussions we received complaints about individuals and groups not paying their fair share of tax. Anecdotal evidence of evasion abounds. The tax system's credibility also has suffered from press reports of companies and indeed state-owned enterprises not making PAYE and VAT remittances on time and more frequent legal or commercial evidence of tax default. There also seems to be resentment of legitimate use of incentive reliefs when institutions or individuals with large incomes are seen to pay little tax. Yet, at the same time, 'penal' rates of tax were quoted to us as a justification for attempts to avoid or evade tax and we were told of a general falling off in standards of 'tax honesty'.

9.3 There is some limited survey evidence of Irish attitudes to these matters. Table 10 shows the results of a 1981 survey, suggesting that the Irish take a laxer view of tax evasion than do other European countries and that disapproval of evasion is less than for other forms of civil dishonesty. However, the figures indicate general disapproval of tax evasion.

TABLE 10

**Attitudes to Tax Evasion and Other Forms of Civic Dishonesty — Permissiveness Scores<sup>1</sup>**

	Republic of Ireland	Northern Ireland	Britain	All Europe
Cheating on Tax	3.35	2.86	2.69	2.64
Avoid Paying Fare on Public Transport	2.49	1.79	2.05	2.14
Claim State Benefits: not Entitled	1.83	1.56	1.67	2.02
Bribery in Course of Duties	1.50	1.31	1.61	1.9*
Average	2.29	1.88	2.01	2.18

<sup>1</sup>Question: whether each form of conduct can be justified; always (score 10), never (score 1) or something in between.

Source: Irish Values and Attitudes: The Irish Report of the European Values Systems Study, Dominican Publications 1984, Table 7 (b) (i).

9.4 The Irish attitudes are broken down by age group and shown in Table 11. The younger a person is, the more tolerant is the view of tax evasion.

TABLE 11

**Irish Attitudes to Tax Evasion and Other Forms of Civic Dishonesty — Permissiveness Scores by Age**

Age Group	18-24	25-34	35-44	45-54	55-64	65-74	75+
Cheating on Tax	4.05	3.36	3.38	3.38	3.02	2.65	2.11
Avoid Paying Fare on Public Transport	3.19	2.64	2.44	2.24	2.03	1.88	1.80
Claim State Benefits: not Entitled	2.27	1.70	1.87	1.68	1.62	1.74	1.38
Bribery in Course of Duties	1.75	1.44	1.49	1.44	1.41	1.41	1.26
Average	2.82	2.29	2.30	2.19	2.02	1.92	1.64

Source: Table 8 (b) (i).

9.5 A more limited survey was carried out in the spring of 1983 on a sample of adults registered for evening classes in the Commerce Faculty of University College, Dublin.<sup>1</sup> The study concluded that

“policy directed against tax evasion should urgently address the complex issues of tax ethics and the perceived inequity of the taxation system. Tax evasion could primarily be a reflection of low moral standards throughout society. If this is true it may be argued that control of tax evasion transcends the power and competence of the tax authorities. If perceived inequity generates the motivation to evade, but if these perceptions are incorrect, then government policy should be directed towards correcting these perceptions. On the other hand, if the perceptions of inequity are accurate and supported by economic reality, then government must urgently redistribute the burden of

<sup>1</sup>‘Tax Evasion: An Empirical Study of Taxpayers’ Behaviour’, Peter J. Clark and Joseph Mahoney, *Journal of Irish Business and Administrative Research*, Vol. 6 No. 2, October, 1984.

taxation in a more equitable manner and therefore reform our taxation system. The perceived probability of being detected was not found to be a deterring factor in the noncompliance decision. This suggests that the absolute probability of being caught as a tax evader is extremely low which is reflected by the respondents’ perceptions at the time of the study.”

**Conclusion**

9.6 We have presented the evidence above as it is the most balanced we have come across. However, while there is a general problem of attitudes and perceptions, the survey evidence does not allow exploration of the root causes of the problems. Nevertheless, it is clear that apparent injustices strike some people particularly hard.

## CHAPTER 10

### TAX EVASION

#### Introduction

10.1 We recall that tax evasion is an illegal understatement of income or assets or overstatement of allowances in an attempt to escape payment of tax. It ranges from deliberate errors or omission to concealment, false declarations and major fraud. It excludes tax which is not paid for any reason once liability has been established: that is a collection problem and we deal with it in Chapter 15.

10.2 We have noted the public concern about tax evasion and the perception that it is widespread and increasing. In this chapter we give a little more background and then outline the measures taken by the Revenue Commissioners to control evasion. We conclude that improved audit arrangements could increase the detection of evasion and hence control it more effectively. Penalties for tax evasion are considered in Chapter 13.

#### The Administrative Background

10.3 The difficulties of quantifying the amount of tax evasion were noted by the Revenue Commissioners in evidence to the Commission on Income Taxation in 1959 as follows:

“Since evasion implies concealment it will be appreciated that a reliable estimate of the extent to which evasion is practised is not feasible. References to tax evasion are heard from time to time, and occasionally even an estimate of its magnitude will be offered, but statements of this kind cannot be properly judged in the absence of evidence; and furthermore people are liable to confuse favoured treatment under tax law with evasion.”<sup>1</sup>

10.4 Despite the lack of clear evidence about the extent of evasion, the

<sup>1</sup>Commission on Income Taxation, Seventh Report, Pr 6581 para. 267.

subject has worried Ministers for Finance over the last decade. In the 1973 Budget Statement, the Minister said

“As far back as 1962, the Commission on Income Taxation referred, in their seventh report, to the belief that evasion was widespread. This belief is probably even more generally held today, and has serious psychological as well as revenue consequences in that it tends to create a climate where evasion becomes socially acceptable. Steps have been taken in recent years to counter evasion. These have not, however, proved adequate to deal with the problem, and further comprehensive provisions to ensure that the burden of the tax will fall more equitably are being studied.”<sup>2</sup>

10.5 In January, 1976, the Minister for Finance announced the launching of an even more rigorous anti-evasion operation by the Revenue Commissioners. Under this campaign, a special staff unit was set up to oversee the anti-evasion drive and to devise new procedures to pursue tax defaulters. Cases which appeared to warrant special attention were to be subject to intensive investigation and where evidence was found of tax evasion, the offenders were to be brought to court and prosecuted. In future there was to be no question, in serious evasion cases, of allowing an option for a financial settlement out of court.

10.6 In inaugurating the new regime, the Minister announced an amnesty to allow

“those who have defaulted in the past a last chance to put themselves right with the law so they can start the future with a slate wiped clean”.<sup>3</sup>

10.7 The amnesty was made available to tax defaulters who, within a strictly limited period of three months

- (i) disclosed to the Revenue Commissioners the fact that they had been understating their incomes,
- (ii) detailed the manner and extent of all their evasions,
- (iii) produced full details of their assets, deposits and other holdings, and
- (iv) made a substantial payment on account of the tax evaded.

10.8 The Revenue Commissioners told us that the 1976 amnesty was a failure.

<sup>2</sup>Budget Speech, 16 May, 1973.

<sup>3</sup>Budget Speech, 28 January, 1976.

10.9 By 1979, the Minister conceded that anti-evasion measures

“are proving inadequate and it is clear that existing Revenue staff resources are not sufficient to deal with the problem. I am therefore making provision for a substantial strengthening of the staffing of the Revenue Commissioners in order to enable them to mount an effective and comprehensive attack on evasion. The campaign will include such measures as examination in depth of particular accounts and, where there are indications of evasion, reconciling them with the general state of the business and the taxpayer's life style. Evasion will also be followed up more intensively in the case of PAYE and VAT. In future, more emphasis will be placed on legal proceedings, rather than compromise action, where the making of false returns is uncovered”.<sup>4</sup>

10.10 In 1981, the Minister for Finance was able to report that the new resources enabled the Revenue Commissioners to strengthen their staffs, particularly in the tax districts where counter-evasion is part of the day's work. Specialist divisions were also set up to deal with the more difficult cases. The Minister went on to say that

“In the past year, the number of staff — inspectors and accountants — attached to the Taxes Investigation Branch has been doubled and the number of cases referred to that Branch for investigation has doubled also.

“The special enquiry units set up in 1979 to seek out those not already on record brought in 14,000 cases and the remainder are under investigation. In 1979 alone, £2.75 million was recovered in back duty. Court proceedings were initiated in over 900 cases, the majority for failure to make returns. Penalty proceedings in connection with underpayments of tax were taken in a number of cases”.<sup>5</sup>

10.11 In 1983, the Minister noted that while it was not possible to estimate the precise extent of evasion, it was evident that it was widespread. He announced a number of new provisions to deal with the problem. These were

- (i) the provision of a term of imprisonment of up to two years, in addition or as an alternative to a heavy monetary penalty, on conviction or indictment for major tax offences involving deliberate fraud,
- (ii) the requirement to disclose the purchase and sale of government securities in tax returns and for nominee holders of such securities to

<sup>4</sup>Budget Speech, 7 February, 1979.

<sup>5</sup>Budget Speech, 28 January, 1981.

disclose particulars of transactions to the Revenue Commissioners, and

- (iii) a reduction in the disclosure limit for bank interest from £70 to £50.

10.12 The Minister also announced that, in future, the Revenue Commissioners would publish annually a list of persons and companies who had been convicted of a tax offence or with whom settlements had been reached in the larger back-duty cases involving default by the taxpayer. Publication would not be made where settlements were made and agreed amounts paid before the end of 1983 or where there was a full and voluntary disclosure in advance of any investigation. The first list of evaders was published in 1985.

### The Extent of the Problem

10.13. No official estimates of the size of tax evasion in Ireland are available. A widely quoted estimate of the size of the black economy in the United Kingdom is that of Sir William Pile, then Chairman of the Board of Inland Revenue, who told the Expenditure Committee of the House of Commons that it was “not implausible” that undeclared income might amount to some 7½ per cent of gross domestic product in 1977. If applied to Ireland, such an estimate would imply that income was underdeclared in 1984 by £1,200 million. At a 30 per cent tax rate, this would be equivalent to 2½ per cent of GNP and about one third of the current budget deficit.

10.14 In the United States, the Internal Revenue Service has attempted to estimate the amount of unreported income in that country. Under its Taxpayer Compliance Measurement Programme, the Internal Revenue Service uses information from detailed audits of selected taxpayers to analyse the characteristics of those who are likely to conceal income. The primary purpose is to facilitate computer selection of taxpayers for subsequent audit but an incidental merit is the capacity to estimate the additional revenue which could be raised from all taxpayers if their affairs were subject to this degree of scrutiny. The study concludes that between 91 per cent and 94 per cent of income from legal sources in the United States is reported.

10.15 The concealment of 6 to 9 per cent of income does not include an additional 2 to 3 per cent of income from illegal sources, the bulk of which relates to traffic in drugs. Of legal but unreported incomes, somewhat less than half relates to self-employment, one quarter to investment income (for which withholding provisions are more limited than in Ireland) and the remainder to incomes from employment. About one-third of additional income attributed to taxpayers relates to deductions (of which the United

States' tax code provides a wide range) which do not survive detailed scrutiny.

10.16 Experience in the United States confirms that voluntary reporting of income is very high where incomes are subject to withholding taxes. Voluntary reporting is lower where income paid to recipients is reported by third parties but it is still considerably better than where incomes are subject to neither withholding nor information reporting.

#### Administrative Data

10.17 Administrative data are sometimes used to assess trends in evasion but the results can be misleading because changes may result from changes in detection methods, in the tax structure or in the extent of evasion. However, the information also gives some insight into the present detection arrangements.

10.18 The Revenue Commissioners publish in their Annual Reports an increasing volume of information about their enforcement activities. We reproduce some of this in the following tables. Table 12 shows the growth in detections of customs and excise offences.

TABLE 12

#### Customs and Excise Offences

Year	Seizures for Smuggling	Illegal Use of Rebated Oil
1975	2,904	634
1976	2,357	541
1977	2,937	244
1978	3,475	379*
1979	2,827	755
1980	3,711	760
1981	4,089	1,391
1982	4,747	1,600

Source: Annual Reports of the Revenue Commissioners.

\*The figures for 1978 and subsequent years refer to total detections of illegal use of rebated oil. The figures for earlier years refer to the number of convictions.

10.19 The number of seizures for smuggling doubled in the six years to 1982 but the overall level of seizures of thirteen per day in 1982 does not, of itself, indicate that smuggling is a serious problem. However, the average duty-paid value of seizures at the border of £1,475 for 1983, compared with £217 elsewhere, is an indication of a more serious problem at the land frontier with Northern Ireland. There has also been substantial growth in the number of cases detected of illegal use of rebated oil commonly known as 'red diesel'. In 1982, this was over four times its 1978 level.

10.20 Table 13 gives details of back-duty settlements in relation to income tax and corporation tax. An amnesty was announced in 1976. This offered freedom from prosecution and penalties to defaulters who, within three months, made a full disclosure of their default and a substantial payment on account of tax evaded. Amnesty cases are identified separately.

TABLE 13

#### Back-Duty Settlements for Income Tax and Corporation Tax

Year	Cases Completed	Settlement £000s	of which Penalties and Interest		Amnesty	
			£000s	% of Total Tax Due	Cases Completed	Settlement £000s
1973	205	610.6	66.2	12.2		
1975	102	830.8	131.1	18.7		
1976	109	891.3	126.5	16.5	59	265
1977	158	1,219.9	227.1	22.9	145	225
1978	55	2,612.5	837.7	47.2	11	477
1979	96	2,518.4	556.3	28.4	24	240
1980	107	1,596.8	429.5	36.8	3	8
1981	98	1,446.1	426.6	41.8	4	101
1982	108	3,078.4	934.0	47.8	2	5

Source: Annual Reports of the Revenue Commissioners.

Notes: 1. Settlements include payments on account of £226,000.

2. The figures for 1973 relate to the year ended 31 March 1973, all other figures are for calendar years.

10.21 In 1981, back-duty settlements for value-added tax were identified separately for the first time. In that year, forty two cases were completed. The amount involved in settlement of the cases was £1.25 million which included £174,000 in penalties and interest charges (13.9 per cent of the total settlement). Thirty two cases were completed in 1982 yielding £2.5 million. The addition for penalties was 12.6 per cent.

10.22 A number of interesting features is clear from Table 13:

- (i) the number of back-duty cases completed in 1982 was about half the number completed in 1973,
- (ii) the proportion of the total final settlements accounted for by penalties and interest has increased very substantially in recent years, suggesting that the Revenue Commissioners have adopted a much tougher approach in relation to tax evasion, and
- (iii) the total value of settlements rose by almost 50 per cent in real terms between 1976 and 1982 but declined by over one-third from the exceptionally high figure in 1978.

10.23 A unit to audit operation of PAYE by employers was set up in mid 1979. Details regarding the operation of this unit are in Table 14.

**TABLE 14**  
**PAYE Audits**

Year Ended	No. of Audits	% of Registered Employers Audited	Average Settlement
May, 1982	3,669	4.1	£ 3,276
May, 1983	4,088	4.4	7,802
May, 1984	3,900	4.1	6,219

Source: The Revenue Commissioners.

Notes: 1. Many of the settlements cover a period of more than one tax year.

If the cases in which settlements are reached are representative of employers as a whole, the total amount of PAYE recoverable by comprehensive audits would be £578 million in respect of the period covered by the settlements. However, the yield of PAYE is highly concentrated in that 70 per cent of the yield arises from six hundred and fifty employers (less than 1 per cent). Therefore, care must be exercised in drawing conclusions based on average settlements.

10.24 The yield from VAT audits is shown in Table 15.

**TABLE 15**  
**Yield from VAT Audits**

Year	Yield	as % of Total Net Receipt of VAT
	£m	
1980	17.5	3.7
1981	24.8	4.0
1982	34.4	3.6
1983	71.6	6.0
1984	69.1	5.1

Source: The Revenue Commissioners.

10.25 We were informed by the Revenue Commissioners that a significant proportion of the yield from VAT audits does not reflect non-compliance. It represents adjustments made in the method of calculating liability arising from errors made by accountable persons which are attributable to the complexity of the system. In addition to the underpayments shown in Tables 14 and 15 further VAT and PAYE underpayments amounting to £17.9 million were detected by the Anti Evasion (Audit) Branch in the four years to 1983.

10.26 Also, in 1979, the Revenue Commissioners established special enquiry units in Dublin and the provinces to uncover liable persons not on

record for tax. The number of new cases not previously on record identified by these units is in Table 16.

**TABLE 16**  
**New Cases Identified by Special Enquiry Units**

Year	Number of Cases
1979	5,145
1980	10,264
1981	7,664
1982	4,268
1983	2,245
Total	29,586

Source: Annual Reports of the Revenue Commissioners.

Most of these cases (about 90 per cent) were traders representing a wide range of activities and the remainder were persons engaged in professions and vocations. The 1981 Revenue Commissioners' Report states in relation to these cases that

"the outcome in these cases will depend upon their individual circumstances but, in a number of instances, there will be liability for earlier years and it is anticipated that some cases will require to be examined in depth by the Investigation Branch".<sup>6</sup>

10.27 Not all cases of evasion which come to light are referred to the Investigation Branch and included in back-duty figures. However, if evasion is taking place on any substantial scale, the figures suggest that the possibility of being caught is relatively small. The figure of just over £2 million for recovery in 1982 of tax evaded<sup>7</sup> translates into an income figure of £5.9 million, assuming an average rate of tax of 35 per cent. If evasion in 1981 amounted to 5 per cent of national income, the probability of being caught would be about one in a hundred. If it is assumed that tax evasion is confined to non-agricultural, non-employee remuneration and that evasion amounts to 1 per cent of such income, the chances of being caught are about one in two. Since evasion is not confined to this type of income, on the assumption made about the extent of evasion, the chances of detection are even less. This analysis suggests that unless evasion is trivial, there is a clear need to increase the probability of detection.

### Tackling Evasion

10.28 The Revenue Commissioners have two methods of curbing evasion. The first is to use to the best advantage, in the routine examination

<sup>6</sup>Annual Report of the Revenue Commissioners, 1981, pl 1437 p. 42.

<sup>7</sup>See Table 13. The tax evaded, excluding penalties and interest, was £2,081 million.

of cases, all the information already in their possession. The second is to increase the proportion of their resources applied to investigative work and to deploy this as effectively as possible.

10.29 We have not examined the organisational structure of the Revenue Commissioners. However, we are aware that different sections deal with the various tax heads such as VAT, PAYE/PRSI, corporation tax and income tax of the directors or proprietors of a single business entity. The existence of different sections dealing with different elements of a case may hinder rather than help control and anti-evasion work. Lack of effective communication could result in one section not fully understanding or appreciating the significance of information being sought by the other section. At present, outdoor visits to traders' premises are largely confined to VAT and PAYE audits. Under our proposals for self-assessment, there would also be visits to traders' premises to verify income tax and corporation tax returns. It would be extremely irritating and expensive for a taxpayer to have separate visits in respect of each different tax head. It would also be inefficient use of staff resources. We consider that there is a *prima facie* case for closer integration of VAT, employers' liability to remit PAYE and PRSI, tax on directors' remuneration, capital gains tax and corporation tax in the case of limited companies and the corresponding tax heads for self-employed persons. We recommend that the Revenue Commissioners give serious consideration to a re-organisation of their structures on these lines.

10.30 It also seems to us that too great a proportion of the resources of the Revenue Commissioners is being devoted to routine processing of the cases of taxpayers who are generally compliant. Hence too little attention can be devoted to persistent defaulters. A simplified tax code and self-assessment would help here. They would allow greater attention to be paid to critical examination of the affairs of a relatively small number of taxpayers. These critical examinations should be integrated, taking account of all aspects of a taxpayer's affairs, including PAYE and VAT liability.

10.31 On the general question of redeploying staff, we recognise that the direct yields in terms of tax, although extremely important, should not be the sole criterion in determining the allocation of investigative resources. Account must be taken of the unquantifiable deterrent effect of being seen to be active against all forms of tax evasion and non-compliance.

10.32 Finally, the penalties for tax offences have to be high enough to be a deterrent but realistic enough to ensure that they are enforced. Ideally, all penalties should be imposed automatically, subject to a right of appeal. Our proposals for penalties for tax offences are in Chapter 13.

## Conclusion

10.33 We are convinced by a variety of partial indicators that tax evasion results in serious revenue losses. The evidence of the Revenue Commissioners shows it to be a problem in certain areas. Yet, the possibility of being caught seems relatively low. There is a clear need to increase the probability of detection.

10.34 We believe that it is in the public interest to establish the degree of tax evasion that is detectable by applying a consistent and reliable method of scrutiny at a given level. This could be done along the lines of the Taxpayer Compliance Measurement Programme in the United States.

## Recommendations

10.35 In the context of the need to deal with tax evasion, we stress the necessity of implementing those proposals we have made to simplify the system, broaden the tax base and reduce tax rates. This would free resources, now engaged in less productive work, for anti-evasion duties. We make the following recommendations:

1. The Revenue Commissioners should undertake, as a matter of urgency, a valid statistical survey on the lines of the Taxpayer Compliance Measurement Programme in the United States to ascertain the level of detectable tax evasion and the characteristics of tax evaders. The results of this survey should be published.
2. The Revenue Commissioners should consider reorganising their structures to ensure closer integration of VAT, employers' PAYE and PRSI, taxation of directors' remuneration, capital gains tax and corporation tax in the case of limited companies and the corresponding tax heads in the case of self-employed persons.

## CHAPTER 11

### TAX AVOIDANCE

#### Introduction

11.1 There are many views on what constitutes tax avoidance. For example, it is possible to reduce or remove tax liability by choosing among perfectly acceptable tax reliefs and incentives or even by refraining from consuming a taxed product. However, for purposes of this report we define tax avoidance as the minimisation of tax liability through taking advantage of some provision or lack of provision in the law in circumstances other than that perceived to be intended by the legislature. Since tax avoidance is taking advantage of opportunities provided by the law, it excludes fraud, concealment or other illegal measures.

11.2 Tax avoidance flourishes when large differences in tax liability rest on fine legal distinctions. The most effective way of dealing with avoidance is to simplify the tax code, as outlined in our previous reports. Nonetheless, we consider some other issues, including the introduction of a general power for the Revenue Commissioners to disregard legal transactions aimed at avoiding tax and whether or not anti-avoidance legislation should have retrospective effect.

#### The Context

11.3 The present tax system of high nominal rates of tax, different tax treatment of income earned or expenditure made in different ways and a multiplicity of special exemptions and reliefs creates the ideal environment for tax avoidance. High nominal rates encourage efforts to minimise taxation. The existence in the law of alternative treatments of income not only affords the opportunity for tax planning but makes it necessary.

11.4 Our proposals for tax reform in Ireland involve a new approach. We have recommended a comprehensive definition of income under which all income, no matter how it is earned, would be taxed at the same rate. Irrelevant distinctions about how it accrues would be avoided. Rates of tax would be much lower. Incentives would be given directly rather than

tax-based. Under such a system, the scope for tax avoidance would be significantly reduced. Lower marginal tax rates would prove effective against tax avoidance, especially in the upper income groups. We believe that the introduction of such a system is the only means of controlling tax avoidance.

#### Official Attitudes to Avoidance

11.5 A major statement of the official attitude to tax avoidance was made in the 1981 Budget Statement. This went so far beyond previous official attitudes that it deserves to be quoted in full.

"Tax avoidance and tax evasion are subjects which arouse strong condemnation in the general body of taxpayers, who rightly condemn such activities which clearly operate to their detriment. Sometimes, much is made of the legal distinction between these two areas, tax evasion being defined as a straight-forward breach of the tax law while tax avoidance is a careful and well-planned exploitation of that law and is defended on the ground that the letter of the law is not breached. As has been stated before, the margin between avoidance and evasion in many cases is no more than hairline. This is particularly so where the device used by the tax avoider involves the use of artificial and legalistic arrangements which serve no economic or commercial purpose but are entered into for the sole purpose of avoiding tax. There is no justification for ambivalent thinking on this subject. The taxes payable are imposed in the name of the community and are expended on purposes determined by the community in a democratic process.

"Whatever merit the distinction between evasion and avoidance may carry in law, it carries none for the general body of taxpayers who must bear, in addition to their own share of the total tax burden, that part of the tax load of which the evader and the avoider have divested themselves".<sup>1</sup>

11.6 The Minister for Finance went on to threaten that in future anti-avoidance provisions would have retrospective effect.

"A major problem in relation to tax avoidance schemes is that, traditionally, the corrective legislation applies only from a current date, so that the tax avoider will already have secured the benefit of his avoidance devices for an extended period. I am concerned that greater control should be exercised to ensure that our taxation system is not subjected to this abuse. I would advise tax planners and tax avoiders

<sup>1</sup>Budget Speech, 28 January, 1981.

that they should not assume that future anti-avoidance legislation will invariably apply from a current date".<sup>2</sup>

11.7 The threat of retrospective legislation was repeated in the 1983 Budget Statement:

"Tax avoidance has become a veritable industry in its own right and it is clear that there is a considerable loss of revenue from artificial transactions designed to avoid tax. Tax planners who engage in these activities can expect that greater attention will be given in future to closing off loopholes which they exploit. They would be unwise to assume that anti-avoidance legislation will invariably apply from a current date only".<sup>3</sup>

#### Attitude of the Courts Towards Tax Avoidance

11.8 Before examining the proper legislative approach to tax avoidance, we consider the attitude of the courts to the subject. The traditional judicial approach to the determination of tax liability is to determine

(i) the meaning of the law in accordance with certain well-established rules of construction, and

(ii) the true legal effect of the taxpayer's transactions and arrangements and then decide whether they fall within the scope of the law.

11.9 The effect of this traditional judicial approach to taxation is to favour the taxpayer who carefully arranges his affairs so as to bring his gains outside the scope of the tax law which he expects will be strictly and literally interpreted by the courts.<sup>4</sup> However, it works against the unwary taxpayer who runs foul of a technical provision. He may incur a tax liability which was never intended.

11.10 Since 1935, the principle in the *Westminster* decision has formed the cornerstone of tax planning. However, a new approach has evolved in recent years, following a series of decisions by the House of Lords in Britain. This new approach, while not fully overruling the *Westminster* case, has been described as an 'emerging principle'. The judge in one key case summed up the situation as follows:

"I shall attempt no exhaustive exposition of all the criteria by which, for the purpose I suggest, form and substance are to be distinguished. Once a basic doctrine of form and substance is accepted, the drawing

<sup>2</sup>Budget Speech, 28 January, 1981.

<sup>3</sup>Budget Speech, 9 February, 1983.

<sup>4</sup>Established in the *Duke of Westminster* case in 1935.

of precise boundaries will need to be worked out on a case by case basis. . . ."<sup>5</sup>

11.11 It is not clear what the attitudes of the Irish courts will be to the issues arising in the House of Lords' decisions. These will not emerge until similar cases are brought to the Irish courts.

#### Attitude of the Legislature to Tax Avoidance

11.12 In the final analysis, action to counter tax avoidance is the responsibility of the legislature. There are four main approaches possible:

(i) the '*specific*' approach envisages enactment of provisions which identify with precision the type of transaction to be dealt with and prescribes exactly the tax consequences of such a transaction.

(ii) the '*transactions not at arm's length*' approach may be applied where the parties to particular transactions are not dealing with each other at arm's length and there is scope to alter the tax consequences of the transactions as a result.

(iii) the '*administrative control*' approach contemplates the grant of wide powers to an official or administrative body in order to counter tax avoidance transactions, and

(iv) the '*general*' approach involves the enactment of a broadly framed provision which imposes tax on transactions defined in a general way.

#### The Specific Approach

11.13 Most of the anti-avoidance provisions in tax law are specific. This approach has a number of advantages. Firstly, it may be held that a taxpayer's liability should be imposed in explicit terms by the Oireachtas and this does not happen where control of tax avoidance is governed by general prohibitions or departmental discretion. Secondly, where specific provisions are enacted, they produce certainty in the law. If they are found to be inadequate they can be amended. Thirdly, it may be argued that specific provisions are adequate to deal with most forms of tax avoidance and that they may be supplemented by court decisions.

11.14 The problem with the specific approach is that it is impossible to foresee every scheme of tax avoidance, so avoidance can never be prevented totally. Indeed, poor drafting of the law can open new loopholes or extend the law to situations which were not meant to be included. One inherent

<sup>5</sup>*Furniss v Dawson* [1984] STC 153, 159.

difficulty is that the use of specific language assists the potential avoider because it defines the problem for him. This may give rise to a tendency to use more vague language in an attempt to cover unforeseen situations, yet more vague language is the antithesis of the specific approach. Another problem of the specific approach is that it leads to a great deal of anti-avoidance legislation and this is responsible for much of the length and obscurity of tax law.

11.15 A specific approach may not always be wholly effective. This is inevitable, given the complexity of the existing system. Unless the basic problem is tackled by ensuring that the same tax is charged on income, however it accrues, specific anti-avoidance measures are doomed to failure even though isolated successes may occur.

### **The Transactions At Arm's Length Approach**

11.16 An important element of tax avoidance, mainly relevant in the field of business income, arises where the parties with a common economic interest arrange transactions to reduce their joint tax liability. Persons in such circumstances are said not to deal with each other 'at arm's length'.

11.17 The Finance (Miscellaneous Provisions) Act, 1968 contains a definition of 'connected persons' which is also incorporated into a number of other provisions of tax law. The definition of what constitutes a connected person is very wide and includes spouses, close relatives, in-laws, trustees, partners and controlled companies.

11.18 Under the proposals made in our first report for reform of the tax system, there would be much less need for special provisions dealing with transactions not at 'arm's length.' In the first place, transactions within a family unit would be free of tax and the income received by all members of a family unit would be aggregated for tax purposes. This would eliminate the need for some of the provisions or at least would reduce the scope of their application. Secondly, the single rate of tax on companies and individuals, together with a full imputation system of company taxation, would remove the need for much of the close company anti-avoidance legislation. Despite this, some problems would remain and it would be necessary to retain provisions to deal with transactions or arrangements between persons not dealing with each other at arm's length. Such provisions are a necessary complement to the specific approach to tax-avoidance.

### **The Administrative Control Approach**

11.19 In some countries, the Revenue authorities are given discretionary anti-avoidance powers for a variety of purposes which may be subject to

supervision by the courts. To take an Irish example, Section 530 of the Income Tax Act (since repealed) provided that

"With a view to preventing the avoidance of the payment of tax at the higher rates through the withholding from distribution of income of a company which would otherwise be distributed, it is hereby enacted that where *it appears to the Revenue Commissioners* that any company to which this section applies has not, within a reasonable time after the end of any year . . . . distributed to its members . . . . a reasonable part of its actual income from all sources . . . . the Commissioners may . . . . direct that for purposes of assessment to tax, the said income of the company shall . . . . be deemed to be the income of the members and the amount thereof shall be apportioned among the members."<sup>6</sup>

11.20 In exercising their power to make 'sur-tax directions', the Revenue Commissioners were to have regard not only to the current requirements of the business but also to "such other requirements as may be necessary or advisable for the maintenance and development" of the business.

11.21 We consider that such discretionary powers are highly undesirable. Where they exist, taxpayers cannot be certain that they will be judged by the same standard as other taxpayers. There is no guarantee that such powers would not be used in an arbitrary fashion. We recommend against any attempt to control tax avoidance by extending the discretionary powers of the Revenue Commissioners.

### **The General Approach**

11.22 Recognising the difficulty of drafting watertight specific provisions, an omnibus anti-avoidance clause is often called for.<sup>7</sup> It is argued that this would be sufficient to deter a great deal of tax avoidance. This general approach would, presumably, regard as null and void transactions which were deemed to be 'artificial' or intended wholly (or perhaps mainly) to secure a tax advantage. There is such a provision in tax legislation in the Federal Republic of Germany which provides that where there is a normal method of carrying out a given transaction, it is taxed as though this method has been adopted, unless the taxpayer can prove commercial necessity or some legitimate reason, other than tax avoidance, for departing from the norm.

11.23 The Revenue Commissioners told us that they did not favour the introduction of general anti-avoidance legislation. It was tried in relation to estate duty in 1965 and gave rise to great uncertainty. Specific provisions

<sup>6</sup>The italics are ours.

<sup>7</sup>'Confronting the Jobs Crisis'. Irish Congress of Trade Union, September, 1984. Page 16.

are far better. A general anti-avoidance provision inevitably leads to greater uncertainty and hence to greater bureaucratic discretion since advance clearance would be necessary in many cases. We do not consider this desirable for the reasons stated in paragraph 11.21.

11.24 General anti-avoidance provisions are very difficult to apply in practice. Transactions which have valid legal consequences are not easy to characterise as 'artificial' unless some standard can be established to determine what is 'natural' for the same purpose. Such standards are not easy to establish. Wide and general provisions may go too far and catch innocent transactions.

11.25 A further problem is that, like beauty, tax avoidance often lies in the eye of the beholder. It was clear to us in discussions that some regarded tax-related lending as a severe case of tax avoidance, while others thought it was an efficient and effective industrial incentive. Under existing arrangements, is a family buying a bigger house doing so because it needs more space or wholly or mainly for tax reasons? It seems to us that it is very difficult to apply general anti-avoidance provisions except in an arbitrary and subjective fashion.

11.26 Finally, a general provision only has an advantage if the legal system allows the legislature's intentions to be taken into account. Otherwise a general anti-avoidance provision would be in conflict with the general law. It is not possible to foresee the attitude of Irish courts to a general provision such as the German one, whereas specific measures, if properly drafted, would be enforced.

### **Retrospective Anti-Avoidance Legislation**

11.27 We now consider the question of retrospective or retroactive anti-avoidance legislation. By this we mean the enactment of provisions which have effect before a date when the intention to legislate was announced in the Oireachtas.

11.28 Such an approach would not be tolerated in the general law. Article 15.5 of the Constitution expressly states that

"The Oireachtas shall not declare acts to be infringements of the law which were not so at the date of their commission."

11.29 We consider that the same principle should apply to taxation; indeed the Courts may well take this view. This has not been tested as yet. We recommend that anti-avoidance legislation should not apply before the date when the intention to legislate was announced.

### **Conclusions**

11.30 The present tax system creates the ideal environment for tax avoidance. This situation will remain as long as marginal tax rates in Ireland are very high and taxes vary on different forms of income and different forms of transactions. Much simpler and comprehensive taxation seems the only avenue towards a solution and we feel that we have already made proposals along such lines. Piecemeal attempts to deal with tax avoidance are likely to end up merely as skirmishes between taxpayers, legislature and the Revenue Commissioners.

11.31 Even with simpler taxation, there will still be some scope for tax avoidance, albeit on a much smaller scale. We consider that appropriate specific provisions are the best means of dealing with such avoidance.

### **Recommendations**

11.32 We make the following recommendations:

1. The system of taxation should be simplified as quickly and as widely as possible in line with our previous proposals. Simplified taxation is the best way to remove the conditions conducive to widespread tax avoidance.
2. In the context of the general system of taxation proposed in our earlier reports, tax avoidance should be dealt with by the enactment of appropriate specific provisions.
3. Anti-avoidance legislation should not apply before the date when the intention to legislate was announced.

Part IV

**Examination, Collection and  
Enforcement**

## CHAPTER 12

### INFORMATION POWERS OF THE REVENUE COMMISSIONERS

#### Introduction

12.1 In this chapter we examine the powers of the Revenue Commissioners to seek information from taxpayers and to verify the accuracy of returns made by trading taxpayers and the corporate sector. These include powers to call for information and documents and to inspect records. In this context we consider the obligations of traders to keep records. We also examine and make recommendations regarding the reporting requirements of banks, building societies and other third parties.

#### Principles

12.2 The granting of powers to the Revenue Commissioners to compel individuals to supply information, either concerning their own affairs or the affairs of other taxpayers, results inevitably in taxpayers being put to inconvenience, trouble and expense to supply the information. Therefore, any requirement to supply information should relate only to that which is strictly necessary to ascertain true liability. The information provided should be both useful and used. Otherwise it should not be sought. Regard should also be had to the costs of supplying the information and a reasonable balance struck between these and the utility of the information to the Revenue Commissioners.

12.3 We see no merit in having draconian provisions on the statute book which are used rarely, if ever. Any powers given to the Revenue Commissioners should be used and the Revenue Commissioners should be accountable for their use. Wide-ranging powers should not be provided on the grounds that they will be applied only in a small number of serious cases unless the legislation specifically limits their use to such cases.

## SCOPE OF INFORMATION POWERS

12.4 The basic information power of the Revenue Commissioners in relation to taxpayers is the power to call for a return of income. In the case of the business sector, other powers are available to verify the accuracy of returns. The existing information powers of the Revenue Commissioners in relation to trading taxpayers and the corporate sector have grown up on an *ad hoc* basis. There are many inconsistencies between the requirements for different taxes and between the obligations laid upon different sectors. A review is needed. We begin by summarising the information powers prescribed for income tax and corporation tax, PAYE and value-added tax. We then consider the persons from whom information about tax liabilities can be obtained and the nature of the information which should properly be available.

### Income Tax and Corporation Tax

12.5 The Revenue Commissioners may call for production of a company's or a trader's books and records, inspect them on the premises and verify transactions with business customers or suppliers.

12.6 Where a person fails to deliver the statement of his income when required to do so by an inspector of taxes or where the inspector is not satisfied with the statement, an inspector or authorised officer may require him to produce accounts, (including balance sheets) books and records. There is also provision for the inspector of taxes to take copies of or extracts from any books, accounts or documents made available for his inspection.

12.7 An authorised officer<sup>1</sup> may enter business premises to obtain information from the taxpayer in connection with his own tax liabilities and

- (i) require the person carrying on the trade or profession or any person who is employed by the person carrying on the trade or profession, to produce any books, records, accounts or other documents relating to the trade and may remove and retain such books, records, accounts or other documents for such period as may be reasonable for their examination,
- (ii) examine such books, records, accounts or other documents and may take copies of or extracts from the books, records, accounts or other documents,
- (iii) examine any property listed in any balance sheets, stock sheets or other such statements, and

<sup>1</sup>Section 34 of the Finance Act, 1976. (Power to obtain information from the taxpayer and to enter the trading premises).

- (iv) require the person carrying on the trade or profession or his employees to give to the authorised officer all reasonable assistance.

Banking business is excluded from the scope of the power. There is also protection for professional communications of a confidential nature.

12.8 While all inspectors of taxes can call for production of books and accounts, only some officers are authorised to enter business premises and remove and retain the records; this includes the inspectors and accountants in the Investigation Branch. The local district inspectors do not have a general authorisation but they can seek it.

12.9 Where an inspector of taxes is not satisfied with the accounts of a business and where acceptable reasons for the apparent discrepancies are not forthcoming, the records can be checked against information<sup>2</sup> sought from the taxpayer's business suppliers or business customers. This power does not apply to banking business. In the case of the taxpayer's professional advisors, there is protection for professional communications of a confidential nature and only information and documents relating to the payment of fees or otherwise relevant to the tax liability of the taxpayer may be sought.

12.10 As noted in paragraph 12.8, a limited number of officers is specially authorised to enter traders' premises to check books and records. The power to obtain information from a trader's business suppliers or customers is also exercised by a limited number of officers. The Revenue Commissioners can effectively authorise any officer serving in the department but in practice they do not. When introducing the provision to enable authorised officers of the Revenue Commissioners to enter premises, the Minister for Finance stated that

"I am prepared to give an assurance that as far as I am concerned I will be at pains to impress on the Revenue Commissioners that this power is to be exercised very carefully and that only people who are in the investigation branch or work which is necessarily related to this particular branch should be given this power. We can be assured that the Revenue Commissioners will not proceed to use this power recklessly or widely because they would not wish that junior officers should have power of this kind which obviously is one which must be exercised with very great caution in the interests of the taxpayers and those of the Revenue Commissioners themselves".<sup>3</sup>

However, the power rests with the Revenue Commissioners to appoint more officers to carry out these duties.

<sup>2</sup>The power to seek such information is conferred on the Revenue Commissioners by Section 31 of the Finance Act, 1979. (Power to obtain information from persons other than the taxpayer).

<sup>3</sup>Dáil Debates, — Vol. 290 Co. 1655, 19 May, 1976.

12.11 Although the Revenue Commissioners do not have a general power to seek information from a bank about transactions with its customers, they may apply to a judge of the High Court for an order requiring a financial institution to furnish particulars of all accounts maintained by any individual resident in the state. This power<sup>4</sup> does not extend to the accounts of companies. Information may be sought regarding accounts maintained during a period of ten years prior to the date of the application, despite the fact that banks, like any other business, are required to keep records for only six years. Where a judge makes an order he may also prohibit any transactions in relation to any account without his consent.

12.12 In addition to the specific powers to seek information, obligations are laid upon persons or institutions paying income, fees or interest to make information returns to the Revenue Commissioners. The most important of these, in terms of the volume of work generated, is the return by banks and financial institutions of interest paid on deposits. We discuss these general information returns later in this chapter.

#### **PAYE/Construction Industry Sub-Contractors**

12.13 Specific information powers prescribed for the control of PAYE include the power to inspect an employer's records from time to time at the employer's premises. A similar power exists for the control of tax deducted under the construction industry scheme for sub-contractors.

#### **VAT**

12.14 VAT is a self-assessed tax. As such, the information powers required are extensive. The VAT information powers<sup>5</sup> may be exercised without need to show grounds for dissatisfaction. They are there to enable the Revenue Commissioners to check the accuracy of returns. An authorised officer of the Revenue Commissioners may enter any premises in which he has reason to believe that business is being carried on, he may request or search for any business records, inspect them and remove them for a reasonable period. Since 1984 the powers have been extended to allow search for goods which, it is suspected, have been excluded from the trading records.

#### **THE ISSUES**

12.15 In this section we consider the issues which arise in relation to the information powers of the Revenue Commissioners. These are

<sup>4</sup>Granted by Section 18 of the Finance Act, 1983.

<sup>5</sup>Section 18 of the Value-Added Tax Act, 1972.

- (i) the powers of entry and inspection of records,
- (ii) a code of conduct for visits to business premises,
- (iii) the search of premises,
- (iv) the power to search persons,
- (v) the power to obtain information from business customers and suppliers,
- (vi) the power to obtain information about tax avoidance,
- (vii) the treatment of banking,
- (viii) general information returns,
- (ix) international exchanges of information, and
- (x) the obligations on traders to keep records.

#### **Powers of Entry and Inspection of Records**

12.16 The powers to enter premises for income tax and corporation tax purposes are, as we have noted, restricted in practice to a small number of senior officers of the Revenue Commissioners. Their use is limited, such powers are used on average in about four cases a year. The powers to enter premises for VAT purposes are exercised on a daily basis by officers of the Revenue Commissioners. There were 30,111 visits in 1984. Over a period of years virtually every trader registered for VAT is visited.

12.17 Since VAT is a self-assessed tax with registered traders themselves responsible for submitting returns of their own liability, it is essential for the effective verification of tax declarations that the officers of the Revenue Commissioners should be able to compare the declared tax liabilities in the returns against both the records and accounts of the business. It is also necessary to be able to examine the systems used to record transactions.

12.18 In relation to the examination of accounts for income tax and corporation tax, we consider that the Revenue Commissioners need the same level of assurance about the reality of transactions and the completeness of records as any auditor carrying out a statutory audit. In this regard we note the emphasis which Irish and international audit guidelines now lay on the need for an auditor to carry out personal checks at the business premises. Section 163 of the Companies Act, 1963 provides that

"Every auditor of a company shall have a right of access at all reasonable times to the books and accounts and vouchers of the company, and shall be entitled to require from the officers of the company such information and explanations as he thinks necessary for the performance of the duties of the auditors."

12.19 We asked the Revenue Commissioners why the power to visit traders' premises in relation to income tax and corporation tax is limited at present to a small number of senior officers and only rarely used. They replied that

"independent audits by officers of the Revenue Commissioners would not produce much revenue. More attention is being paid to non-accounts cases which are more fruitful and certified accounts where the auditor's report indicates that there are fundamental weaknesses in the accounting procedures. Our policy is one of critical rather than 'in-depth' examination of accounts. 'In-depth' examination which attempts to reconstruct the profits of a case can be very costly to the taxpayer and wasteful of our resources. If results are not forthcoming, the investigative system is discredited. The power to enter premises and check records for income tax and corporation tax has not been widely used and is limited to a small number of our senior officers. The Dáil Debates at the Committee Stage on Section 34 of the Finance Act, 1976 indicated a lack of willingness to allow us to use this power widely. Nevertheless, it is hoped that it will be possible to have each District Inspector made an 'authorised officer' for the purposes of Section 34 of the Finance Act, 1976 thus enabling him to enter business premises and remove and retain records where necessary. The existing provisions are considered defective in that they do not allow the 'authorised officer' to search for documents and records. In this area our policy is 'to hasten slowly'."<sup>6</sup>

12.20 The Consultative Committee of Accountancy Bodies — Ireland advised us that

"Evasion could be tackled more effectively by increasing field staff. The CCAB-I would not object to audits on business premises by senior, trained, Revenue personnel."<sup>7</sup>

12.21 We conclude that the powers of the Revenue Commissioners to visit business premises to inspect books and records and to get a firsthand impression of the business are necessary to check the accuracy of returns of trading profits. In order to deal with evasion and to ensure that tax returns are made for all businesses it is also necessary that powers extend to premises where there is reason to believe that a business is being carried on. Once on the premises, the powers of an 'authorised officer' in relation to the inspection of books and records, the checking of stocks and the recording of transactions should be the same as those of an auditor carrying out a statutory audit.

<sup>6</sup>Agreed note of meeting, 12 December, 1984.

<sup>7</sup>Agreed note of meeting, 12 November, 1984.

12.22 We recommend that the powers of the Revenue Commissioners to enter premises and check books and records should be harmonised for all direct taxes (income tax, including PAYE, deductions under the construction industry scheme and corporation tax) and VAT. This could best be done under a general provision allowing checks at business premises for any tax. The provision should enable the inspector of taxes and any other authorised officer to exercise such powers. The harmonisation of the powers of entry to business premises would ease the change to a system of integrated units to deal with all the tax affairs of a trading entity, as discussed in Chapter 10.

### Code of Conduct

12.23 Visits from the taxman are a burden on the taxpayer. They can cause anxiety even when the taxpayer is making every effort to make a full return. Since VAT is the only tax for which businesses are likely to be visited at present, this burden is limited, in practice, by the long intervals between visits. In such circumstances we do not find the burden excessive nor the intrusion unwarranted. We envisage a similar situation in relation to the checking of self-assessed returns of Schedule D profits.

12.24. Because checking visits are an intrusion, it is vital that officials behave in a reasonable way and that the taxpayer is made aware of his rights and duties in relation to such visits and of the statutory provisions which apply. We consider that this requirement can best be met by informing the taxpayer in writing of his rights, duties and the statutory safeguards. The taxpayer should also be afforded the opportunity of having his accountant present during checking visits if he so wishes.

12.25 The following matters require to be covered in any notification to the taxpayer:

- (i) the purpose of the visit,
- (ii) the possibility of having the taxpayer's accountant present,
- (iii) the inspection and information powers of the visiting officer and, in particular
  - (a) what the official may inspect,
  - (b) what information the official may ask for,
  - (c) where the records and documents should be produced, and
  - (d) what the requirements relating to the removal of documents are and similar information relating to the giving of receipts and the provision of copies of documents removed and the taxpayers' right of access to the records,

- (iv) the possible consequences of the discovery of errors, and
- (v) the taxpayer's rights of appeal in cases of dispute.

12.26 We recommend that an explanatory booklet covering these matters should be prepared by the Revenue Commissioners and issued to all traders. The booklet should be re-issued to traders before a checking visit begins.

### Search of Premises

12.27 We have already noted that the value-added tax legislation includes a provision to allow an authorised officer of the Revenue Commissioners to search for books, vouchers and for goods which may have been excluded from the trading records. Indeed the VAT search power is so widely drawn that it may even allow Revenue officials to carry out personal searches. The direct tax legislation contains no comparable search powers.

12.28 The Revenue Commissioners told us that

"the power of search is necessary for VAT control and has been extended in the Finance Act, 1984 to allow a search for goods which may not have been included in the trading records. By international standards the power is quite narrow.<sup>8</sup>

12.29 In the United Kingdom, if there are reasonable grounds to suspect that an offence in connection with value-added tax has been committed, a justice of the peace or a magistrate may issue a warrant authorising the entry and search of premises, whether business or private. A person acting under such a warrant may seize and remove any documents or other things found on the premises reasonably required for evidence and may search any person found there whom he reasonably believes has committed or is about to commit an offence.

12.30 In their evidence to the Keith Committee,<sup>9</sup> the Department of Customs and Excise in the United Kingdom, which has responsibility for the administration of VAT, stated that

"they regarded the search warrant power in VAT as essential in serious cases, to protect the revenue from the minority who deliberately engaged in fraud, particularly in respect of VAT repayments and postponed accounting. Such persons were unlikely to produce evidence of their fraud voluntarily. Since the start of VAT, Departmental

<sup>8</sup>Meeting with the Revenue Commissioners, 12 December, 1984.

<sup>9</sup>Report of the Committee on Enforcement Powers of the Revenue Departments. The Rt Hon The Lord Keith of Kinkel PC. Volume 1, PPs 235-236.

guidelines for the use and execution of VAT search warrants had been kept under review. . . . Against this background, and given the number and scale of frauds proved where the evidence could only have been obtained by means of search under warrant, the Department considered that the power was well justified."

The Department of Customs and Excise in the United Kingdom did not seek a general power to search without the procedure of getting a warrant from a justice of the peace or a magistrate.

12.31 In cases involving deliberate fraud, documents containing evidence of the fraud would be largely in the possession of the taxpayer himself and might not be kept on the business premises. Such documents would not be produced voluntarily if demanded, even if the demand were made on the spot without notice. If notice of suspicion were given, incriminating documents would likely be destroyed or removed to an unknown place. With this in mind, we consider that for VAT it is reasonable for the Revenue Commissioners to have a power to search premises. However, it is undesirable that the VAT search power should be any wider than it needs to be. We therefore recommend that the power to search should only be available under warrant issued by a District Justice where there is reasonable ground for suspecting that an offence of fraud in relation to, or in connection with, VAT has been committed and where there is reasonable ground for suspecting that evidence of that offence is to be found on specified premises (whether or not the offence was committed there). The considerations applicable to the direct taxes are in our view the same as in VAT and we see no good grounds for differentiating between the various taxes. We therefore recommend that a similar power be enacted in respect of direct tax searches under warrant.

### Power to Search Persons

12.32 We have already noted that the VAT search power is very widely drawn and may even extend to personal searches of persons found on the premises. However, this is not clearly set out in the legislation.

12.33. In the United Kingdom, an officer acting under the authority of a VAT search warrant may search any person found on the premises whom he has reasonable cause to believe has committed or is about to commit a VAT offence or is in possession of evidence of such an offence. No woman or girl is to be searched except by a woman. The Keith Committee recommended that

- (i) the power be limited to the search of persons whom there is reasonable cause to believe are in possession of evidence of an offence of fraud in relation to or in connection with VAT, and

- (ii) the existing safeguard that a woman or girl should only be searched by a woman be retained.

12.34 If a substantial fraud has taken place, the documentation may be too bulky to conceal about the person. However, it is possible that in the course of VAT searches, evidence of fraud could be concealed on the person of suspects. If the Revenue Commissioners are to combat fraud successfully, they must have a sanction against anyone who, to avoid prosecution, blatantly conceals evidence of fraud about his person during the course of a search of premises. We believe a power of search on reasonable suspicion is justified. The direct tax legislation contains no power to search persons. The considerations applicable are in our view the same as in VAT and we see no good grounds for differentiating between the various taxes.

12.35 We recommend that an officer of the Revenue Commissioners, acting under the authority of a search warrant, should have the power to search persons whom there is reasonable cause to believe are in possession of evidence of an offence or fraud in relation to or in connection with VAT or the direct taxes. The person executing the search warrant should also be empowered to take with him such other persons as appear to him to be necessary. This would enable the person entering the premises to be accompanied by a Garda to provide reassurance to the occupier or, if necessary, to prevent a breach of the peace.

#### **Power to Obtain Information about Named Taxpayers**

12.36 The Revenue Commissioners have power to serve a formal notice for the production of documents on the business suppliers and business customers of a named taxpayer for the purposes of enquiring into the tax liability of the taxpayer. The scope of the power extends to particulars of any business transactions but notice may only be served on persons who themselves carry on a business or profession. Thus, non-business customers cannot be asked to produce information about their transactions with traders. Banking business is also excluded and there is protection for professional communications of a confidential nature. Before a notice may be served on a business supplier or business customer, an inspector of taxes must advise the taxpayer under investigation that he is not satisfied with the accounts submitted and that he has requested an authorised officer to issue a notice seeking independent information.

12.37 In our discussions with them the Revenue Commissioners did not indicate a wish to extend the existing scope of the information power, other than to comment on banking business which we discuss later. Neither did we receive any submissions about the operation of this aspect of the information powers of the Revenue Commissioners. However, this is a

relatively new provision introduced by the Finance Act, 1979 and, so far, its use has been limited.

12.38 This power is invoked in selected cases under investigation. A trader who is required to provide information about transactions with another trader under investigation is placed in a very difficult position. He will undoubtedly feel aggrieved that he should be singled out to provide information and, from a commercial point of view, he must reconsider whether he should continue to do business with someone whose affairs are under investigation by the Revenue Commissioners. In extreme criminal cases there is the possibility that the trader might be intimidated by the taxpayer under investigation. The alternative to the existing powers is to place a general obligation on all traders to deliver information returns showing sales to business customers and purchases from business suppliers. This would place heavy compliance costs on traders and the Revenue Commissioners would not be able to cope with the volume of information.

12.39 In Chapter 1 we set out the elements of a good system of tax administration. In our view, only as much information as can be efficiently processed should be gathered and there must be an efficient system for converting the selected information into a form useable for enforcement purposes. The independent information necessary to verify transactions and to establish tax liabilities in cases under investigation for tax evasion can be efficiently gathered only if it is done in selected cases. Against this background we consider that the existing power is necessary and justified. We recommend that the power to obtain independent information from business suppliers and business customers should be retained.

12.40 Anyone who conceals, exports or destroys documents which are subject to a notice requiring their production should be liable to a penalty. In our view, the appropriate penalty should be a criminal, not a civil, one in order to mark the seriousness of attempting to obstruct due process.

#### **Power to Obtain Information about Tax Avoidance**

12.41 An information power is included in the anti-avoidance legislation regarding the transfer of assets abroad. This can be used by the Revenue Commissioners even if they cannot specify any specific transaction or identify a taxpayer for whom they require information. Indeed the power is used largely to get details of the names and addresses of persons involved in particular types of transactions. For example, in a case<sup>10</sup> which reached the courts in the United Kingdom under an exactly similar provision, the London representative of a Bermuda bank was asked for particulars of the

<sup>10</sup>Clinch v CIR (1973), 49TL52.

formation and management of foreign companies and partnerships. The court upheld the validity of the notice issued by the Inland Revenue.

12.42 In December, 1982, an officer of the Revenue Commissioners, acting under the authority of this legislation, issued notices to a number of firms of accountants and solicitors, seeking information about the formation and management of foreign companies, foreign partnerships and foreign settlements and the transfer of assets to such bodies. The information sought referred to the period from 6 April, 1972 to the date of the notice, even though the legislation was introduced only in 1974. The firms were required to give details of any transactions or operation of a kind specified in the notice which had been carried out by any partner or any member of the staff over the period of some ten and a half years. The scope of the information required extended to cases where advice had been given and where clients had been introduced to other persons with a view to the carrying out of specified transactions or operations. The firms were given forty days to comply with the terms of the notice. This type of all-embracing request for information is unreasonable and effectively impossible to comply with. It highlights the need for the Revenue Commissioners to act reasonably. A specimen copy of a notice is reproduced in Appendix 3.

12.43 In Chapter 10 we recommended that appropriate specific provisions are the best means of dealing with avoidance. Such anti-avoidance provisions in legislation must be backed up with powers which enable the Revenue Commissioners to operate them, including, in particular, powers to obtain information. We do not favour a general provision for anti-avoidance enquiries. The information powers of the Revenue Commissioners in connection with the transfer of assets abroad are clearly too widely drawn. We consider that information regarding specific anti-avoidance transactions and connected operations should be required to be notified to the Revenue Commissioners by tax practitioners and professional advisers on a current basis, rather than retrospectively over long periods. Such obligations should be enacted in each situation when they are required and there should be substantial penalties for failure to comply.

### **Treatment of Banking Business**

12.44 Banking business is largely excluded from the scope of the information powers of the Revenue Commissioners. In particular, the Revenue Commissioners may not enter banking premises to inspect books and records, although it is open to the inspector of taxes to require banks to forward their books for examination. Information may not be sought from other businesses in order to check the accounts of a bank nor may banks be asked to supply particulars of business transactions with other taxpayers. The Revenue Commissioners advised us that the Irish Banks' Standing Committee successfully argued that if third party information powers were

extended to domestic institutions only, their competitive position vis-à-vis foreign institutions operating here would be undermined. If the powers were extended to all institutions it could have serious effects on the domestic money market. There are some £2.5 billion external deposits (including foreign currency deposits) with Irish banks and exchange controls are ineffective. The Revenue Commissioners have, nonetheless, tried to have the powers extended.

12.45 It was put to us that the justification for this differential treatment of banking business, as a source of information available to the Revenue Commissioners, lies in the fact that, unlike other businesses, the relationship of banker and customer gives rise to a duty of secrecy on the part of the bank. This duty is not merely a moral duty, it is actually enshrined in the constitution of banks generally, that is, in the Articles of Association or Bye Law of a bank. However, the banks' duty to secrecy is not an absolute duty and compulsory disclosure by a bank of the affairs of a customer may be required from time to time under provisions of law or orders of court.

12.46 The main departure<sup>11</sup> from the general exclusion of banking business as a source of information available to the Revenue Commissioners is Section 18 of the Finance Act, 1983 which enables the Revenue Commissioners to apply to the High Court for an order requiring financial institutions to furnish full particulars of all accounts maintained by any person. This legislation strikes a balance between the conflicting interests of the traditional kind of confidentiality between a banker and his customer and the need for an effective means of preventing and detecting tax evasion. In addition, tax legislation<sup>12</sup> treats banking business in the same way as any other business in respect of production of the bank's books for the purpose of the bank's own assessment of tax.

12.47 We asked the Central Bank for its view of an extension of the powers of the Revenue Commissioners as they apply to banks. It replied that

"the Bank agrees in principle that banking business should be treated in the same way as any other business as regards the checking of banks' records by the tax authorities. It is of the view, however, that it would be extremely difficult to maintain confidence in the normal relationship between banks and their customers if there were to be unrestricted

<sup>11</sup>The anti-avoidance legislation regarding transfer of assets abroad does not impose any obligation on a bank to supply information about ordinary banking transactions between banker and customer carried out in the ordinary course of banking business, unless the bank has acted or is acting on behalf of the customer in connection with the formation or management of a closely held company resident or incorporated outside the state or in connection with the creation or execution of certain trusts or settlements.

<sup>12</sup>Section 174 of the Income Tax Act, 1967.

access to the customers' accounts by the Revenue Commissioners. The Bank would be concerned that an erosion of that confidence would result in an outflow of funds abroad from both resident and non-resident accounts.<sup>13</sup>

12.48 The existing powers ensure that the Revenue Commissioners may seek from financial institutions particulars of all accounts maintained by a taxpayer and information relating to the financial transactions of the taxpayer recorded in the books of the financial institution going back over a period of ten years. We are satisfied that this facility should continue to operate, subject to the safeguard that when the Revenue Commissioners seek such particulars, they must apply to the High Court for an appropriate order. We make no recommendations for change in the existing treatment of banking business as a source of information available to the Revenue Commissioners.

### Occasional Information Returns

12.49 The most widely known and most extensively used general information requirement is the return by banks of interest paid or credited to a depositor. The Revenue Commissioners also have powers to require a person to deliver

- (i) a return of fees and commissions paid by a person carrying on a trade or business,
- (ii) information concerning interest paid without deduction of tax by persons other than financial institutions, for example, solicitors who hold clients' money on which interest becomes payable,
- (iii) details of receipt of taxable income belonging to others,
- (iv) lists of lodgers and inmates, and
- (v) lists of employees, together with particulars of any preferential loans made to any employee and the payments made to employees including wages, salaries, expenses and expense allowances.

12.50 Table 17 shows the present reporting requirements of financial institutions. Most financial institutions are required<sup>14</sup> to report to the Revenue Commissioners all interest exceeding £50 per annum paid or credited to depositors. Particular arrangements apply to the disclosure of interest paid to non-residents. We discussed these in Chapter 5. Building societies are not subject to these disclosure requirements.

<sup>13</sup>Letter of 23 July, 1985.

<sup>14</sup>Section 175 of the Income Tax Act, 1967.

TABLE 17

### Reporting Requirements of Financial Institutions

Institution	Revenue Commissioners to be Notified of Interest Paid or Credited in Excess of:
Associated Banks	£50
All non-associated Banks	£50
Building Societies	No Disclosure Required
ACC and ICC	£50
Post Office Savings Banks	£50
Trustee Savings Banks	£50

Source: Taxes Acts

12.51 In a submission, the Central Bank of Ireland said that

"In order to remove the inequities and inefficiencies resulting from the differences between institutions in reporting requirements and any consequent distortions in the allocation of deposits, it is recommended that all financial institutions be required to supply information to the Revenue Commissioners on a comparable basis. It is proposed, therefore, that all interest on deposits of residents with financial institutions be notified by these institutions to the Revenue Commissioners. Banks which operate branch networks should be required to aggregate interest on all accounts belonging to a customer (even if held in different branches) for the purpose of reporting to the Revenue Commissioners."

12.52 The Irish Building Societies' Association submission rejected any suggestion that they be brought within the Scope of Section 175 of the Income Tax Act, 1967 on the grounds that

"it would have disastrous effects on investors' confidence in the societies. It has always been accepted that savings with building societies are not subject to scrutiny by the Revenue (Commissioners)."

12.53 We believe that the Revenue Commissioners should receive information from financial institutions to enable them to verify tax returns made by taxpayers. The exclusion of building societies from the obligation to return information to the Revenue Commissioners facilitates tax evasion and creates an anomaly in the tax treatment of financial institutions. We recommend that building societies be subject to the same disclosure requirements in respect of interest as other financial institutions.

12.54 If it is thought that the existing reporting requirements are too onerous to impose on building societies, the reporting requirements for other financial institutions should be brought into line with those which apply to building societies. Unless disclosure requirements are comprehensive, they are virtually useless in tracking evasion and merely succeed in distorting the market for deposits.

12.55 Under our proposals for the taxation of banks and building societies, income tax on real interest would be paid in full through the composite payment system we have already recommended in Chapter 5. We think that this reduces the need to have relatively small amounts of interest returned. In this context we recommend that the automatic reporting limit be raised substantially and applied to all financial institutions. We stress that there is no necessary link between any exemption threshold for deposit interest and the limit for reporting requirements.<sup>15</sup>

12.56 Insurance companies also offer a range of investment policies to the public. These provide a safe haven for untaxed income because insurance companies are under no obligation to make information returns to the Revenue Commissioners. We consider that insurance companies should be obliged to make returns relating to certain forms of investment-related policies on the same basis as other institutions. We have in mind transactions involving the payment of large single premiums.

12.57 Details of interest should be submitted on computer tape by financial institutions and other information reporters with computer facilities. The simplest way to achieve linkage of the information returns with the correct taxpayer's file is for the taxpayer himself to be required to provide details of his Revenue Social Insurance (RSI) number to the information reporter. In our view, such an additional requirement would not breach the confidentiality of the individual's tax affairs in relation to his bank or building society. Businesses are already required to show their tax reference number on receipts and other documents. We also think that the Revenue Commissioners could supply tax reference numbers to financial institutions in cases in which they had already identified accounts.

12.58 Present requirements about notifying the taxpayer are not uniform. We find it difficult to see the reason for any distinction between them, other than the obvious one of scale and certainly we see no difference of principle between an employer's PAYE return and a bank's return of interest credited, a trader's return of fees or commission paid and an agent's return of the income of others. Yet only in the first case is there an obligation on the person giving the information to tell the third party what he has told the Revenue Commissioners. Notifying the taxpayer as well as the Revenue Commissioners of the particulars in the returns might, over time, be expected to tend to reduce the work of the Revenue Commissioners by reducing the number of discrepancies between returns made by taxpayers and information returns. We recommend that all information reporters should be placed under a statutory obligation to notify the taxpayer of the amount of income reported to the Revenue Commissioners and the period

<sup>15</sup>Changes in the exemption limits for certain categories of taxpayers in 1984 and 1985 mean that the exemption limits and the limit for reporting requirements no longer coincide in all cases.

to which it relates. The precise method of satisfying this requirement would have to be agreed with the bodies obliged to comply.

### Compliance Costs

12.59 We consider that compliance with the obligation to make general information returns of payments made is part of a civic duty and that costs of compliance should remain the responsibility of the citizen and should not be recoverable from the Revenue Commissioners. Neither should the costs of advising the taxpayer of the amount of income reported be recoverable. Specific requests to provide detailed information relevant to the tax liabilities of another taxpayer could put a person to a great deal of work for which he may be unable to charge the taxpayer. We feel that the costs of complying with specific, as opposed to general, requests for information about the affairs of other taxpayers should be borne by the Revenue Commissioners where they are shown to be material. We recognise that there can be difficulties in quantifying such costs but we do not consider this to be an insuperable problem.

### International Exchanges

12.60 The Revenue Commissioners are involved in exchange of information on an international basis under various double taxation treaties, an EEC directive and under customs' conventions, some involving European Community members only and others of wider application. In addition, in respect of VAT, customs' duties and agricultural levies, exchange of information takes place under various Community directives relating to Mutual Assistance and the Mutual Recovery of Debts.

12.61 All the conventions and instruments under which exchange of information takes place provide, with little difference in wording, that the Revenue Commissioners may refuse to make available information if to do so would, in their opinion, involve disclosure of an industrial, commercial or professional secret. However, while the Revenue Commissioners may refuse to pass on such information when requested to do so, they may not be always in a position to recognise when information of this nature is being requested.

12.62 Since both the Revenue Commissioners and taxpayers are concerned to ensure that commercially secret information is not passed on, we recommend that

- (i) there should be a procedure whereby, when the Revenue Commissioners are requested to pass on to foreign revenue authorities information which they hold, the taxpayer should be informed,
- (ii) the taxpayer should have the opportunity of stating either that he

is content with the information being passed on, or that he regards such information as commercially secret, together with his reasons for so regarding it, and

- (iii) where a dispute arises between the taxpayer and the Revenue Commissioners as to whether information is commercially secret or not, it should be referred to the Appeal Commissioners.

### Obligation to Keep Records

12.63 The legislation governing the records to be kept for income tax and corporation tax purposes is in general terms because of the variety of records held by different trades and businesses. The list of records and the form of records to be kept for VAT and PAYE is more specific and is governed by regulations made by the Revenue Commissioners. The provisions governing the records to be kept by businesses for income tax, corporation tax, value-added tax and PAYE are set out in Appendix 4.

12.64 We accept the arguments against attempting to prescribe the form of records to be kept for income tax purposes. This choice should be made by the taxpayer, subject to certain minimum standards. We make no recommendations for change in the legislation governing the records to be kept for income tax and corporation tax.

### Period of Retention

12.65 The period of retention for all books, records and documents is the same for income tax, corporation tax, value-added tax and PAYE/PRSI. These business records must be preserved for six years unless the written permission of the inspector of taxes has been obtained for their retention for a shorter period. This permission is given subject to conditions.

12.66 We are concerned to strike a balance between imposing an unreasonable burden on individual traders and the Revenue Commissioners' potential need to examine original records for control or investigation purposes. One problem is that the period of retention does not coincide with the period of years 'in date' for normal assessment purposes or the purposes of Irish repayment claims. An assessment may be made within ten years of the end of the year of assessment to which it relates. Where fraud or neglect is involved, an assessment may be made at any time for any year for which tax would otherwise be lost to the Exchequer. The time limit for repayment claims is ten years.

12.67 It is desirable that the period of retention of records and the time limits for assessment and repayment purposes should coincide. A change

to a self-assessment system would not change the argument in favour of a fixed period of retention for most business records. In the United States, records must be kept as long as they may be needed in the administration of any Internal Revenue Law. In practice, records supporting items on a tax return are needed for a maximum of three years.<sup>16</sup> However, some records must be kept indefinitely, for example, records supporting a decision to change the method of accounting for stocks and records relating to property. We favour a fixed period for the retention of business records under self-assessment. The present time limit of six years should be kept under review in the light of the operation of self-assessment. When the change to a system of self-assessment for all business as recommended in Chapter 4 is made, the general time limit for assessments and repayment claims should be reduced to six years.

### Micro-film Records

12.68 We also realise that the retention of supporting records, such as invoices, places a burden on traders in terms of storage costs. We recommended in Chapter 8 that traders be allowed to retain supporting records on microfilm, subject to technical specifications to be laid down by the Revenue Commissioners to deal with the quality of film and equipment.

### Recommendations

12.69 We recommend that:

1. There should be a single power of entry to business premises, on notice, to ensure that returns are made for all businesses and to check the accuracy of returns of VAT, PAYE/PRSI and trading profits. All inspectors of taxes should be authorised to exercise this power.
2. A booklet setting out the rights and duties of traders should be prepared by the Revenue Commissioners and issued to all traders. The booklet should be re-issued before a checking visit begins.
3. The power to search premises should be available under warrant issued by a District Justice where there is reasonable ground for

<sup>16</sup>In the United States, individuals must keep records of income, deductions and credits shown on their tax return, as well as any worksheets used to figure them, until the statute of limitations runs out for that return. Usually this is three years from the date the return was due or filed or two years from the date the tax was paid, whichever is the later. Copies of the tax return must also be kept. Certain records must be kept longer. For example, property records, including those relating to a taxpayer's residence, must be kept as long as they are needed to figure the basis of the original or replacement property.

suspecting that an offence of fraud in relation to tax has been committed and where there is reasonable ground for suspecting that evidence of that offence is to be found on specified premises (whether or not the offence was committed there).

4. The existing VAT power to search premises should be brought into line with recommendation 3 above.
5. An officer of the Revenue Commissioners acting under the authority of a search warrant should have power to search persons whom there is reasonable cause to believe are in possession of evidence of an offence of fraud in relation to VAT or the direct taxes. The person executing the search warrant should also be empowered to take with him such other persons as appear to him to be necessary.
6. The powers of the Revenue Commissioners to seek independent information about a taxpayer's accounts and returns from his business suppliers and business customers, by virtue of Section 21 of the Finance Act, 1979, should be retained.
7. There should be an appropriate criminal penalty for any person who conceals, exports or destroys documents which are subject to a production notice.
8. Information regarding specific anti-avoidance transactions and connected operations should be required to be notified to the Revenue Commissioners on a current basis rather than retrospectively over long periods. Such obligations should be set down in each situation when they are required. There should be substantial penalties for failure to comply. We do not favour a general power to enable the Revenue Commissioners to seek information about anti-avoidance.
9. All financial institutions, including building societies, should be subject to the same reporting requirements.
10. The automatic reporting limit for interest paid by financial institutions should be raised substantially. This should be done when interest paid by such institutions is subject to withholding tax on the basis recommended in Chapter 5. For the purposes of the return, an institution should aggregate all the accounts held by a single individual with that institution.
11. Insurance companies should be obliged to furnish information returns to the Revenue Commissioners in relation to certain policies.
12. The Revenue Commissioners should explore with information reporters improved means of matching information with taxpayers'

files. In particular, the possibilities of requiring taxpayers to advise information reporters of their Revenue and Social Insurance number or the Revenue Commissioners supplying such information to the institutions appear desirable and should be investigated.

13. Any person or body who makes general information returns to the Revenue Commissioners concerning a taxpayer should be obliged to inform the taxpayer of the information reported.
14. The costs of complying with specific, as opposed to general, requests for information about the affairs of other taxpayers should be borne by the Revenue Commissioners where they are shown to be material.
15. Since international conventions for exchange of information provide that the Revenue Commissioners may refuse to make available information if to do so would, in their opinion, involve disclosure of an industrial, commercial or professional secret they should be required to notify the taxpayer of a request for information. He should then have the opportunity to object to disclosure on the grounds that the information is commercially secret, with any dispute being adjudicated by the Appeal Commissioners.
16. The period of retention of business records for income tax, corporation tax, value-added tax and PAYE/PRSI should remain at six years. When the change to a system of self-assessment for all business recommended in Chapter 4 is made, the general time limit for assessments and repayment claims should be reduced to six years.

## CHAPTER 13

# TAX OFFENCES AND PENALTIES

### Introduction

13.1 The system of penalties for tax offences exists to encourage taxpayers to comply with the law, to enable the Revenue Commissioners to collect the right amount of tax due, to make offences unprofitable and punish the most serious offenders. In this chapter we describe the present system and examine its application in general. We conclude that in order to establish an effective compliance code it is essential to have penalty procedures capable of being applied in a summary way, subject to a right of appeal by the taxpayer. We make our proposals for a new scheme of offences and penalties in the next chapter.

### Present Range of Offences and Level of Penalties

13.2 The Taxes Acts recognise two categories of offences in relation to direct taxes: minor regulatory offences (simple failure to comply with a notice within the prescribed time) and major offences (sustained failure to comply with obligations, or negligence or fraud in complying).<sup>1</sup> In addition to negligence and fraud, there is the concept of a wilful act or omission in relation to certain criminal offences. The tax code also recognises the possibility of innocent error on the part of the taxpayer. An error initially made innocently but which subsequently comes to the taxpayer's attention must be remedied without unreasonable delay. Otherwise the inspector can claim negligence. Broadly similar categories of offences apply in relation to VAT.

13.3 The primary form of sanction imposed is a monetary penalty,

<sup>1</sup>Simple failure by an individual to make a return for income tax runs for a maximum of two years before the offence turns into 'sustained failure', thereby falling into the major offence category. The penalty for simple failure is £500 increasing to £800 for sustained failure. Simple failure to submit a corporation tax return carries a penalty of £500 plus a daily rate of £50 for each day on which the failure occurs where a company fails to comply with a notice to deliver a return within a year from the date of the notice. There is a higher flat-rate penalty for sustained failure.

although the Finance Act, 1983 widened the scope of criminal penalties. For minor offences involving failure to submit returns, there is commonly a flat rate fixed amount and sometimes a fixed additional daily amount if failure continues after it has been established in penalty proceedings. Major offences consisting of sustained failure to submit a return or other document attract higher fixed penalties. The distinction between simple and sustained failure to make a return is not recognised in relation to employers' PAYE returns, VAT returns or certain information returns. All of these offences carry a level of penalty which suggest that they are regarded as major offences, irrespective of the length of the delay.

13.4 Where the offence involves the fraudulent or negligent delivery of incorrect returns of the taxpayer's own liabilities, the statutory penalty generally incorporates an element of tax-gearing, that is, the penalty increases in proportion to the amount of tax due on the income under-declared. The tax-gear penalties for fraud and negligence are 200 per cent and 100 per cent respectively of the unpaid tax. Similar penalties apply in relation to the delivery of incorrect returns for VAT but they do not apply in relation to incorrect returns by employers in respect of PAYE. Fraud or negligence in relation to third party returns normally attracts a flat-rate penalty.

13.5 Besides the various penalties, interest is chargeable at a rate of 15 per cent per annum on late payment of tax. This interest is not deductible in computing profits for tax purposes. The effective rate of interest, for a taxpayer or company paying tax at 50 per cent, is therefore twice as high as a comparable commercial rate of interest on money borrowed from a bank. Thus, the interest now chargeable has a penalty element. In the case of income tax and corporation tax, an even higher rate of interest of 24 per cent per annum is chargeable back to the original due date where an assessment is made to recover an undercharge attributable to fraud or neglect. The rate is set at a very high level because, in some cases, this special rate of interest may be the only significant monetary penalty which can be imposed. Since the interest is not deductible for tax purposes the effective rate of interest can amount to 50 per cent or more, depending on the rates of tax. The normal interest on late payment is not chargeable for any period for which the higher rate is due.

13.6 A complete list of penalty provisions in relation to income tax, capital gains tax, corporation tax and value-added tax is in Appendix 5.

### IMPOSITION OF PENALTIES

13.7 Penalties may be imposed only in proceedings before a court. The procedures are cumbersome, with the result that relatively few cases are pursued. Proceedings are generally in the name of the Director of Public

Prosecutions (DPP), however, the Collector General is authorised to institute proceedings in his own name for certain penalties. The Revenue Solicitor, the Chief State Solicitor or the local State Solicitors conduct the proceedings in the appropriate courts. Proceedings for certain penalties are taken in the High Court, irrespective of the amount involved, under legislation which allows the penalties to be recovered like civil debts. This means that juries are not involved in such cases. Proceedings in respect of incorrect returns involving fraud or neglect would only be taken where a settlement has not been reached. Where a settlement is reached, it is the practice of the Revenue Commissioners not to initiate legal proceedings.

13.8 Table 18 shows the number of cases in which penalty proceedings for failure to make a return were commenced in each of the years 1977 to 1982 together with the numbers finalised and the penalties awarded. The overall number of cases in which proceedings are initiated is small. However, the number of proceedings commenced in 1982 increased substantially in relation to earlier years. The Revenue Commissioners advised us that

“as the penalty action is undertaken primarily to force production of the required data in order to enable the inspector of taxes to correctly assess the tax liability, it is the practice to withdraw a case from the Revenue Solicitor where the relevant items are submitted by the taxpayer before legal action is commenced, that is, before a summons has been issued and served.”<sup>2</sup>

**TABLE 18**

**Penalty Proceedings: Failure by an Individual or a Company to Make a Return of Income**

Year	No. Commenced	No. Finalised	Total Penalties	Average Penalty
			£	£
1977	n.a.	54	45,176	837
1978	16	34	19,900	585
1979	82	33	27,805	843
1980	29	34	35,525	1,045
1981	95	33	29,480	893
1982	166	38	36,071	949

Source: Revenue Commissioners.

13.9 The existing penalty code is clearly ineffective in securing compliance. There is an urgent need for penalties which are specific and automatic to secure basic information.

13.10 Legal proceedings for the imposition of penalties are ordered by the Collector General for failure to remit PAYE tax and PRSI contributions monthly and for failure to furnish P35 end-of-year returns of PAYE and

<sup>2</sup>Letter 15 July, 1983.

PRSI particulars. Proceedings under income tax legislation are taken for failure to remit tax and furnish P35s; under powers devolved on the Collector General by the Minister for Social Welfare, proceedings are taken simultaneously for failure to pay PRSI and to furnish PRSI end-of-year particulars. The penalty sanction is directed mainly at P35 defaulters and is invoked in only a relatively small number of cases for non-compliance with PAYE/PRSI monthly payment obligations. The Revenue Commissioners advised us that

“the more appropriate action against payment defaulters is by way of estimation of amounts due and enforcement recovery action by the issues of certificates to sheriffs and county registrars or by legal proceedings through the courts. . . .

“Penalties, like interest, are seen as an additional item of charge and taxpayers are very reluctant to pay them. The Collector General has in some cases to deal with three items of charge, *viz.* the tax itself, penalties and interest. The additional items are a burden on the administration and deflect attention away from the collection of the tax.”<sup>3</sup>

13.11 Penalty proceedings in respect of a total of 3,724 PAYE/PRSI offences were ordered as follows in 1984:

failure to pay PAYE tax — income tax law	28
failure to pay PRSI — social welfare law	28
failure to furnish P35s — income tax law	2,008
— social welfare law	1,660
Total	3,724

13.12 The penalty sanction is invoked in only a relatively small number of cases for non-compliance with VAT payment obligations. As with PAYE, the Revenue Commissioners consider that action by way of estimation of amounts due and enforcement recovery action is more appropriate, although the number of penalty proceedings ordered has more than doubled in the past two years. Penalty proceedings were ordered in 917 cases in 1984 for failure to make VAT returns and payments.

### Back-duty Settlements

13.13 Formal penalty proceedings in relation to incorrect returns involving fraud or negligence are rarely taken. The Revenue Commissioners are empowered to mitigate any penalties and the normal course is to effect back-duty settlements without recourse to legal action. In the period from

<sup>3</sup>Letter of 15 July, 1983 and agreed note of meeting with the Revenue Commissioners, 12 December, 1984.

1977 to 1982 only two cases were fully processed through the courts; one defendant was adjudicated bankrupt and penalties of £4,391 were imposed in another case. A further three cases were withdrawn on the basis of agreed settlements.

13.14 We asked the Revenue Commissioners to outline the basis on which back-duty settlements are made. They advised us that

- “(i) The tax is agreed. It is not negotiable.
- (ii) The inspector then decides the amount he is prepared to accept in settlement of the liability to penalties and interest having regard to the various factors involved including
  - (a) the gravity of the offence
  - (b) the level of co-operation
  - (c) the strength of the penalty/interest position
  - (d) ability to pay.

For example, in a straightforward case, he may be prepared to accept 50 per cent of the tax but, if the circumstances are particularly bad, he may look for 75 per cent. (In some cases, prosecution will be considered).

- (iii) He will consider what penalties and interest are exigible. In many instances, the intended settlement will be less than either of these and, in most, much less than both combined. Consequently, it is not necessary for him in most cases, to compute the penalties and interest precisely. He only does so in exceptional cases where they are less than the normal settlement.

- (iv) He then negotiates the settlement with the taxpayer on the basis of the foregoing.”<sup>4</sup>

13.15 We noted earlier that the statutory penalties for fraud and neglect are tax geared, being calculated on 200 per cent or 100 per cent respectively of the unpaid tax. The actual settlements in the period 1977 to 1982, as shown in Chapter 10 (Table 13), reveal that penalties and interest accounted on average for less than 42 per cent of the tax lost in cases settled up to 1981. Penalties and interest amounted on average to almost 48 per cent of the tax lost in cases settled in 1982. A composite settlement in respect of penalties and interest is normally made and no breakdown between the two is available. However, if interest at a rate sufficient to comprise commercial restitution and no more were to be regarded as included in the settlement for penalties and interest, the actual level of penalties would be much lower. In fact it is doubtful whether the total settlements in some cases cover interest chargeable at commercial rates.

<sup>4</sup>Material supplied at meeting held on 12 December, 1984.

13.16 Besides back-duty settlements, which are dealt with by Investigation Branch, a programme of critical examination is carried out in the local tax districts in selected cases. This programme of critical examinations began during 1984. Where an examination reveals an underpayment of tax, the taxpayer may also be liable for penalties and interest. It is intended that the vast majority of cases will be finalised by settlement with the taxpayer for the agreed tax and a sum in lieu of penalties and interest. Very few settlements have yet been reached.

13.17 There would clearly be significant difficulties in any procedure which required every Revenue investigation, which identified a default, to be referred to the courts, to determine the penalty. Investigation cases would take longer to settle and possibly fewer cases would be taken up. The number of back-duty settlements involving penalties amounts to more than one hundred in any year. The programme of critical examinations will eventually add hundreds more. In order to establish an effective compliance code it is essential to have penalty procedures capable of being applied in a summary way, subject to a right of appeal by the taxpayer.

13.18 Many countries allow their Revenue authorities or bodies other than the courts to impose penalties. In Australia and New Zealand, the Inland Revenue impose penalties by raising assessments for ‘penal tax’. These assessments are subject to the normal rights of appeal. In the United Kingdom, the General and Special Commissioners have a role in imposing penalties. The Keith Committee recommended that the Inland Revenue should assess penalties and interest, subject to certain rights of appeal. Already in Ireland, the interest in back-duty cases chargeable under Section 20 of the Finance Act, 1971 is required to be assessed by the Revenue Commissioners and the assessment may be appealed. We recommend that the Revenue Commissioners be given power to assess and collect statutory penalties in the same way as tax, subject always to a right of appeal.

13.19 The practice of agreeing settlements in default cases works effectively and it has stood the test of time. One of its advantages is that it generally secures payment of the tax and penalties and interest without the need to resort to the enforcement agencies.

13.20 We consider that the practice of negotiating settlements should be retained as a means of dealing with tax offences. Nevertheless, we recognise that the present procedures and the mitigation of penalties, in particular, leave a great deal to the discretion of the Revenue Commissioners. Until recently, virtually all settlements involving a penalty element were negotiated in Investigation Branch. This made it possible to exercise a high degree of control to ensure consistency of treatment in relation to comparable offences. However, under the programme of critical examinations, an increasing number of settlements will, in future, be negotiated in the local

tax districts. This could lead to wide variations in the level of penalties in negotiated settlements. Our proposals for change, set out in Chapter 14, while preserving the basis of negotiated settlements, seek to impose automatic penalties as far as possible and to limit the scope of the power of the Revenue Commissioners to mitigate penalties. This we believe will lead to a fairer system of penalties for tax offences.

### Publication of Names of Tax Defaulters

13.21 The Finance Act, 1984 which requires the Revenue Commissioners to prepare and publish a list of names of tax defaulters will make negotiated settlements more open. Settlements exceeding £10,000 in 1984 and subsequent years will be published in the Annual Reports of the Revenue Commissioners or in *Iris Oifigiúil*. The names of the evaders who, on their own initiative, voluntarily disclose information about past defaults will not be published.

13.22 The obligation to publish names and details of settlements, coupled with anonymity for those who make voluntary disclosures of defaults, might be expected to enhance the attractions of confession and full cooperation. In fact the result of the publication of names may be to make tax evaders less cooperative in negotiating settlements. The Revenue Commissioners advised us that

“we have no evidence that tax evaders ever wished to disclose anything until forced to do so.”

13.23 In view of this it seems that the number of tax evaders likely to avail of the anonymity provision by making a spontaneous disclosure will be very small. Most tax evaders do not disclose their defaults until challenged in an investigation. Some may be fully cooperative from this point onwards. However, the incentive to cooperate is likely to be reduced if the tax evader is aware that his name and details of the settlement will be published at the end of the investigation.

13.24 Whilst publication of names of tax evaders may slow down settlements, it is likely to improve compliance generally. There is a clear conflict here between the public's right to know that tax evasion is being tackled and efficiency in administration. We think our proposal in Chapter 14, to allow the Revenue Commissioners to mitigate penalties in fraud settlements in recognition of the degree of cooperation by the taxpayer, is sufficient incentive to maintain the system of negotiated settlement. We recommend that the names of tax evaders liable to penalties should be published, irrespective of whether the penalties are formally imposed or included as part of a negotiated settlement. The names of defaulters who, on their own

initiative, make a voluntary disclosure of past defaults, should not be published.

### Summary

13.25 A wide range of penalties may be imposed for failure to comply with the Taxes Acts. There are some inconsistencies in the statutory penalties and, in many instances, the Revenue Commissioners may invoke more than one penalty for a particular tax offence. The penalty provisions are used in only a very small number of cases but the threat of penalty proceedings is sometimes made to compel a taxpayer to submit outstanding returns. The Revenue Commissioners do not consider penalty sanctions to be the most appropriate way to enforce compliance with obligations to make PAYE and VAT returns and remit the payments due.

13.26 Penalties cannot be imposed by the Revenue Commissioners; they can be imposed only in proceedings before a court. In practice, however, most penalties relating to unpaid taxes are collected following a settlement<sup>5</sup> by agreement. The mitigation of penalties by the Revenue Commissioners, which results in the payment of less than the statutory penalties, may be arbitrary but it offers the advantage that every case does not have to be processed through the courts.

13.27 It seems to us that the relative rarity of penalty proceedings, due in part to their inherently cumbersome nature, contributes to the apparent failure of the penalty code to operate as an effective sanction. The existing penalty code is also clearly ineffective in securing compliance. There is an urgent need for penalties which are specific and automatic to secure basic information. However, because of the frequency of PAYE and VAT returns which are due every month and every two months respectively, special provisions may be necessary to deal with non-compliance in these areas.

13.28 As regards penalties for incorrect returns, we consider that the categories of offences should be redefined and their statutory penalties revised. Statutory penalties of up to 200 per cent of the evaded tax may have been realistic in an age when tax rates did not exceed 5 per cent (as was the case until 1908). However, in modern conditions, with rates of tax of up to 60 per cent, they produce absurd results. The total tax and penalties on an undeclared sum of £10,000 assuming liability at 60 per cent, amounts to £18,000 and this does not take account of interest charges which may also be due. On the other hand, the actual settlements reached by the Revenue Commissioners in back-duty cases may amount to less than the taxes unpaid in real terms.

<sup>5</sup>Paragraph 13.13.

13.29 We conclude that for the system to work efficiently, it is necessary to have penalty procedures capable of being applied in a summary way, subject to a right of appeal by the taxpayer.

### **Recommendations**

13.30 We recommend that:

1. The Revenue Commissioners should be given power to assess and collect statutory penalties in the same way as tax, subject to a right of appeal by the taxpayer.
2. Details of all penalties and negotiated settlements should be published. The names of defaulters who, on their own initiative, make a voluntary disclosure of past defaults, should not be published.

## **CHAPTER 14**

### **A NEW SCHEME OF OFFENCES AND PENALTIES**

#### **Introduction**

14.1 In Chapter 13 we noted the wide powers of the Revenue Commissioners to mitigate penalties and the need to revise the present unrealistic penalties and the scale of offences involving underpayments of tax. Our objective is to establish a penalty scale and tariff which is simpler and more certain than the present one and which gives equitable results, while protecting the revenue. In this chapter we recommend the abolition of the old scale of offences, a revised penalty tariff with limits on the scope for mitigation of penalties and interest levied at a rate sufficient to ensure commercial restitution and no more. We have used figures to illustrate the possible limits for defaults and the level of certain penalties. These are intended only as guidelines. The correct level of penalties is a matter of judgement for the legislature and once set it would need to be adjusted to take account of the standard of compliance.

14.2 Let us make it clear at the outset that we are dealing with penalties which are in addition to the payment of outstanding tax bills. Understatement or omission in returns should be corrected, the appropriate tax collected and a commercial rate of interest paid on the sum due over the period between liability occurring and payment being made. This chapter deals with penalties in addition to this normal restitution and the circumstances under which such penalties should arise.

14.3 First, we set out some general principles which we feel should apply. Then we deal with offences related to incorrect returns, failure to submit returns and failure to notify chargeability to a particular tax. Finally, we consider appeals against penalties and criminal offences related to taxation.

#### **General Principles**

14.4 Before setting out our proposals we consider some general principles which should apply in relation to the imposition of penalties.

14.5 The main object of the system of taxation is to raise revenue. Accordingly, the effective, efficient and timely collection of that revenue is extremely important. Any delay in the payment of tax should, therefore, give rise to an interest charge on a commercial basis. Default interest should be treated separately from any penalty for non-compliance.

14.6 The Keith Committee,<sup>1</sup> which carried out an extensive review of the enforcement powers of the Revenue Departments in the United Kingdom, established a number of principles which relate the tax offences and penalties. We endorse these principles. They are:

- (i) penalties should be precise and logically formulated, and should so far as practicable be harmonised over the whole direct and indirect tax field,
- (ii) the scope for administrative discretion should be reduced to a minimum, so that it is available only where required for strictly practical reasons. As a general rule, particular consequences should follow particular acts or omissions in every case. In this way, everyone knows where they stand, and compliance is likely to be improved. If everyone is treated alike, grounds for complaint are minimised, provided always that the sanction is regarded as broadly fair,
- (iii) every routine obligation should not, in the tax field, be fenced with criminal sanctions. Automatic civil surcharges and penalties are more appropriate, and more reliable in their application,
- (iv) all penalty procedures should be capable of being applied in a summary and expeditious way, subject to a right of appeal by the taxpayer,
- (v) in general, and wherever possible, penalties should be adjusted in line with the tax due (tax gearing). Where tax gearing is impracticable, a time-gearing penalty, for example, at a monthly rate, might be appropriate. On occasions, a combination of tax-gearing and time-gearing may be necessary to reflect most appropriately the seriousness of the default,
- (vi) frequent changes in fixed penalties would be disruptive. However, there should be some procedure for keeping all penalties under regular review, coupled with some mechanism that would enable comprehensive uprating to be accomplished more readily than at present, and

<sup>1</sup>Report of the Committee on Enforcement Powers of Revenue Departments, Volumes 1 and 2, March 1983.

- (vii) effective criminal sanctions should be available to check the incidence of deliberate and serious frauds.

#### **Incorrect Returns (Defaults)**

14.7 We propose that there should be three categories of default: civil fraud; substantial misdeclaration; and marginal errors and omissions. These categories are close to those which operate now but we feel that clarity requires their formal definition.

14.8 Civil fraud is the most serious category. We use the term 'civil fraud' to distinguish between conduct being dealt with as a default and conduct (fraud) which is prosecuted as a criminal offence before the courts. To establish civil fraud it must be possible to prove, on a balance of probabilities, the presence of a dishonest intention, normally an intention to deceive the inspector of taxes with the object of evading tax.

14.9 The second category consists of cases in which the taxpayer cannot effectively plead error or inadvertence, yet the Revenue Commissioners cannot prove civil fraud. We suggest the term 'substantial misdeclaration' as we consider that the size of the understatement or omission from the tax return ought to be the principal determinant of conduct falling within this default category. The principle is that the size of the discrepancy is such that a reasonable man, paying the proper attention to his tax affairs, could not have failed to notice the error in question. Where the omission or understatement of income in a tax return amounts to 10 per cent or more of the total taxable income, we consider that proof of the fact should by itself constitute absence of due care and be deserving of a penalty. However, an understatement or omission would not be regarded as a substantial misdeclaration, provided the tax return was made in accordance with the practice generally prevailing at the time.

14.10 In the interests of securing fairness in relation to the tax paying public in general, some alternative tests for measuring substantial misdeclaration are desirable. For example, in order to prevent taxpayers with very considerable tax bills gaining an unfair advantage over the majority, there ought to be an alternative minimum measure of substantial misdeclaration for such cases. For illustrative purposes we suggest a figure of £1,000 of income or one half of one per cent of the total taxable amount, whichever is greater.

14.11 The arithmetic test ought, in our view, to apply equally in circumstances where a taxpayer accepts an estimated assessment which has been made in the absence of a tax return and which is less than the true bill. A similar measure of substantial misdeclarations would also be appropriate

for such taxes as advance corporation tax. We discuss later the tests to be applied to VAT and employers' PAYE returns.

14.12 We also consider that fairness demands that some provision be made for dealing with a defaulting taxpayer whose standard of care, while just on the right side of the objective standard of substantial misdeclaration nevertheless leads him to make repeated understatements in this tax returns. This situation could be met also by applying penalties for cumulated understatements over a number of years even if each of these were less than the limit for substantial misdeclaration.

14.13 The least serious of the defaults would be omissions or understatements in tax returns which are smaller than substantial default. They would include relatively small errors arising innocently from simple inadvertence or negligence. What these would have in common in our proposed scheme is that none of them would give rise to a presumption of culpability which deserves to be penalised. Above all, there would be no question of the presence of a deliberate intention to deceive the revenue authorities. Where such an intention is present and can be proved, the objective arithmetical tests are irrelevant. The default could be considered under the civil fraud provisions, regardless of the amount of underdeclaration or omission.

### Penalty Scale

14.14 Civil fraud at present attracts a maximum penalty loading of 200 per cent of the unpaid tax. Given Ireland's very high marginal rates of tax, this can result in almost twice the undeclared income being confiscated in tax and penalties. In addition, a penal rate of interest may also be chargeable. We have recommended that all underpayments should be made up and should be liable to interest charges at a commercial rate for the period of delay. The money penalty should be 50 per cent of the tax evaded. However, we consider that a power to mitigate down to 30 per cent (but no further) in recognition of the degree of the taxpayer's co-operation in the investigation is desirable. The minimum penalty for civil fraud should be 30 per cent of the tax evaded.

14.15 In the case of substantial misdeclarations, the straightforward definition of the offence could be matched by an automatic, non-negotiable penalty. We consider, therefore, that there should be a flat-rate penalty of 25 per cent of the evaded tax. However, a default should not give rise to a penalty if there is a reasonable cause for the default or if the taxpayer on his own initiative provides full information with respect to the understatement.

14.16 Offences in the third default category, marginal errors and omissions would not attract a penalty but interest would be charged on the tax unpaid, by virtue of the understatement.

14.17 The new scale of defaults would also apply to incorrect returns of tax for which a taxpayer is required to account as employer or construction industry contractor or VAT-registered trader. Civil fraud would attract a maximum penalty of 50 per cent of the underpaid tax mitigable down to 30 per cent. We consider that a measure of substantial misdeclaration similar to that set out in paragraphs 14.9 and 14.10 would be appropriate. Although in these instances the amount of the omission or understatement would be measured against the total tax for which the taxpayer was required to account in the year in question.

14.18 For ease of reference we have summarised in Table 19 our proposals in respect of defaults and the tariff of surcharges, both interest and penalties.

**TABLE 19**  
**Suggested Scales of Defaults and Tariff**

Default	Tariff
Civil fraud: the deliberate omission or understatement of amounts in tax returns with the intention to deceive the revenue authorities and the object of evading tax.	Tax due plus interest plus a maximum penalty of 50 per cent of the tax underpaid by reason of the default, mitigable to 30 per cent for cooperation in the investigation. Minimum penalty of 30 per cent of the tax due.
Substantial misdeclaration: the omission or understatement in tax returns of an amount equal to 10 per cent or more of the total taxable amount, or if less, the greater of £1,000 of income or gains or one half of 1 per cent of the total taxable amount. Alternatively, omissions or understatements below these limits which occur over a number of years.	Tax due plus interest plus a penalty of 25 per cent of the tax underpaid by reason of the default. A default should not give rise to a penalty if there is a reasonable cause for the default or the taxpayer on his own initiative provides full information about the understatement.
Marginal cases: any error leading to the omission or understatement from tax returns of any amount not within the above.	Tax due plus interest.

### Failure to Submit Returns

14.19 In Chapter 4 we recommended a new scheme of penalties for failure to submit self-assessed returns of income tax and corporation tax. Here we consider the system of penalties for failure to submit VAT and PAYE/PRSI returns.

14.20 The typical pattern of progress of receipt of VAT and PAYE/PRSI returns is shown in Chapter 15 where we deal with the problems of collecting tax. The standard of compliance is poor and compares unfavourably with that for similar taxes in the United Kingdom. The changes we recommend later in the collection procedures, involving much more action

at local level, should help to improve compliance but an effective penalty code is also needed. The existing penalties are imposed in only a very small number of cases.

14.21 We consider that to pursue penalty proceeding for every failure to submit VAT and PAYE returns on time would be impossible because of the vast number of returns due each year. More than half a million VAT returns forms were issued in 1984. Nevertheless, the compliance problem is sufficiently serious to justify some further action. We propose the implementation of a system of surcharges. The system would involve

- (i) a warning to any trader who failed to submit by the required dates two returns or payments within any period of one year,
- (ii) an initial surcharge of 5 per cent of the tax due or £50, whichever is the greater, for the first default in the year following the issue of the warning,
- (iii) an increased surcharge, rising in steps of 5 per cent, for repeated failures to submit timely returns during the surcharge period,
- (iv) late returns during the surcharge period would also extend the time during which the trader would be liable to surcharge, and
- (v) liability to surcharge would only lapse after a period of one year's satisfactory compliance.

14.22 Failure to remit PAYE/PRSI or VAT due within the times specified is a criminal offence under the provisions of the Finance Act, 1983. We comment on this later but our view is that criminal sanctions should only be invoked as a last resort for very serious offences.

#### **Failure to Notify Chargeability**

14.23 It is essential for the proper functioning of the tax system that all persons with a potential liability to pay or account for tax should take the initiative in getting in touch with the appropriate authorities. The law places an obligation on taxpayers, employers and VAT-registered traders to bring themselves to the notice of the Revenue Commissioners. Penalties are imposed for failure to meet the statutory obligations. At present, the penalties vary in amount, depending on the obligation but in general they are flat rate amounts.

14.24 We see no grounds for distinguishing between notifying personal liability and notifying an obligation to account for tax whether as employer, VAT-registered trader or company payer. It should not be a defence to a charge of failing to notify a particular obligation that the taxpayer is already known to the revenue authorities. This is of particular importance in

circumstances where there is no longer, for some classes of taxpayers, a universal issue of tax returns every year. The obligation to notify should run in respect of each separate source of income and obligation to account for tax.

14.25 We recommend that the penalty for failure to notify the Revenue Commissioners, within the time limits allowed, of an obligation to pay or account for tax should be tax-g geared on the basis of the offence scale set out in paragraph 14.7. The offence of failure to notify chargeability would constitute a substantial misdeclaration if the objective tests were satisfied, or civil fraud, where there was evidence of a dishonest intention to deceive the inspector of taxes. There should be no fixed element but there would be an interest charge in minor cases.

#### **Appeals Against Penalties**

14.26 We have proposed that a power of mitigation from 50 per cent down to not less than 30 per cent should exist in respect of defaults involving civil fraud. We consider that wherever there is a failure to agree a settlement, the inspector of taxes, after due notification to the taxpayer, should be empowered to raise an assessment to recover the tax underdeclared and that he should include in it, separately distinguished, charges in respect of interest and up to a 50 per cent penalty. The taxpayer would then have a right to appeal to the Appeal Commissioners. The burden of establishing liability to interest and a penalty would lie with the inspector of taxes. The Appeal Commissioner would then be in a position to adjudicate at one and the same hearing upon the amount of the underassessment, the nature of the default and the interest and penalty charge appropriate. The Appeal Commissioners would, on our proposals, have the power to mitigate the penalty from 50 per cent down as far as 30 per cent. The Appeal Commissioners would not have the power to mitigate interest charges but they would determine the period of delay.

14.27 As regards the imposition of penalties for substantial misdeclaration of income the inspector of taxes should be empowered, after due notification to the taxpayer, to make assessments to recover the tax underdeclared and include thereon, separately distinguished, charges in respect of default interest and a penalty calculated at 25 per cent of the tax underdeclared. The penalty is intended to be automatic and is non-negotiable. However, the taxpayer would have a right of appeal on the grounds that there is a reasonable excuse for the default. The Appeal Commissioners would have the power to waive the penalty but not to mitigate it. They would also have the power to determine the period of delay in respect of interest charges.

## Mitigation of Penalties

14.28 In addition to our proposal to allow the Revenue Commissioners to mitigate penalties in respect of civil fraud in recognition of the degree of cooperation in the investigation we considered whether the Revenue Commissioners should have a general power to mitigate penalties. Some flexibility should exist but the correct place for this is at the collection stage and it should be confined to exceptional cases.

## Criminal Offences Related to Taxation

14.29 The imposition of monetary penalties does not preclude the possibility of proceedings under common law. It is a matter for the Director of Public Prosecutions to decide upon and to initiate proceedings in relation to common fraud or conspiracy to defraud. However, criminal penalties are specified in the Taxes Acts in relation to certain revenue offences. Until recently the specified offences related mainly to making or assisting in the making of false statements or false representations for the purpose of obtaining any allowance, reduction, rebate or repayment of tax. The maximum penalty was a term of imprisonment not exceeding six months.

14.30 The Finance Act, 1983, imposes, without prejudice to any other penalty to which a person may be liable, more stringent penalties for serious tax offences, including imprisonment for some offences which up to now have attracted monetary sanctions only. This legislation, which relates to all taxes under the care and management of the Revenue Commissioners, applies to serious offences involving

- (i) refusal to comply with statutory provisions designed to allow tax liabilities to be ascertained, for example, notifying the Revenue Commissioners that one has commenced a business or has become chargeable to tax, keeping proper business records and producing them when asked and furnishing returns and other documents when obliged to do so,
- (ii) deliberate furnishing of incorrect information in return and other documents or assisting others to furnish such information,
- (iii) failure to make PAYE and VAT remittances when due, and
- (iv) obstruction of persons exercising statutory powers for tax purposes.

Persons found guilty by the courts under this legislation of committing

such offences<sup>2</sup> will be punishable on summary conviction, by a fine of up to £1,000, or a term of imprisonment not exceeding twelve months, or both fine and imprisonment, and on conviction on indictment, by a fine of up to £10,000, or a term of imprisonment not exceeding five years, or both fine and imprisonment.

14.31 Criminal proceedings for income tax offences under the Taxes Acts were initiated in four cases in the period from 1977 to 1984. Two of these were taken in 1978. One resulted in the taxpayer being sentenced in the District Court to three months imprisonment but on appeal to the District Court the sentence was suspended. The other case was dismissed in the District Court. The third case was initiated during 1981 and the case was heard in March 1982. The taxpayer was convicted and was given a suspended sentence of one month's imprisonment. A further case was dismissed in 1984.

14.32 Criminal proceedings for the new revenue offences under the provisions of the Finance Act, 1983 have not yet been initiated. The Revenue Commissioners advised us that

"In the light of actual and threatened challenges to earlier legislation Counsel's advice has been sought on procedures to be followed prior to a prosecution. Several cases are awaiting processing when the procedures are settled."

14.33 We have expressed a preference for civil sanctions for regulatory matters and for civil proceedings in respect of offences ranging from substantial misdeclaration to civil fraud. This does not, however, mean that we wish to exclude the possibility of the revenue authorities ever instituting criminal proceedings for offences of dishonesty. It is emphatically not the case that the criminal law has no role to play in tax enforcement. Rather the principle should be that the criminal law is invoked as a last resort for 'heinous' cases. These include cases where there is an intention to deceive and

- (i) there is evidence of collusion between the taxpayer and others,
- (ii) evidence that documents have been forged with intent to deceive the Revenue Commissioners,
- (iii) evidence of other irregularities which are denied on challenge,
- (iv) the taxpayer has already enjoyed the benefit of a negotiated civil fraud settlement following a previous investigation,
- (v) the taxpayer while making a show of cooperation, withholds

<sup>2</sup>Section 94, Finance Act, 1983 applies only to offences committed on or after 8 June, 1983, that is, the date of enactment of the 1983 Finance Act.

significant information leading to a materially incomplete disclosure in a current investigation,

- (vi) obstruction of persons exercising statutory powers for tax purposes, and
- (vii) the Board of the Revenue Commissioners takes a view about either the status of the potential offender or about particular exceptional circumstances in relation to the offence itself. For example, the amount of the tax at risk in absolute terms or where the nature of the fraud is particularly blatant.

Criminal penalties may also be necessary where there is persistent failure to comply with obligations to submit returns but the criminal sanction should be reserved for the most serious cases.

14.34 It follows that we have no proposals to do away with the existing criminal offences in the direct tax penalty code. However, some changes in the existing provisions are desirable. Section 516, Income Tax Act, 1967 and Section 94, Finance Act, 1983 should be consolidated into one provision to deal with criminal offences. Each offence should be specifically formulated and set out in the new provision. We consider that an intention to deceive is crucial to any criminal offence of dishonesty in relation to tax matters. The phrase 'with intent to deceive' could be included in the legislation. The present legislation, except in relation to failure to remit PAYE and VAT, makes it an offence to 'knowingly' or 'wilfully' deliver an incorrect return or to fail to meet certain obligations.

14.35 The state of mind of the employer or VAT-registered trader is not an issue in deciding whether failure to remit payments due is a criminal offence. Penalties of up to £10,000 or five years imprisonment or both may be imposed for failure to remit PAYE and VAT due within the specified time limits. We think this is undesirable. In the first instance the monetary sanctions we have proposed should apply. Criminal sanctions should only be invoked as a last resort for very serious offences. We recommend that the provisions of Section 94 of the Finance Act, 1983 should be amended to restrict the circumstances in which a criminal sanction can be invoked for PAYE and VAT offences.

### Criminal Investigations

14.36 The Director of Public Prosecutions advised us that

"early Garda involvement is desirable in criminal cases involving fraud. A special section of the 'Fraud Squad' would help to ensure that the appropriate procedures are followed in criminal cases. Ideally, the Revenue Commissioners should end an investigation which indicates that fraud might be involved and the Fraud Squad should be alerted"

We recommend that the Revenue Commissioners explore with the Garda authorities the possibility of setting up a unit within the Fraud Squad to deal with criminal tax offences.

### Recommendations

14.37 We recommend that:

1. Tax paid late as a result of an understatement or undercharge should attract interest at a commercial rate for the period of the delay.
2. The existing scale of defaults should be abolished and replaced with three new categories:
  - (i) civil fraud,
  - (ii) substantial misdeclarations, and
  - (iii) marginal errors or omissions.
3. The new code of offences might attract penalties of the following order:
  - Civil fraud:** 50 per cent of the evaded tax mitigable down to 30 per cent for co-operation in the investigation. The minimum penalty should not be less than 30 per cent of the evaded tax.
  - Substantial Misdeclaration:** 25 per cent of the tax lost. However, a default should not give rise to a penalty if there is a reasonable cause for the default or the taxpayer on his own initiative provides full information about the understatement.
  - Marginal cases:** there should be no penalty for minor errors or omissions. However, the more serious instances of these offences could be considered under the civil fraud provisions where they had been committed with an intent to deceive.
4. A system of surcharges should be introduced to deal with failure to submit PAYE and VAT returns or pay the tax due. The system would involve
  - (i) a warning to any trader who failed to submit by the required dates two returns or payments within any period of one year,
  - (ii) an initial surcharge of 5 per cent of the tax due or £50, whichever is the greater, for the first default in the year following the issue of the warning,
  - (iii) an increased surcharge, rising in steps of 5 per cent for repeated failures to submit timely returns during the surcharge period.
  - (iv) late returns during the surcharge period would also extend the time during which the trader would be liable to surcharge, and
  - (v) liability to surcharge would only lapse after a period of one year's satisfactory compliance.

5. The penalty in respect of failure to notify chargeability to tax should be related to the amount of the tax unpaid in respect of each separate obligation.
6. The civil penalties should be imposed administratively but would be subject to appeal.
7. There should be a right of appeal to the Appeal Commissioners in respect of penalties and surcharges. The Appeal Commissioners should have powers to
  - (i) mitigate the penalties, within the limits set out in recommendation 3 above, in cases of civil fraud,
  - (ii) waive the penalty for substantial misdeclaration but not to mitigate the penalty, and
  - (iii) determine the underpayment and the period of delay giving rise to interest charges but not to mitigate interest.
8. The Revenue Commissioners should continue to have a general power to mitigate penalties at the collection stage but the use of the power should be restricted to exceptional cases. The Revenue Commissioners should be required to report upon the use made of mitigation to the Comptroller and Auditor General.
9. There should be a set of specific criminal offences of dishonesty in respect of direct taxes and value-added tax. The criminal sanction should only apply where certain things are done or not done with an intent to deceive.
10. The Revenue Commissioners should explore with the Garda authorities the possibility of setting up a unit within the Fraud Squad to deal with criminal tax offences.

## CHAPTER 15

### COLLECTION AND ENFORCEMENT OF PAYMENT

#### Introduction

15.1 In this chapter we examine the collection and enforcement of payment of tax. Non-compliance by taxpayers has resulted in delays in collecting tax to the point where there is a near breakdown in the system. We believe that simplified taxation, self-assessment, more systematic auditing and the application of our scheme of penalties and surcharges would improve compliance and ease the difficulties of collection. We also suggest changes in the present system to make the Revenue Commissioners responsible for all aspects of collection and enforcement of payment and we recommend some alternative methods of enforcing payment. In Chapter 16 we consider a number of special collection arrangements and the preferential claims of the Revenue Commissioners in receiverships and liquidations.

#### Broad Impressions

15.2 In submissions made to us and in discussions we have had with various bodies, the view was expressed that communication between the assessing and collection arms of the Revenue Commissioners needs to be improved and that much more action at local level in collection matters is needed.

15.3 Many of the problems of collection and enforcement arise because taxpayers will not send in returns promptly and in some cases will not send them in at all. Non-compliance by traders in relation to VAT and PAYE/PRSI returns causes particular difficulties because returns are due every two months and every month respectively. The enforcement machinery is being used to force compliance in making returns in addition to its primary function of collecting tax. When taxpayers fail to submit returns the Revenue Commissioners must raise estimates of tax liabilities. These estimates, although they are legally enforceable debts, cause problems for the enforcement agencies. Where enforcement action leads the trader to submit outstanding VAT or PAYE/PRSI returns, the estimates are withdrawn. This action may be seen as successful in terms of forcing compliance

but it undermines the credibility of the enforcement agencies as tax collectors. The confidence of the enforcement agencies in the validity of revenue debts is also eroded.

15.4 The increased volume of enforcement work in recent years has placed enormous burdens on the agencies responsible. Most of the burden falls on the sheriffs and county registrars who have summary powers to enforce payment of tax debts. There has also been some increase in the number of cases processed through the courts, although court proceedings are used only as a last resort or in special circumstances.

15.5 Besides the volume of enforcement work and the particular problems of enforcing collection of estimated sums, there are deficiencies in the enforcement system and in the range of powers available to enforce payment of outstanding tax. The county registrars, who are responsible for revenue debt collection in twenty four counties, have other duties and responsibilities, most of which take precedence over their role as revenue debt collectors. The powers available to county registrars/sheriffs have their origins in the last century when seizure of goods was a relatively simple affair as most wealth lay in property, livestock and physical possessions. Today, wealth can take forms which cannot be touched under sheriff law to enforce payment of tax debts. The deterioration in revenue debt collection and the failure to keep the range of enforcement powers up to date have resulted from the division of responsibility for collection and enforcement between two government departments, namely, the Revenue Commissioners and the Department of Justice. There is no effective accountability for the enforcement of revenue debts.

### THE COLLECTION SYSTEM

15.6 The Office of the Collector General is responsible for collecting income tax, corporation tax and capital gains tax. It is also responsible for collecting income tax deducted by employers under PAYE and associated pay-related social insurance contributions, tax deducted from payments to sub-contractors under the construction industry scheme, value-added tax and interest on late payment of taxes. Health contributions and the youth employment levy are collected on behalf of the Department of Health and the Department of Labour from self-employed persons, including farmers. We recommended in our first report that the collection of health contributions and the youth employment levy should be discontinued and the revenue foregone collected from general taxation. The collection procedures vary for the different taxes. A full description of the procedures is in Appendix 6.

15.7 In our first report we concluded that the arrangements for payment of gifts and inheritances' taxes in instalments should be rationalised. At

present, this tax is collected by Capital Taxes Branch and is accounted for by the Accountant General of Revenue. We recommend that collection of tax on gifts and inheritances should be the responsibility of the Collector General.

15.8 The collection of VAT and PAYE/PRSI places the greatest burdens on the collection machinery. The total number of VAT-registered traders is 107,000 and approximately 100,000 employers are registered for PAYE. Collection procedures are geared to gather in the bulk of the estimated Exchequer receipts as soon as possible after the due dates. In this process there is understandable emphasis on those cases from which the bulk of total payments will be collected. It is worth noting that one thousand companies account for 70 per cent of the revenue from VAT and some seven hundred employers account for more than 80 per cent of the PAYE yield and 75 per cent of the PRSI contributions.

15.9 It was put to us that the Revenue Commissioners were over-concerned with money management, that they were excessively vigilant in the case of large companies with large tax liabilities. While we reject this criticism, we understand that to the compliant taxpayer the amounts due in respect of VAT and PAYE/PRSI by even a small business appear large enough to warrant immediate and vigorous collection and enforcement action. We examine later how the collection and enforcement of tax debts could be improved, given the existing constraints on the resources of the Revenue Commissioners. Before doing so it is worthwhile considering the extent to which taxpayers fail to comply with their obligations.

### Compliance

15.10 Collection of tax depends on information about the liabilities of taxpayers under different tax heads. This information must be supplied to the Revenue Commissioners by the taxpayer. The necessary information is usually required in the form of a tax return for the relevant tax. When taxpayers fail to submit returns the Revenue Commissioners raise assessments or estimates to establish enforceable debts.

15.11 The Revenue Commissioners advised us that the compliance rate in VAT is generally lower than that in PAYE/PRSI. There seems to be a greater resistance to the timely submission of VAT returns and payments. This may be because VAT payments tend to be bigger for many businesses. Table 20 shows the level of compliance in making returns and payments of VAT for the taxable period March/April 1983. A more detailed breakdown of this pattern and a comparison with other years is in Annex 1 to Appendix 6. The pattern of compliance does not vary greatly from year to year.

**TABLE 20**

**Level of Compliance in Making Returns and Payments of VAT**

	Taxable Period March/April 1983	
	Returns	Tax
Received by End of Due Month	%	%
Received by End of Following Month	24	57
Received by End of 31/12/83	41	77
	64	96

Source: The Revenue Commissioners.

Note: The percentage for returns is expressed by reference to the number of returns issued. The percentage for tax is expressed by reference to the total tax received for the month at twelve months after the due date.

15.12 Table 21 shows the monthly return pattern for PAYE

**TABLE 21**

**Level of Compliance in Making Returns and Payments of PAYE**

	Month ended 5 May, 1983		Month ended 5 June, 1983	
	Returns	Tax	Returns	Tax
Received by End of Due Month	%	%	%	%
Received by End of Following Month	33.5	80.6	35.0	83.8
Received by 31/12/83	48.1	92.8	47.3	93.0
	69.8	98.8	68.5	98.8

Source: The Revenue Commissioners.

Note: The percentage for returns is expressed by reference to the number of returns issued. The percentage for tax is expressed by reference to the total tax received for the month at twelve months after the due date.

15.13 VAT returns are generally submitted later than PAYE returns. In addition, the proportion of total tax paid is significantly lower for VAT in the initial period after the due date for payment. About six months after the due month, the proportion of tax paid is still lower for VAT but not significantly so. There is a number of factors which may influence this different pattern between PAYE and VAT. PAYE is paid monthly and there is a shorter period for making the payment. PAYE is also concentrated among large employers and includes public sector agencies and financial institutions which are not normally liable for VAT.

15.14 The compliance rates of VAT and PAYE returns are much lower in Ireland than in the United Kingdom where 60 per cent of traders make

their VAT returns within a month of the due date and 95 per cent of employers pay their PAYE income tax liabilities within a fortnight of the due date. However, when comparing the compliance rates of VAT in Ireland and the United Kingdom, it must be borne in mind that VAT returns in the United Kingdom are three-monthly with payment by the end of the following month as against Ireland's two-monthly return with payment after nineteen days. The period of time allowed for payment of PAYE is the same in both countries.

15.15 When a trader or employer fails to submit a return declaring his tax liability, an estimate is issued by the Collector General to establish an enforceable debt. The trader or employer has a right of appeal against such an estimate but, in practice, formal appeals are seldom made and the estimate is withdrawn if a return is submitted. Payment of an estimated amount of tax does not relieve a person of the obligation to furnish a return and failure to do so leaves a person liable to a penalty. Penalties are not considered by the Revenue Commissioners to be the most appropriate form of action to deal with non-compliance in this area because of the frequency of returns and the cumbersome nature of the procedures. The taxpayer is generally pursued for a return by estimating the tax liability and by taking action to collect the debt established by the estimate. Since the objective of raising an estimate is to prompt the trader or employer to forward the return and the remittance, there is an inclination to overestimate the liability. However, estimates which are wildly off the mark create problems for the enforcement agencies. Estimates frequently have to be withdrawn from enforcement and the credibility of the system is undermined.

15.16 We accept that it is difficult for the Revenue Commissioners to make good estimates of tax due for collection when the information is in the hands of the trader or employer. This is certainly the case in relation to VAT. Value-added tax liabilities can fluctuate greatly not only from one period to the next but for the same period in different years. Nevertheless, we consider that the approach should be to estimate the true liability rather than to use the system of estimates to force the trader to submit returns. Where there is a history of repeated payments on estimates it is likely that they are significantly less than the true liability. Graduated increases in estimates would encourage traders to submit returns and thus provide a more accurate base for any subsequent estimates that may be necessary. The more long-running cases of payment on estimates should be audited to establish the correct liability and penalties for any underpayments should be imposed in accordance with our recommendations in Chapter 14. Apart from these measures, it seems to us that the principal need is to reduce the time it takes for the Collector General to respond effectively to failure by a taxpayer to submit his return and remittance. We believe that there is

little prospect of improving the present collection system until there is more local involvement in collection matters.

### The Office of the Collector General

15.17 The collection of taxes is centralised in the Collector General's Office in Dublin. Because of the enormous volume of work, collection is conducted on the basis of process rather than case work. This means that any one taxpayer's case can be handled by many different people at the various stages in the collection process. The margin of error is, therefore, wide. The Revenue Commissioners advised us that collection is

"undertaken by staff at a low level of grading relative to the complexity of the work done. The cost in terms of resources of securing for the taxpayer significantly less exposure to error would be prohibitive. Under any system, however costly, errors could not be completely eliminated and accordingly some level of error would have to be tolerated as inevitable."<sup>1</sup>

15.18 Given the strength of the statutory power to enforce payment, i.e. seizure of goods, we are concerned about the existing situation. A high level of errors makes it almost impossible to use the ultimate sanction and the collection and enforcement machinery is undermined.

15.19 It is widely felt that centralisation of collection and a lack of effective communication between the collecting and assessing branches of the Revenue Commissioners has led to inefficiencies in the collection system. The separation of the assessment and collection branches is not just physical; the functions and responsibilities are entirely separate. The Revenue Commissioners strongly reject this criticism. They assured us that

"any breakdown is not between assessment and collection but between the inspector of taxes and the taxpayer. Inspectors have ready access to the computer file in the Collector General's Office."<sup>2</sup>

Nevertheless, evidence from outside the Revenue Commissioners indicates that communication between the two sections needs to be improved substantially. We are aware that some improvement has taken place since inspectors now have access to collection information on the computer file.

15.20 The Collector General does not always have the benefit of the information available to the inspector nor the more general local knowledge about the most appropriate cases to pursue for collection or the most

<sup>1</sup>Agreed note of meeting, 12 December, 1984.

<sup>2</sup>Agreed note of meeting, 12 December, 1984.

suitable time at which to pursue them. Elaborate procedures are necessary to ensure that all relevant information is in the hands of the enforcement agent before he takes enforcement action.

15.21 We conclude that non-compliance in making returns and payments is putting a severe strain on the collection and enforcement procedures to a point where there is near breakdown of the system. Many of the changes we have recommended in our first three reports involving simplified taxation together with the scheme of penalties and surcharges recommended in this report would improve the rate of compliance. Nonetheless, we believe that decentralisation of certain collection functions is necessary to establish an efficient and effective collection system capable of responding quickly to counter non-compliance. While some of the initial collection procedures, such as issuing demands, should continue to be organised by a central collection unit, it is clear to us that there is considerable scope for follow-up action at a local level.

15.22 We believe that local action would be much more effective in securing payment and in selecting cases for further enforcement action where taxes remain unpaid. Collection and enforcement systems based largely on postal demands are ineffective. A telephone call or a personal call from a local office is more effective in securing payment than an anonymous computer demand. Traders respond to those creditors who exert most pressure. In many cases, reluctance rather than inability to pay is at the root of non-compliance and a personal approach by a collector before enforcement proceedings are taken would be more successful, provided it is backed up with adequate enforcement powers. In addition, a local collection system would be in a position to communicate directly with the inspectors responsible for assessment of tax and would be more aware of the circumstances of the defaulting taxpayer. We, therefore, recommend that certain collection functions be decentralised. There is a number of ways in which decentralisation could be organised. The precise details of the organisation at local level are a matter for the Revenue Commissioners.

### ENFORCEMENT OF PAYMENT

15.23 If any tax remains unpaid, enforcement proceedings are undertaken. Under the present system the Collector General may

- (i) issue a certificate directly to the appropriate county registrar or sheriff certifying the amount of tax due, or
- (ii) notify the Revenue Solicitor to initiate court proceedings for the recovery of outstanding taxes.

15.24 The county registrar/sheriff has a power of summary distraint. On receipt of a certificate from the Collector General he applies to the defaulter for payment, under threat of seizure of goods. If payment is not forth-

coming he is legally entitled to seize and eventually sell enough of the defaulter's goods (if these are so available) to realise the amount due on the certificate plus his costs.

15.25 Where action by the county registrar/sheriff is unsuccessful or seizure of goods is inappropriate, (for example, goods which can only be sold under licence), recovery action is conducted through the courts. This is the only area where the Revenue Commissioners have responsibility for enforcing payment of taxes. The Commissioners have available to them the services of the Revenue Solicitor. There are also two external solicitors — one in Dublin and one in Cork — who are contracted on a fee and commission basis. At present, all court cases where the debt exceeds £15,000 are referred to the Revenue Solicitor for High Court action. The external solicitors deal with cases appropriate to the Circuit Court and the District Court. In the second half of 1985, a limited number of High Court cases where the debt exceeds £15,000 but does not exceed £100,000 will be referred to these two external solicitors.

15.26 Enforcement by county registrars/sheriffs is preferred to court proceedings by the Revenue Commissioners for administrative reasons. Enforcement through the courts is not very satisfactory. Income tax and corporation tax cases require an intense level of preparation before actual referral to solicitors. The court process is lengthy, taking up to nine months to get a judgement. In addition, the frequency of due dates, every month for PAYE and every second month for VAT, means that a large liability accrues while judgement is being sought. The High Court and Circuit Court recess for up to four months in the aggregate each year and this in turn limits the availability of the procedure. Also, the costs of collection through court proceedings are considerably higher than through summary distraint. A full description of the procedures for court proceedings and a comparison of the costs of solicitor enforcement and enforcement by the county registrar/sheriff are in Appendix 7.

15.27 In the vast majority of cases, ordinary enforcement procedures should be sufficient to collect taxes from even the most recalcitrant of taxpayers. However, solicitor enforcement is a necessary part of recovering unpaid taxes, especially as an action of last resort. There are obvious constraints on the number of cases which can be referred to the courts. Nonetheless, we consider that there is some scope for extending the system. This could be done by using the state solicitors in provincial areas or extending the use of solicitors in private practice and by increasing the limits<sup>3</sup> for Revenue debts in the lower courts. We so recommend.

<sup>3</sup>There are no monetary limits in respect of summary proceedings by summons for the recovery of arrears of rates and it has been the practice of the district courts to entertain proceedings irrespective of the amount.

## County Registrar/Sheriff Enforcement

15.28 There are twenty eight sheriffs in Ireland. Outside Dublin and Cork their role is played by the county registrar who is the chief court officer for the county circuit court. There are four independent sheriffs who handle enforcement action in Dublin and Cork. County registrars are employed by the Department of Justice on a salary basis. The sheriffs are engaged by the government on a fee and commission basis. The primary duty of county registrars and sheriffs is to enforce court orders, although the county registrars exercise a number of other official functions. Under the Income Tax Act, 1967 arrears of tax are collectable by the same process as court orders. A large number of certificates for unpaid tax is issued each year to county registrars and sheriffs for enforcement. In 1984, 58,756 tax certificates were issued for collection with a face value of over £530 million. The revenue collected by county registrars and sheriffs in 1984 amounted to £32.1 million. Full details of the operations of county registrars and sheriffs are in Appendix 8.

15.29 There is evidence that the enforcement agents, especially the county registrars, are unable to cope with the volume of tax collection work. The Report of the Comptroller and Auditor General for 1981 drew attention to the system of enforcement by sheriffs and county registrars in the following terms:

“A review carried out by my officers of the statistics relating to cases referred to the Sheriffs/County Registrars under all tax headings indicated that the level of collection was not keeping pace with the number of cases referred with the result that the number of uncleared cases was progressively increasing”.<sup>4</sup>

15.30 By 1983 there had been a further deterioration, as Table 22 shows.

TABLE 22  
Cases on Hands of County Registrars/Sheriffs, 1981 and 1983

	Number of Cases		Face Value of Certificates	
	1981	1983	1981	1983
			£m	£m
Income Tax	22,080	36,835	25.7	82.6
Corporation Tax	5,446	8,406	14.4	37.0
PAYE PRSI	9,013	34,894	14.9	98.3
VAT	16,150	34,420	30.3	81.2
Total	52,689	114,555	85.3	299.1

Source: Appropriation Accounts, 1981 and 1983.

<sup>4</sup>Appropriation Accounts, 1981.

Of the 114,555 cases on hands at the beginning of 1983 and referred to the sheriffs/registrars during the year, only 5 per cent were returned paid, 26 per cent returned unpaid or withdrawn and 69 per cent carried over to the following year.

15.31 We discussed with county registrars and sheriffs the problems of enforcing this vast number of certificates. While their experiences are different, both highlighted the difficulties of enforcing estimated certificates from the Collector General. They told us that only a small proportion of the thousands of certificates issued each year is for the collection of tax determined on the basis of final liability. The rest are issued in error or are estimates which in many cases are clearly excessive and designed to obtain a return from the taxpayer.

15.32 While it may be necessary to use the county registrars/sheriffs to force compliance, this can only be successful if used on a limited scale. The present widespread use of the enforcement agencies to deal with non-compliance is contributing to the breakdown in tax enforcement. It also seriously lessens the effectiveness of these agencies in recovering established tax liabilities. The difficulties of attempting to use the enforcement machinery to solve the problem of non-compliance in the submission of returns (as opposed to non-payment of tax) would be more clearly recognised by the Revenue Commissioners if they had overall responsibility for collection and enforcement.

15.33 Deficiencies in sheriff law, which has not been updated since the last century, also contribute to the problems of tax enforcement. In a submission to the Department of the Public Service, a copy of which we received, the President of the Association of County Registrars stated that in 1967, when the county registrars were given responsibility for enforcing tax collection, they were aware that sheriff law was seriously out of date and that it was becoming increasingly difficult to enforce court orders. The addition of collecting tax arrears in 1967 not only overburdened the enforcement agents but demonstrated even more clearly that without a thorough overhaul, sheriff law is an unsuitable and inefficient vehicle for dealing with the collection of tax arrears. We consider the issue of adequate enforcement powers later in this chapter.

15.34 Despite the inadequacies of sheriff law, the sheriff appears to be a more effective enforcement agent than the county registrar because

- (i) he has no staffing constraints. He can determine his staff requirements and select the most qualified personnel,

- (ii) being employed on a commission basis, he has a financial incentive to finalise cases, and
- (iii) disposal of seized goods is easier in the more anonymous urban environment.

15.35 We sought the observations of the Revenue Commissioners on the effectiveness of the enforcement system. They said that

"The County Registrar system is not working well. Manpower is scarce and there is the problem of providing adequate resources to enable the system to operate efficiently. The City and County Sheriffs are more effective. The Sheriffs want to enforce collection. The performance of County Registrars is variable between different areas."<sup>5</sup>

15.36 The Department of Justice told us that

"Most of the actual enforcement work is done by court messengers. There are forty court messengers at the moment and three vacancies. Most counties have only one messenger but twelve counties have two each and two counties have three each. In view of these difficulties and the priority of other functions of the county registrars we would like to see the burden of enforcing revenue debts removed from county registrars."<sup>6</sup>

15.37 In November, 1984, the Minister for Finance in reply to a parliamentary question said that

"neither my Department nor the Revenue Commissioners have any statutory function in relation to the performance of the duties imposed on Sheriffs and County Registrars in connection with the enforcement of revenue and civil debt collection. Any matters arising in relation to such duties are primarily the concern of the Minister for Justice."<sup>7</sup>

It is clear that responsibility for enforcement of tax debts is divided. It seems to us that this division is the fundamental defect in the present structure. It has hindered the effective collection of unpaid taxes and, as a result, the credibility and efficiency of tax enforcement is threatened.

## Conclusion

15.38 We conclude that the enforcement of collection is in a very sorry state. The system is incapable of processing the large number of cases each

<sup>5</sup>Agreed note of meeting, 12 December, 1984.

<sup>6</sup>Agreed note of meeting, 19 June, 1985.

<sup>7</sup>Dáil Debates, 15 November, 1984, Col. 2326.

year and the situation is deteriorating. The reasons for this are many. Non-compliance by taxpayers is having serious effects down the line to collection and enforcement so that too many cases for enforcement are based on estimates and are not actual amounts due. The Revenue Commissioners have attempted to deal with the problems of non-compliance in the submission of returns by using the enforcement agencies. The division of responsibility for collection between the Revenue Commissioners and the Department of Justice, with the resulting lack of accountability, has led to the enforcement system becoming more inefficient and ineffective.

15.39 Our proposals for change in the collection system, with more effective action at local level, should improve the general levels of compliance and the selection of cases for enforcement. However, effective enforcement of outstanding taxes is essential to sustain high levels of compliance in any tax system. The present system of enforcement is not working. The county registrars, because of the demands on their time and resources to carry out their functions as officers of the courts, are a completely unsuitable and inefficient vehicle for dealing with the collection of revenue debts. We consider that there is a need for a radical change in the enforcement structure. We recommend that overall responsibility for enforcement of tax arrears should be given to the Revenue Commissioners and that the county registrars should be relieved of the responsibility for collection of revenue debts other than those resulting from court judgements.

#### PROPOSED ENFORCEMENT STRUCTURES

15.40 We now consider the issues involved in handing over the responsibility for enforcement to the Revenue Commissioners. It is essential that the Revenue Commissioners have powers to enforce the payment of outstanding taxes. However, although the overall responsibility for enforcement of payment should rest with the Revenue Commissioners, this need not prevent them from engaging the services of the sheriffs in Dublin and Cork in connection with enforcement. We examine the type of structure needed to enable the Revenue Commissioners to establish a collection/enforcement system of their own. We also consider the necessary powers to establish an effective enforcement procedure.

15.41 In many other countries the Revenue authorities have responsibility for enforcing collection, for example, the United States and the United Kingdom. In England, Wales and Northern Ireland collectors are appointed to collect unpaid taxes. After the issue of a final notice to pay, the collector either visits or telephones the defaulter. In only 12 per cent of cases, payment is not forthcoming after the call.<sup>8</sup> Collectors are usually

<sup>8</sup>Committee on Enforcement Powers of the Revenue Departments, Volume 2, March, 1983.

accompanied by a bailiff who provides assistance and expertise in the valuation of distrainable goods. If no payment is made, the collector takes 'walking possession'<sup>9</sup> of the goods. A period of a few days is allowed to elapse before goods are put up for sale or auction. Payment often takes place in this period and in only a tiny fraction of cases is sale at auction necessary. The system is regarded by the UK Revenue authorities as simple and cost-effective.<sup>10</sup> The taxpayer is liable for payment of costs for appraisal, removal, storage and sale of goods. The prospect of having to pay costs in addition to the tax due is in itself often seen as an inducement to settle before distraint and statistics show that the debtor can and almost always does stop the process of distraint at any stage up to the actual sale.<sup>11</sup>

15.42 The enforcement system we envisage is connected closely to the locally based collection system we recommended in paragraph 15.21. Local collectors should be at the centre of any enforcement structure and responsible for collection and enforcement in a defined area. Local collectors would also have the advantage of having close liaison with the inspector of taxes, thus improving communication.

15.43 Such a structure is not new to the Revenue Commissioners. Prior to the appointment of a Collector General, collectors of taxes were appointed on an annual, contractual basis. The contract covered payment of a specific sum which included provision for remunerating his staff if he found it necessary to employ them. These collectors were located throughout the country. This local collection system had its faults, some of which were identified by the Commission on Income Taxation. The collectors were not established civil servants and were a low level staff grade. Their offices were separate from the inspectors' offices so they did not have the benefit of up to date information on taxpayers. Finally, there were doubts about declarations of secrecy once a person ceased to be employed by a collector<sup>12</sup>. Nevertheless, they were successful in collecting revenue.

15.44 In the early seventies when problems with collection arose to such an extent as to cause concern,<sup>13</sup> the Revenue Commissioners appointed assistants to the Collector General in some districts to call on defaulters and deliver a final demand for tax outstanding. The appointments again were at a low level of grading relative to tax office staff generally and the people involved had no powers. This scheme was not particularly successful

<sup>9</sup>'Walking possession' means that the defaulter is given an inventory of the distrained goods and signs an acknowledgement, in effect a contract, that the goods remain under distraint and that in consideration of the collector refraining from taking actual possession, the defaulter undertakes not to remove them or permit their removal from the premises.

<sup>10</sup>Committee on Enforcement Powers of the Revenue Departments, Volume 2, March, 1983.

<sup>11</sup>Committee on Enforcement Powers of the Revenue Departments, Volume 2, March, 1983.

<sup>12</sup>Commission on Income Taxation, Sixth Report, March, 1961.

<sup>13</sup>Committee of Public Accounts Report, 1973/74.

as the agents, as they were known, were diverted to more general duties as messengers and paperkeepers.

15.45 We believe that it is possible to avoid the faults and preserve the benefits of a local collection system. We favour a system with a number of local collectors who have powers of summary distraint. We believe that it is vital for the success of any collection system that the right staff are recruited for the job. They should have a degree of discretion in pursuing tax defaulters enabling them to defer tax payments or to agree instalment arrangements where this is appropriate to secure the collection of the revenue. Their most powerful asset, however, will be their breadth of local knowledge. We recommend that the collectors should be full time, established civil servants and should be of a grade comparable to credit managers in private business so that they can deal adequately with the complexities of collection and enforcement.

15.46 We asked the Revenue Commissioners for their views on setting up an enforcement arm. They replied

“we recognise frailties in the civil enforcement system which affect the collection of revenue. It may be necessary to introduce a separate system to collect revenue. We would be unable to do this given the current staffing constraints”.<sup>14</sup>

15.47 We acknowledge that a structure of local collectors with responsibility for enforcement would have financial implications for the Exchequer. Debt collection is a time-consuming and labour intensive activity. However, we believe that the additional costs would be more than offset by increased returns to the Exchequer. The alternative is to move to a system of taxation by voluntary donations and arbitrary penalties.

15.48 It is clear that the structure of tax enforcement could be organised in different ways. We favour a locally based system. However, the precise details are a matter for the Revenue Commissioners. We content ourselves with endorsing the principle that the Revenue Commissioners should be accountable for all aspects of the collection and enforcement of outstanding taxes. This entails having powers to enforce payment.

### **Powers to Enforce Collection**

15.49 The principal power of any enforcement agent is the power to distraint goods. The alternative is to recover debts through the normal process of the courts. In paragraph 15.25 above we examined the court process and concluded that it was unsatisfactory as the main method of

<sup>14</sup>Agreed note of meeting, 12 December, 1984.

enforcement. It is too lengthy, costly and cumbersome, given the present scale of failure to pay taxes promptly and the willingness to delay to the bitter end. There are constraints also on the use of the power of seizure. The law relates to certain goods only and these may not always be available for seizure. Traditionally, seizures are emotive, particularly in rural areas, where they are met with some resistance. Nevertheless, we consider that seizure of goods is essential for enforcement. However, seizure should be a weapon of last resort, the final act in a process of collection which has at its disposal a variety of other means to obtain payment. We now examine the power of seizure and consider a number of other ways to enforce collection.

### **The Power of Seizure**

15.50 Section 480 of the Income Tax Act, 1967 provides the power to distraint goods. This section, however, has fallen into disuse since the county registrars and sheriffs are the enforcement agents and they operate their seizure powers under sheriff law. The Revenue Commissioners have some doubts that Section 480 of the Income Tax Act, 1967 would confer a power of distraint on the Collector General or any Revenue Officer. We recommend that the doubts concerning Section 480 of the Income Tax Act 1967 be resolved without delay, either by further legislation or otherwise, so as to ensure that the Collector General has power to distraint and that other officers may distraint at his discretion on his behalf.

15.51 Questions may be raised about whether the power of summary distraint by the Collector General is repugnant to the Constitution. It is the responsibility of the courts to determine this, if it is challenged. However, if there is to be effective enforcement a constitutionally acceptable method of enforcement must be provided.

15.52 We now consider whether the power of distraint, as it exists under Section 480 of the Income Tax Act, should be extended from goods and chattels to include all property both real and personal.

15.53 Seizure of goods was a relatively simple affair when most wealth lay in property, livestock and physical possessions. It has little place in the late twentieth century when many people live and trade on credit and when wealth takes the form of income and financial assets. These things cannot be touched under sheriff law to enforce payment.

15.54 Goods, to be available for seizure under sheriff law, must be the sole unencumbered property of the debtor and must be saleable. Nowadays, a great proportion of the more valuable items of household equipment are held on hire-purchase or credit sale. Many other articles are leased. Stock in trade in very many businesses is held subject to a ‘retention of title’

clause, that is, ownership remains with the supplier until the moment of sale to a retail customer. None of these goods is available for seizure because they are not, in law, the property of the apparent possessor.

15.55 Seizure of cattle is also difficult. There are disease regulations which restrict the movement of cattle. Livestock has to be kept in suitable pounds pending sale, and local authorities are reluctant to provide these facilities.

15.56 'Walking possession', such as exists in the United Kingdom, would solve some of the problems of storage and movement of physical goods. We recommend that goods be subject to seizure in such a manner.

15.57 If the power of seizure is to be effective it may be necessary to extend it to real property. In the United States and in Denmark the Revenue authorities have power to seize real property, subject to the authorisation of the courts. We recommend that the possibility of extending the power of distraint to real property, subject to court authorisation, should be examined.

#### **Other Powers and Procedures**

15.58 Court proceedings and seizures are essential measures to secure the revenue in cases of default but it is impossible to have an efficient administration which depends solely on these measures. Other summary powers are necessary to enforce collection of tax arrears. Collection of tax from PAYE taxpayers is a straightforward and efficient procedure. The taxpayer does not receive a bill which has to be pursued to collection and enforcement, his tax liability is deducted throughout the year from his main source of income. The PAYE taxpayer does not have the opportunity to pay at his discretion. A similar or comparable procedure is necessary to achieve efficient collection of other tax debts. Tax provisions which can only be enforced in some areas are unfair and result in distortions.

15.59 There is a number of other enforcement procedures already available as a means of executing judgement against a debtor. Proceedings allow sums owed to the debtor by third parties to be diverted to the creditor to satisfy the debt owed to him. For example, charging orders charge the amount of the judgement upon stocks or shares belonging to the judgement debtor. In these procedures and in others that are available, some kind of court proceedings are necessary. These are all valuable additions to the power of distraint but they do not provide a basis for an efficient and effective collection system.

15.60 In the United States, the main enforcement procedure involves the

use of a levy on taxpayers' income or bank accounts. Under the levy procedure the Internal Revenue Service may take all but a very small amount of a taxpayer's net income to meet his tax liability.<sup>15</sup> Alternatively, they may require a bank to hand over the full balance on an account. The tracing of bank accounts is facilitated by a requirement that taxpayers list all bank accounts on their income tax return. Generally, court authorisation is not required but three legal requirements must be satisfied before levy action can be taken:

- (i) the tax must be owed.
- (ii) a notice and demand for payment must be sent to the taxpayers last known address, and
- (iii) if payment is not made, a notice of intent to levy must be given at least ten days in advance.

If collection is in jeopardy, the ten day waiting period and the notice of intent to levy are not required. While the use of this levy is controversial, it has not been successfully challenged in the courts.

15.61 We believe that this type of levy is the only effective answer to the problems of collecting outstanding taxes. We do not accept that this is a measure which is inappropriate for Ireland. We consider that it does no more than place the collection of other taxes on the same footing as the collection of PAYE from employees. We recommend that the Revenue Commissioners be given the power to levy the income or financial assets of a taxpayer to satisfy a tax liability.

15.62 There is also a number of other enforcement procedures which might be useful additions to the general armoury for enforcing collection of unpaid taxes.

15.63 In 1972 the Committee on Court Practice and Procedure recommended that stop orders on banks and other financial institutions be used to enforce debt collection.<sup>16</sup> Stop orders on financial institutions would allow a judgement creditor to prevent a judgement debtor who has funds to his credit in an account with a financial institution from disposing of those funds before the judgement creditor can realise his debt. This recommendation falls short of the levy procedure used in the United States but nevertheless would be a useful addition to the powers of an enforcement agent.

15.64 In Scotland there is a power known as assessment and inhibition

<sup>15</sup>There is a minimum exemption from levy for wages, salary and other income of \$75 per week, plus an additional \$25 for each legal dependant.

<sup>16</sup>Eighteenth Interim Report of The Committee on Court Practice and Procedure, GPSO 1972.

on the dependence of a civil action. This allows a creditor to freeze any movables, debts and money belonging or owing to the debtor while the creditor is commencing legal action to recover the debts. This measure ensures that any assets belonging to the debtor remain in the jurisdiction. Such assessments do not have to be justified by demonstrating grounds for apprehension that assets will vanish from the jurisdiction and frivolous attempts to freeze assets are severely penalised. In practice, freezing assets by this measure induces speedy payment of undisputed sums in the great bulk of cases as a condition of unfreezing, without the need for a decree.

15.65 If legal proceedings have to be taken against a defaulter, the Revenue Commissioners must first seek a judgement from the courts that a debt is owed. The judgement is formally issued, then registered and finally given to the county registrar or sheriff for execution. The county registrar or sheriff then must attempt to seize the goods of a defaulter. If there is nothing to be seized which would satisfy the debt, the registrar or sheriff has to return a *nulla bona*<sup>17</sup> certificate. The Revenue Commissioners may then register a judgement mortgage or return to court to petition for liquidation or bankruptcy. The requirement to seek a *nulla bona* certificate may be a waste of time if it is apparent from the start that there are no goods to be seized. The Committee on Court Practice and Procedure examined this issue and concluded that the creditor should not be required to concern himself with the question of whether the judgement debtor has goods which can be seized. The creditor should be entitled to dispense with the process of obtaining a *nulla bona* certificate in the first place and to proceed immediately to enforce his judgement by other means at his disposal.<sup>18</sup> We endorse this recommendation.

15.66 Finally, the Revenue Commissioners can exert pressure to ensure that outstanding taxes are paid by the use of tax clearance procedures in relation to certain transactions. For example, in June, 1984 a tax clearance certificate scheme for public sector contracts was introduced. Under this scheme firms applying for government contracts must obtain a certificate from the Revenue Commissioners stating that all outstanding tax liabilities have been paid. We have been told by the Department of Finance that this initiative is working effectively and large sums of tax arrears have been paid over to the Revenue Commissioners.

15.67 In Chapter 5 we described a procedure under capital gains tax which allows the proceeds of a sale to be handed over to the vendor's solicitor without any provisional deduction for the capital gains tax liability if the vendor is resident in the state. The procedure involves the issue of a clearance certificate by the Revenue Commissioners which may not normally be

<sup>17</sup>Literally, having no goods. The debtor has no goods that can be legally seized to settle a debt.

<sup>18</sup>Eighteenth Interim Report of the Committee on Court Practice and Procedure, GPSO 1972.

refused if the vendor is an Irish resident. We consider that such certificates should be refused if there are outstanding taxes or should only be given where the solicitor gives an undertaking to discharge all established tax debts out of the sale proceeds. However, where there are no taxes outstanding it is the duty of the Revenue Commissioners to see that clearance certificates are issued promptly.

### Conclusion

15.68 Radical changes are necessary in the collection and enforcement of outstanding taxes to improve the standard of compliance. Effective enforcement would secure and maintain high levels of compliance. The lack of effective enforcement at present undermines the willingness of even the most compliant taxpayers to meet their obligations and to pay their taxes on time. The failure to collect outstanding taxes encourages non-compliance. Traders and businesses are put at a competitive disadvantage if they pay their taxes while others ignore the demands of the Collector General. The changes we recommend in the collection and enforcement system would improve the fairness and efficiency of the administration.

### Recommendations

15.69 We make the following recommendations:

1. The Revenue Commissioners should be responsible for all aspects of collection and enforcement of tax. They should set up a formal and integrated system to carry out the enforcement of revenue debts. This would involve
  - (i) the decentralisation of certain collection functions,
  - (ii) greater use of legal action in local areas to enforce payment through the courts, and
  - (iii) the appointment of local collectors on a full time established basis with powers to seize goods.
2. County registrars should be relieved of the responsibility for collection of revenue debts other than those resulting from court judgements.
3. The Revenue Commissioners should be empowered to levy the income and/or financial assets of a taxpayer to satisfy a tax liability.
4. The doubts concerning Section 480 of the Income Tax Act, 1967 should be resolved without delay, either by further legislation or otherwise, so as to ensure that the Collector General has power to distrain and that other officers may distrain at his discretion on his behalf.

5. The power of seizure should be extended to enable the Revenue Commissioners and sheriffs to take 'walking possession' of goods.
6. The possibility of extending the power of distraint to real property, subject to court authorisation, should be examined.
7. The requirement that a *nulla bona* certificate must be returned by the sheriff before a judgement mortgage can be registered against a defaulter or before legal proceedings to petition for liquidation or bankruptcy can be initiated should be abolished as recommended by the Committee on Court Practice and Procedure.
8. The limits on Revenue debts which may be pursued in the lower courts should be increased substantially.
9. Collection of tax on gifts and inheritances should be the responsibility of the Collector General.

## CHAPTER 16

### SPECIAL COLLECTION ARRANGEMENTS

#### **Introduction**

16.1 The Revenue Commissioners use a number of special arrangements to deal with difficult collection cases or to recover outstanding tax in certain situations. In this chapter we examine these special collection arrangements and discuss

- (i) instalment arrangements and deferred payments,
- (ii) the write-off of uncollected taxes and interest, and
- (iii) preferential claims in liquidation or receivership.

16.2 We also consider the 'phoenix syndrome' which occurs when a company begins trading, builds up a significant tax debt, disposes of its assets and liquidates without payment of the tax due. Trading is then resumed by one or more of the directors of the previous company, often in the same premises and using the same equipment but under the protection of the limited liability of the new company.

#### **Instalment Arrangements and Deferred Payments**

16.3 Instalment arrangements are formal agreements for arrears totalling more than £20,000 negotiated as a result of approaches from traders. These approaches are made on foot of enforcement action by the Collector General, investigation by the inspector of taxes and to a lesser extent refusals by lending institutions to advance money until tax liabilities are cleared up. These arrangements are made for PAYE/PRSI and VAT. They are not a significant feature in the collection of other taxes.

16.4 Normally, a trader in financial difficulties will propose instalment terms to the Revenue Commissioners. The Revenue Commissioners seek confirmation of this proposal in writing. The proposal is examined and ultimately a period of time for clearance of the arrears may be agreed. While negotiations may proceed for some time, these are not allowed to interrupt the momentum of collection and enforcement of outstanding

taxes and the trader is advised that current taxes must be paid. The arrangement, when completed, is put into an agreement (signed by the trader) stating the time period and the number of cheques, plus interest to be paid. The conditions regarding interest in instalment arrangements have been tightened recently. Once the agreement is signed, enforcement action is suspended.

16.5 Arrangements are monitored to ensure payment by due date of current taxes and honouring of all post-dated instalment cheques. In the event of non-compliance, a decision may be taken to end the arrangement and to refer collection of all outstanding taxes to the Revenue Solicitor or sheriff. In some cases the termination of an arrangement may be succeeded by proposals from the trader for a further arrangement. Only in very exceptional circumstances is a further arrangement agreed. In such circumstances, it is not unusual for the banks, Foir Teo or the IDA to be involved in a rescue package.

16.6 Deferred payments are a common feature of collection of all taxes. These apply to payments of arrears of tax not considered large enough to justify formal instalment arrangements. The arrears in these cases do not exceed £20,000 or extend over a long period. If it is decided that an arrangement may be allowed, post-dated cheques are accepted and the trader is advised that current payments must be paid as they fall due and interest on the late payments must be paid when demanded. There is none of the elements of formal instalment arrangements, such as protracted negotiations, formal agreement signed by the trader, inclusion of interest in each instalment, application of current payments to protect the preferential rights of the Revenue Commissioners and close monitoring of progress of the arrangement and current tax position.

16.7 We are satisfied that the Revenue Commissioners should have some discretion in relation to the approach to be adopted to secure payment of outstanding taxes. However, the procedures should operate within stated guidelines and should be subject to independent review. Instalment arrangements should be based on practical collection considerations and the Revenue Commissioners should not have the option to take account of considerations, such as the implications for employment, in deciding whether or not to collect overdue tax. If a financial analysis shows that a taxpayer must use tax money to remain in business, no permanent cure for the problem can be gained through granting instalment payments. There is a number of state agencies operating under the aegis of the Department of Industry, Trade, Commerce and Tourism and the Department of Finance whose function it is to provide financial assistance in circumstances where it is considered wise, as a matter of policy, to do so and it is for them and not for the Revenue Commissioners to provide such assistance. We

recommend that the Public Accounts Committee should review the procedures to clear arrears of tax by instalments.

16.8 In instalment cases, current tax and the instalment payments are sometimes offset against the oldest arrears. The effect of this is to preserve at all times a full twelve months' preferential indebtedness to the Revenue Commissioners, even though this indebtedness has been specifically paid as it arises. This practice gives the Revenue Commissioners a significant advantage over other creditors at a time when the ability of a company to survive may be in question.

16.9 The Irish Institute of Credit Management told us that

“By rapidly reducing the older liability while continuing to preserve and indeed increase its preferential claim against the company the Revenue Commissioners gain a significant double advantage over suppliers.”

16.10 We examine later the need for preferential status for tax debts and we conclude that there are grounds for retaining the preferential status of VAT and PAYE/PRSI. However, where current taxes have been paid it is reasonable that the Revenue Commissioners should stand in line with other unsecured creditors. Even then, the Revenue Commissioners may be entitled to the lion's share of any assets available because tax debts due are often substantial in relation to other debts. We recommend that the practice in instalment cases of setting payments of current tax liabilities against the oldest arrears should be terminated.

#### **Write-off of Uncollected Taxes and Interest**

16.11 The approved procedures in the Office of the Revenue Commissioners for passing unpaid tax as irrecoverable require that any case in which there is no realistic prospect of collecting unpaid tax be submitted formally to the Commissioners to have such tax so designated. Schedules of all such cases involving a tax loss of £100 or upwards are passed to the Comptroller and Auditor General who carries out a test examination on the items included and reports his findings to Dáil Éireann in his Report on the Appropriation Accounts. The Comptroller and Auditor General does not lay down guidelines on the amount of tax which may be written off. However, he must be informed of and be satisfied with the reasons.

16.12 Table 23 shows that tax remitted or written off as a proportion of total tax revenue is very small. However, the absolute amounts of tax written off each year are increasing. Over one third of the amounts written off each year relates to VAT. Other significant amounts relate to income tax and PAYE (between 23 and 29 per cent).

TABLE 23

## Remissions and Amounts Irrecoverable

Year	Amount	% of Total Tax Revenue
	£	
1981	492,564	0.02
1982	1,077,879	0.03
1983	1,380,807	0.03

Source: Appropriation Accounts.

16.13 There are no approved procedures for bringing details of interest not collected to the notice of the Dáil, although we understand that suitable procedures will be devised shortly. Collection of interest is very haphazard and it is unclear whether the Revenue Commissioners have powers to decide not to pursue statutory interest.<sup>1</sup>

16.14 We asked the Revenue Commissioners for a statement of the current policy and practice in relation to the collection of interest on overdue tax. They replied that

“Interest is reported for enforcement when overdue tax is reported. It is generally collected with the tax in these circumstances. In some instances taxpayers pay the tax to the enforcement agency but not the interest and the pursuit of such interest items is affected by the same considerations as arise in relation to interest on late payments.

“Very many payments are paid late but not so late as to become involved in the enforcement process. There are severe limitations in regard to the enforcement of interest arising on these late payments as will be evident from the overloading of the enforcement agencies which arises in connection with enforcement of tax. In practice only a very small minority of cases are pursued for interest on late payment. Selection is by reference to the scale of the accumulated interest charges in individual cases.”<sup>2</sup>

16.15 Under our proposals, interest on late payments would be charged at a commercial rate. Because of this we envisage that, in general, interest would be pursued to collection in all cases. Nevertheless, we recognise that administrative considerations may require some measures of latitude in relation to interest. However, the Revenue Commissioners should be obliged to report annually any mitigation of interest to the Comptroller and Auditor General in the same way as tax written off as irrecoverable.

<sup>1</sup>See paragraphs 3.14 to 3.16

<sup>2</sup>Agreed note of meeting with the Revenue Commissioners, 12 December, 1984.

We recommend that

- (i) the Revenue Commissioners should have a general power to mitigate interest but the use of the power should be restricted to exceptional cases, and
- (ii) the Comptroller and Auditor General should review the use made of mitigation in these exceptional cases.

#### Preferential Claims in Liquidation or Receivership

16.16 Section 285 of the Companies Act, 1963 puts the Revenue Commissioners in a favourable position in the event of receivership or liquidation of a company. In general, the Revenue Commissioners are preferential creditors in respect of one year's tax. The provision applies to all of the main direct taxes including corporation tax, income tax, capital gains tax, PAYE and to VAT. Similar provisions apply in relation to bankruptcy. However, capital acquisitions tax and wealth tax do not rank as preferential debts. Revenue preference extends also to interest on amounts claimed in priority.

16.17 It was put to us that the Revenue Commissioners have played a negative role in business failure, acting like a supportive bank by not demanding back taxes. If the Revenue Commissioners, sometimes by far the biggest creditor, had moved earlier and thus ensured some kind of corrective action, many of the trade creditors of big firms which have gone to the wall would not have collapsed. The perception of the Revenue Commissioners' attitude is that they rely on the fact that money will flow in from a preference claim in the event of insolvency.

16.18 This perception was reflected in the submission of the Irish Institute of Credit Management which stated that

“it is most improper, unfair and potentially disastrous for the Revenue Commissioners to allow ailing companies to continue trading and incurring further credit from suppliers of goods and services while in receipt of vital information which may indeed cast serious doubt on the ability of such companies to survive.

“The Institute believes that the provision of a twelve month period of preferential status has allowed companies in the past to falsely survive”.

16.19 We discussed the question of revenue priority in liquidation or receivership with the Institute of Taxation which suggested that

“there should be some mechanism whereby the Revenue Commissioners would have to register a charge publicly against a trader to obtain priority. Businesses which extend credit and then find that Revenue have a priority have a genuine complaint. However, a more efficient local collection system dealing with arrears would lessen the

argument for revenue priority in liquidation. Most felt that it was unfair that the Revenue Commissioners by deferring tax liabilities should decide whether a business should continue or go into liquidation. Revenue officials do not have sufficient expertise to decide this".<sup>3</sup>

16.20 The Consultative Committee of Accountancy Bodies — Ireland advised us that

"because the collection system operates so inefficiently, collection is not prompt, tax debts are allowed to accumulate and are seen as a source of working capital by a number of companies. It is essential that the Revenue Commissioners collect promptly. The Revenue Commissioners' status as preferential creditors would be unnecessary if a more efficient collection system was operated."<sup>4</sup>

16.21 We discussed these criticisms with the Revenue Commissioners. They told us that

"By reference to the overall numbers of employers and traders the incidence of formal insolvency is low. (See Table 24 below). Collection procedures are geared to gather in the bulk of the estimated Exchequer receipts as soon as possible after the due dates. In this process there is understandably emphasis on those cases from which the bulk of the total payments will be collected. Cases with lesser amounts due are processed as soon as possible thereafter by raising estimates where returns and payments remain outstanding and by referral for enforcement collection if necessary. Any undue delay in securing payment is attributable in the main to the problems associated with civil debt collection. There is absolutely no question of relying upon the preferential status accorded to portion of the taxes to protect the moneys due to the Exchequer. In particular cases, some of which may have been the subject of comment by the media, efforts by the Revenue to secure High Court judgements were obstructed by abuse of the legal system by the companies for as long as possible and it was only when it was clear that the Revenue was on the verge of obtaining and registering judgements that the companies went into liquidation/receivership."<sup>5</sup>

<sup>3</sup>Agreed note of meeting with the Institute of Taxation, 12 June, 1984.

<sup>4</sup>Agreed note of meeting with the Consultative Committee of Accountancy Bodies — Ireland, 12 November, 1984.

<sup>5</sup>Agreed note of meeting with the Revenue Commissioners, 12 December, 1984.

TABLE 24

Details of the Numbers of Companies Cases which Went into Liquidation/Receivership, 1981 to 1984

Year	Liquidation	Receivership	Total
1981	432	28	460
1982	608	95	703
1983	522	136	658
1984 (9 months to 30 September)	434	100	534
Totals:	1,996	359	2,355

Source: The Revenue Commissioners.

16.22 We regard as mistaken the criticism that the Revenue Commissioners frequently allow non-viable businesses with tax debts to continue to trade and to continue to incur liability for PAYE tax in reliance on the fact that unpaid tax is preferential in an insolvency. We have already recognised the particular problems of dealing with non-compliance in relation to such taxes as VAT and PAYE/PRSI. Time to pay outstanding tax is allowed only in exceptional cases. Postponed payments are allowed only to businesses which are able to continue operating and only on the basis that current liabilities are paid as they arise. The Revenue Commissioners do not rely on the expectation of recovery in an insolvency as an excuse for refraining from pursuing arrears of tax.

16.23 A frequent complaint of unsecured creditors is that they suffer from a lack of vital information in relation to the likely preferential debts of a company, particularly VAT and PAYE/PRSI payments due to the Revenue Commissioners. The published accounts of a company, if available, normally show the corporation tax liability of the company but amounts due for VAT and PAYE/PRSI are usually included in the figures for trade creditors and they are not separately identified. This information would be very useful to those attempting to assess the credit worthiness of existing and new customers. We recommend that consideration be given to the feasibility of requiring preparers of accounts to identify in financial statements amounts overdue in respect of these preferred debts.

### The Case for Revenue Preference

16.24 The justification advanced for revenue preference is firstly that debts owed to the community should have priority over others and secondly because the Revenue Commissioners, unlike others who give credit, do so involuntarily. Different considerations arise where the debtor is an agent of the tax collector rather than a taxpayer. Unless some measure of priority were accorded in these cases, the money collected would go to swell the insolvent's estate to the advantage of the general body of creditors.

16.25 The issue of revenue preference was dealt with by the Cork committee in the United Kingdom.<sup>6</sup> We agree with the conclusions of the Committee which unhesitatingly rejected the argument that debts owed to the community ought to be paid in priority to debts owed to private creditors. A bad debt owed to the state is likely to be insignificant in terms of total government receipts. The loss of a similar sum by a private creditor may cause substantial hardship and lead to further insolvencies.

16.26 Unlike other creditors, the Revenue Commissioners cannot choose those with whom they will transact business. Even if there are no delays on the part of the taxpayer, there will inevitably be a significant lapse of time after the transactions giving rise to tax liability before any attempt to collect the tax can be made. There is no means, such as may be available to private creditors, to restrict the amount of credit which is extended or to require existing tax liabilities to be discharged before further transactions, giving rise to fresh tax liabilities, are entered into. Moreover, it is common experience to find that the taxpayer, in his efforts to avoid impending insolvency, has ignored the demands for payment of tax while continuing to pay suppliers and other important creditors who will not continue to supply unless they are paid.

16.27 The Cork Committee was not persuaded that these facts justified the conclusion that debts due in respect of unpaid tax ought to be paid in an insolvency in priority to other debts. While the Revenue Commissioners are an involuntary creditor, they have much greater powers than other creditors. They may impose penalties, charge interest and have remarkable powers to obtain information including powers of entry and in some cases powers of search and seizure.

16.28 In any event, the Revenue Commissioners are not alone in being an involuntary creditor. The Cork Committee noted that

"Many suppliers of goods and services are constrained to extend credit facilities in accordance with the custom of the trade. In a practical sense they have no real choice in the matter and are sometimes unable to exercise credit control. Many other categories of involuntary creditors may readily be called to mind: litigants who obtain judgments for costs, for example, and the victims of breach of contract and tort do not normally extend credit voluntarily to their debtors. It is no fault of theirs that they find themselves owed money by an insolvent. In many cases, such creditors are deserving of much sympathy, yet their debts are subordinated to the Revenue Commissioners'

<sup>6</sup>Report of Committee on Insolvency Law and Practice (Cork Report). HMSO. CMND 8558.

preferential claim to tax. Sympathy for the misfortune of an involuntary creditor is not a sufficient ground for setting aside the over-riding principle of fair distribution of an insolvent's estate."

16.29 We recommend that the preferential position of the Revenue Commissioners be abolished in relation to assessed income tax, corporation tax and capital gains tax. The preference of local authorities in relation to rates and motor vehicle duties should also be removed.

16.30 Different considerations arise in relation to PAYE, employees' PRSI contributions, value-added tax and excise duties. In these cases, the Revenue Commissioners' claim is for money collected by the debtor, whether by deduction or charge and for which the debtor is accountable. The debtor is to be regarded as an agent of the tax collector rather than a taxpayer. Unless some measure of priority were accorded in these cases, the money collected would become part of the insolvent's estate to the advantage of the general body of creditors. We do not think it right that statutory provisions enacted for the more convenient collection of the revenue should accrue to the benefit of private creditors. In these special circumstances we believe the retention of a measure of Revenue preference is justified.

16.31 PAYE and PRSI returns are made monthly; returns for value-added tax are made very two months. We have considered whether the present twelve month period for preference in these and other cases is appropriate. To illustrate the nature of the problem, we set out below the procedure for collecting PAYE and PRSI contributions:

- (i) employers have a duty to deduct income tax from the pay of employees whether or not there has been a direction to do so from the tax office. The amount which should be deducted is ascertained from tax deduction cards, certificates of tax free allowances and tax tables which are supplied to employers,
- (ii) the net total of the tax deducted during each income tax month (beginning on the 6th of one month and ending on the 5th of the next) must be paid to the Collector General within nine days of the end of that month. There should thus be a payment by the 14th of each calendar month. There is no breakdown of the monthly payment to show the attribution of amounts to individual employees: that breakdown is made only at the end of each tax year. The only breakdown that the Collector General will expect to see in the monthly remittances is between PAYE tax and PRSI contributions which employers pay to him at the same time,
- (iii) the practical effect of these rules is that a response of some kind is expected from employers every month, usually in the form of a

remittance. Where there is no payment when one is expected, the Collector General raises an estimate of the liability to establish an enforceable debt. An employer is not expected to justify the amount of his monthly remittance and fluctuations from month to month are the common pattern, and

- (iv) the adequacy of the total remittances by an employer over the year is normally checked only at the end of the tax year and any underpayment is then recovered as quickly as possible.

16.32 It is obvious that the procedure is not proof against exploitation by dishonest or unscrupulous employers but there would be a very large cost to employers, as well as to the Revenue Commissioners in tightening up the procedure, for example, by monitoring employers' PAYE returns as a matter of course more frequently than at the end of each twelve months. Moreover, even if employers' underpayments were established more often than every twelve months, that would not necessarily reduce the time it takes to recover arrears. Speedy action to recover tax debts depends on establishing an efficient and effective collection system, as recommended in Chapter 15.

16.33 The vast numbers of VAT and PAYE/PRSI returns issued every year make it virtually impossible to take immediate and effective action to ensure compliance in every instance of failure to submit returns. We recognised this in Chapter 14 where we recommended a new system of penalties for failure to submit VAT and PAYE/PRSI returns. We also recommended that surcharges should be imposed only where there is repeated failure to submit timely returns in any period of one year.

16.34 In these circumstances, we have reached the conclusion that the present twelve month period for preference is not excessive. We recommend that the period for preference for each tax should continue to be twelve months. However, in the context of our proposed new structure for enforcement of revenue debt, we believe that a shorter period of preference is justified where returns have been made but the liabilities shown have not been discharged. The period of preference in relation to established tax debts for VAT and PAYE/PRSI should be limited to three months.

16.35 The question remains whether the Revenue Commissioners should have a preferential claim in respect of interest on preferential VAT and PAYE/PRSI debts. The underlying principle is that tax collected on an agency basis should not go to benefit the insolvent's estate. In view of this we see no grounds for the Revenue Commissioners to recover any more than the tax collected. We recommend that the preferential position of the

Revenue Commissioners in relation to interest on preferential debts be abolished.

### THE 'PHOENIX SYNDROME'

16.36 The so-called 'phoenix syndrome' occurs where a company begins trading, builds up a significant tax debt, particularly in relation to VAT and PAYE/PRSI but disposes of its assets and liquidates without discharging the debt. Trading is then resumed almost immediately by one or more of the directors of the previous company, often in the same premises and using the same equipment but under the name of a different company which then registers for VAT and PAYE/PRSI. Ordinary trade creditors and consumers may also suffer from this abuse of limited liability. The customs and excise authorities in the United Kingdom see this as an increasingly worrying collection problem in relation to VAT. There is also evidence that the phoenix syndrome could present collection problems in Ireland.

16.37 The Revenue Commissioners informed us that there is no definite information available on the scale of disposal of assets without first discharging amounts due in respect of PAYE/PRSI and VAT. Very often, the remaining surplus is too small to meet the creditors' claims, let alone the expense of an investigation by the liquidator into any such activities.

16.38 The Revenue Commissioners operate specific procedures where revenue is at risk. Publication of any development which might have an impact on the financial status of a company is noted and a check made to see how that company stands in the Collector General's records. In cases where charges are registered, there is a detailed examination of the company's tax payments. If payments are up-to-date, no further action is taken. This happens in about half of the cases checked. In the other cases action is taken to speed up payment if, by reference to the perceived level of liability, such action is desirable. Information of this nature is particularly relevant in cases where instalment arrangements to clear arrears have been made with the Revenue Commissioners.

16.39 The presence of a Collector General's certificate issued to a county registrar/sheriff inhibits the disposal of land and premises held under a lease because the vendor will be unable to give clear title. In particular cases, certificates are issued at short notice if the Revenue Commissioners become aware of an attempt to dispose of land or premises by a company which has arrears due. The company is then forced to go to the Revenue Commissioners and would have to provide a solicitor's undertaking to hold the net proceeds of the disposal to pay the arrears.

16.40 While these arrangements help to identify potential defaulters and go some way toward securing the revenue, in such cases they do not deal

adequately with the phoenix syndrome. There are two problems here; one is identifying phoenix cases, the other is devising special measures to deal with them.

### Identification

16.41 Apart from the usual investigative procedure undertaken by the Revenue Commissioners, we believe that persons who have been responsible for previous VAT, PAYE/PRSI defaults should be required to notify the Revenue authorities if they have become involved in a new business, whether as sole proprietor, partner or director. Such a notification requirement should be backed up by substantial penalties for failure to comply.

### Special Measures

16.42 A number of special measures has been considered by the Government in the United Kingdom to deal with the wider issue of irresponsible directors and to end the phoenix syndrome as it affects creditors and consumers generally. A White Paper on Insolvency Reform was published in 1984. It holds that the most effective way to stop irresponsible directors is to introduce tough penalties, including a measure of personal liability for wrongful trading. Under existing law, a director is only held personally liable if found to have traded fraudulently, a criminal action which is very difficult to prove in court. Under the UK Government's plans, as set out in the White Paper, wrongful trading arises when directors allow a company to trade beyond the point where they know, or ought to have known, that there is no reasonable prospect of meeting its liabilities. Other penalties proposed include automatic disqualification for three years from being a director of any company in the case of a director of a company which goes into compulsory liquidation.

16.43 In Ireland, there is a similar need to check rogue directors. The Department of Industry, Trade, Commerce and Tourism is carrying out a review of company law in this area and is preparing proposals for legislative change in 1986. This is a very complex area. In principle we agree that there is a need to check rogue directors but honest and responsible directors should not be deterred from joining companies needing their skills. The means by which these objectives could be achieved involve fundamental changes in the concept of limited liability. Such remedies are outside our brief. We therefore make no recommendations for change in company law.

16.44 However, there is a number of measures in the tax area which could be taken to secure revenue from businesses involving promoters of other companies which went bankrupt owing substantial amounts of PAYE and VAT. Once identified, such cases could be carefully monitored to ensure

that tax returns and payments are made on time. Early and vigorous enforcement action should be taken to deal with non-compliance.

16.45 Another option is to require some form of security from a phoenix company for taxes such as VAT. In the United Kingdom, the Commissioners of Customs and Excise may require a trader to give security, normally in the form of a bank guarantee, before registering him for VAT. Generally, the power is invoked where the directors of a company which wishes to register have been involved in other businesses which went bankrupt owing substantial amounts of VAT. We believe that some sort of security is justified where the revenue is at risk. The security could take the form of a bank guarantee or personal guarantees from the directors.

16.46 We recommend that the Revenue Commissioners should have the power to request security for any tax collected on an agency basis in cases where they are satisfied that the promoters of the business have been involved in other businesses which went into liquidation owing substantial amounts of PAYE or VAT. We do not specify the form the security should take. A company which is required to give security should have the right of appeal to the Appeal Commissioners and subsequently to the courts. If satisfactory security is not given it should be an offence to continue trading.

### Recommendations

16.47 We make the following recommendations:

1. The Public Accounts Committee should review the procedures to clear arrears of tax by instalments.
2. The Revenue Commissioners should have a general power to mitigate interest. The use of the power should be restricted to exceptional cases and the Comptroller and Auditor General should review the use made of mitigation in these cases.
3. In relation to PAYE, employees' PRSI contributions, value-added tax and excise duties, a measure of preference should be retained. In general, the period of preference should be twelve months. However, where returns have been made but the liabilities shown have not been discharged, the period of preference in relation to the established tax debt should be limited to three months.
4. The preferential position of the Revenue Commissioners in cases of insolvency should be abolished in relation to assessed income tax, corporation tax and capital gains tax. The preference of the local authorities in relation to rates and motor vehicle duties should also be removed.

5. The preferential position of the Revenue Commissioners in relation to interest on preferential tax debts should be abolished.
6. Consideration should be given to the possibility of requiring preparers of accounts to identify in financial statements amounts overdue in respect of these preferred debts.
7. Where the directors of a company which went into liquidation owing tax debts again set up in business in any capacity, they should be obliged to notify the Revenue Commissioners.
8. The Revenue Commissioners should have power to request security for PAYE, employees' PRSI contributions and VAT payments where the promoters of a company/ business which went into liquidation without discharging tax liabilities again set up in business. If satisfactory security is not given, it should be an offence to continue trading.
9. The Appeal Commissioners and the courts should have the power, on appeal, to waive any requirement for the provision of security if there is no culpability.

## Part V

### Administration of Specific Taxes

## CHAPTER 17

# ADMINISTRATION OF DIRECT EXPENDITURE TAX

### Introduction

17.1 In this chapter we deal with administration of the direct expenditure tax proposed in our first report. Because this tax would be new to Ireland we wanted to satisfy ourselves that the proposal was practicable so we dealt with a great number of the administrative issues in our first report. We repeat some of the arguments here. Now that we are making recommendations on the administration of taxation, it is easier to see how the operation of the direct expenditure tax would fit into the general system.

17.2 Our proposals for the reform of the Irish tax system are designed to be implemented in three phases. The introduction of a direct expenditure tax is the final element in phase three. The existing income tax system needs to be greatly simplified before the direct expenditure tax stage is reached.

### Developments in the United Kingdom

17.3 Following the publication of the Meade Report<sup>1</sup> which recommended a universal expenditure tax to replace income tax entirely, the Board of Inland Revenue in the United Kingdom published a memorandum<sup>2</sup> which commented on various aspects of the proposal including the administrative implications. While the memorandum deals mainly with the possibility of a complete change to an expenditure tax, it also deals with the effects of replacing the higher rates of income tax with a progressive expenditure tax of the type recommended in our first report. The importance of the memorandum from our point of view is that the Revenue

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<sup>1</sup>'The Structure and Reform of Direct Taxation'. Institute of Fiscal Studies, 1978.

<sup>2</sup>'An Expenditure Tax'. Board of Inland Revenue, Central Division, 1978.

Commissioners told us that they are in general agreement with its conclusions.<sup>3</sup>

17.4 The United Kingdom Inland Revenue memorandum sets out the difficulties to be overcome before a progressive expenditure tax could be introduced, provided this is confined to a relatively small number of taxpayers at the top of the scale of income and wealth as we have recommended. These difficulties appear to us to be capable of being overcome.

#### Assessment of Tax

17.5 The United Kingdom Inland Revenue memorandum concluded that a universal expenditure tax would only be possible if taxpayers assessed themselves. However, it went on to say that

“there would be less of a problem with an EST (expenditure sur-tax) only. There would be far fewer EST payers and (it can be argued) they would be more capable of assessing themselves, or of employing financial advisers to do it for them. Under such a regime, all taxpayers would continue to pay VAT or income tax at the basic rate and presumably the latter would be administered by the Department on the same lines as now. The question would be how to operate the EST to which the minority . . . would be liable. Meade assumes that this minority would be sophisticated enough to cope with self-assessment, although twenty years ago Kaldor thought otherwise. On the other hand, since there would be comparatively few EST payers, Revenue assessment would seem a possibility”.

17.6 We have already recommended a change from the existing system of direct assessment to self-assessment for non-PAYE income. Such a system should be well established before the beginning of phase three when the direct expenditure tax is due to be introduced. The basis of assessment for direct expenditure tax should be the same as that for income tax.

17.7 Liability to direct expenditure tax will be confined to a relatively small minority of taxpayers. These taxpayers generally will either have high incomes or substantial wealth and can be expected to be able to cope with compliance requirements more easily than the vast majority of taxpayers. Self-assessment would help to avoid some of the problems discussed in our first report of identifying taxpayers. The substantial administrative savings which would flow from the simplification of income tax which we have recommended would release sufficient resources to enable the direct expenditure tax to be administered properly.

<sup>3</sup>Extract from paper representing views of the Department of Finance and the Revenue Commissioners, November, 1981.

#### Information Required

17.8 We envisage that liability to direct expenditure tax would be computed on the basis of the income adjustment method. This method of assessment is best understood by examining a sample assessment for these purposes. This is shown in Table 25 which is reproduced from our first report.

TABLE 25  
Assessment Form for Comprehensive Direct Expenditure Tax

Add (1)	<i>Personal Income</i>		
	Wages and salaries	20,000	
	Dividends	2,000	
	Interest	500	
	Rent	1,500	
	Net Profits (Losses) Royalties	Nil Nil	
			24,000
(2)	<i>Capital receipts</i>		
	Realisation of capital assets	2,000	
	Amount borrowed	5,000	
	Receipt of repayment of past loans Reduction in money balances	1,000 Nil	
			8,000
(3)	<i>Windfalls</i>		
	Inheritances received	Nil	
	Gifts received	2,000	2,000
	Total chargeable items		34,000
Deduct (4)	<i>Non-Consumption Outgoings</i>		
	Acquisition of assets	10,000	Nil
	Amount lent		
	Capital repayment of past borrowings	1,000	
	Increase in money balances Gifts made	1,000 Nil	
			12,000
(5)	<i>Chargeable Balance</i> (Representing expenditure on consumption)		
			22,000

17.9 The tax return required for a direct expenditure tax would be little more detailed than the present income tax return. Details under item 1 are always required in the present return of income. The first categories under items 2 and 4 are generally also included if the assets disposed of or acquired are chargeable assets for capital gains tax purposes. Gifts and inheritances might also be returned for capital acquisitions tax purposes. Some additional

information would be required but this would be offset, at least in part, by a reduction in the information required for income tax purposes due to the abolition of some reliefs and allowances which we have recommended.

17.10 Separate returns would not be required for direct expenditure tax purposes. We consider that the existing Form 11 could be expanded slightly to provide the additional information required. This procedure was followed when capital gains was introduced and we see no reason why it could not be followed for direct expenditure tax.

### Collection of Tax

17.11 The Department of Finance and the Revenue Commissioners have advised us that

"There would be collection problems because an expenditure tax does not lend itself to a pay-as-you-go system like PAYE. The use of estimates for a pay-as-you-spend system would require a total review of each case at the end of the year since there is no way of knowing in advance what savings and dissavings are likely to arise in each case during the course of a year. The PAYE system would nevertheless have to be retained in full to deal with the collection of basic rate tax although this would be simplified, for example, through the elimination of all but one of the tax tables and a reduction in the number of end-of-year reviews."<sup>4</sup>

17.12 Those liable to direct expenditure tax whose income arises mainly from wages and salaries should continue to use the PAYE system as a means of paying their direct expenditure tax on a provisional basis. End of the year reviews would be required in a significant number of direct expenditure tax cases. However, the overall number of reviews would be substantially less than is needed now, due to the present complexity of the income tax system.

17.13 As far as other forms of income are concerned, the arrangements for payment of direct expenditure tax should be the same as for income tax.

### Certificates from Financial Institutions

17.14 Under existing law, deposits and withdrawals from bank, building society and other accounts are ignored for tax purposes. Changes in these accounts would affect direct expenditure tax liability.

<sup>4</sup>Extract from paper representing views of the Department of Finance and the Revenue Commissioners, November, 1981.

17.15 To assist taxpayers in preparing their returns, financial institutions would have to send them a certificate at the end of each year showing the net change in the balance of each account. This should not cause any difficulty. It was required under the transitional arrangements for phasing out income tax relief on personal borrowings after 1982.

### TREATMENT OF ASSETS

17.16 A direct expenditure tax must be operated by the income adjustment method outlined in paragraph 17.8. In principle, this adjustment, which we refer to as the 'expenditure tax adjustment', requires that all purchases of assets should be deducted from the tax base and all sales of assets as well as the income yield should be added to the tax base. In most cases, it is a simple matter to say whether a particular item of expenditure should be regarded as saving or as consumption. Difficulties would arise when an individual acquires assets which do not fall clearly into either category. To overcome this problem, the Meade Report suggests that assets be divided into two distinct classes which we refer to as 'listed assets' and 'unlisted assets'<sup>5</sup>. Only transactions in listed assets would be debited or credited to taxable income so that the expenditure tax adjustment would include disposals less acquisitions of listed assets. All transactions in unlisted assets would be omitted from the calculation. The income yield on unlisted assets would normally be included in the tax base. This would mean that unlisted assets would receive the normal income tax treatment. Any income out of which they were purchased would be subject to tax but the capital proceeds from their sale would not be subject to tax if spent on consumption.

17.17 In determining whether or not a particular type of asset should be listed, the Meade Report suggests that

- (i) listed assets should include all those items on which substantial capital gains can be made,
- (ii) durable consumer goods should be unlisted, and
- (iii) private houses should be listed assets.

We believe that a workable dividing line is that all assets which are chargeable assets for the purposes of capital gains tax would be listed assets, while all other assets would generally be unlisted.

17.18 The most serious difficulties arise in the treatment of the following assets:

- (i) housing,

<sup>5</sup>The terms 'listed' and 'unlisted' are used to distinguish between the tax treatment given to the two types of asset. It does not mean that there would be any formal register of assets.

- (ii) loans,
- (iii) consumer durables and
- (iv) antiques.

These issues were considered our first report. However, we return here to the treatment of housing.

### Housing

17.19 A dwelling-house purchased for owner-occupation represents an important form of saving and investment. For this reason, we believe that owner-occupied houses should be listed assets for direct expenditure tax purposes. This is consistent with our recommendation to regard all houses as chargeable assets for capitals gains tax purposes.

17.20 In principle, this would require that the annual benefit arising from such assets should be included in the tax base. This would be measured by the notional expenditure which the occupier would be deemed to make on the dwelling house. In this case, notional expenditure is the same as notional income which we discussed in Chapter 10 of our first report. The notional rent for the dwelling is the imputed rent on the dwelling, less an allowance for repairs and maintenance. Therefore, in principle, the occupier's tax base for direct expenditure tax purposes should be increased by the excess of the net annual rental value of the house over the net rent paid, if any.

17.21 The local property tax proposed in our fourth report is a simpler method of taking into account the notional income which arises from the occupation of houses. Whether or not this income is taxed as heavily as other income depends on the relative rates of property tax and income tax. In principle, a higher tax would be justified on houses occupied by those liable to expenditure tax or indeed income tax at the higher rates.

17.22 If this is not done, a person on the higher tax scale can distort his post-tax return on investment by putting his money mostly into his private dwelling. This raises the question of whether this treatment should be allowed to an unrestricted extent where the notional income from the investment is not fully charged to tax. One possible solution is to place an upper limit, both for acquisition and for improvement, on the amount of investment in private housing entitled to investment treatment and to treat outlay in excess of this limit as consumption. This leads to complications and distorts the housing market at the level of the upper limit.

17.23 It is important that genuine saving and investment should neither be over-taxed nor allowed to escape tax completely. The treatment of the purchase and maintenance of a dwelling house as tax-free saving therefore

requires a certain level of taxation in its use. The alternative is to treat the acquisition of a home as consumption, which would bring otherwise non-liable taxpayers into the direct expenditure tax net just when they can least afford to be there.

17.24 The widening of the direct expenditure tax base to include the notional income from property would help to reduce the rates of direct expenditure tax or to broaden the bands between rates. We recommend that the notional income from owner-occupied housing should be included in the tax base for direct expenditure tax purposes. The income should be calculated by reference to the value of the property as envisaged in Chapters 5 and 6 of our fourth report.

### RELIEF FOR SAVINGS MADE BEFORE THE TRANSITION

17.25 If it were decided that relief should be given to avoid the double taxation of savings made before the transition to a direct expenditure tax, it would be possible to do so. The objective would be to allow the consumption of accumulated savings without incurring tax liability and to disallow repayments of existing loans qualifying for an expenditure tax credit. Such an approach could also have advantages in preventing tax avoidance and avoiding changes in consumption patterns solely for tax reasons.

17.26 There is a number of methods of giving relief for accumulated savings.<sup>6</sup> Most of these involve a registration of initial net worth based on a detailed return. The concealment of savings would be of minor significance since it is immaterial whether a deduction for savings is obtained at the transition or later. There would be no reason for a taxpayer to conceal property in order to obtain a savings deduction at a later date.

17.27 The verification of a taxpayer's indebtedness would be even less important. If this item were under-reported, the taxpayer would have to continue this under-reporting when the tax came into operation, for, if the amount reported were increased, the increase in the amount of declared indebtedness would be registered as new borrowing and would attract liability to tax. However, if part of the indebtedness continued to be concealed, there could be no gains to the taxpayer because amounts applied to the repayments of the debts in question would not be deductible.

17.28 Neutrality in the transitional phase, both on the assets and liabilities side, would mean that neither tax gains nor tax losses could be made by arranging for consumption to be brought forward before the date of

<sup>6</sup>"Progressive Expenditure Tax — an alternative?" Sven-Olof Lodin, p. 123.

introduction of the direct expenditure tax. The question to be answered in determining liability would be whether or not the consumption was financed from income earned before the introduction of direct expenditure tax. Thus, the transitional rules would not lead either to a rush to consume or to increase savings before the introduction of the new system. Nor would there be any reason for a taxpayer to increase cash holdings.

17.29 The problem of arranging for existing savings to be free of tax if consumed and ensuring that the repayment of existing loans would not qualify for a tax credit could be tackled, as previously mentioned, by any one of the following methods.

#### **The Total Assets Method**

17.30 Under this method, the taxpayer's total assets and total liabilities are established. So long as gross savings remain above the initial level, all new savings and dissavings are taken into account in determining tax liability. The same applies to all new borrowing and loan repayments, so long as the aggregate indebtedness does not fall below the initial level. On the other hand, the consumption of savings existing at the time of the changeover would not involve liability to tax. The repayments of existing debts would not carry a right of deduction.

17.31 Under this method, the problems of control are minimised as it is only an overstatement of the asset side of the account which can yield a tax advantage. However, it would be difficult to achieve this, since any overstatement could give rise to a re-opening of income tax liability for earlier years.

#### **The Net Assets Method**

17.32 Under this method, the taxpayer's net assets would be established at the time of the changeover. If net assets were to fall below the initial level, then consumption would not attract tax liability. Other changes in net assets would be taken into account.

17.33 If the taxpayer had net liabilities at the outset, he would not obtain a credit when subsequently his net assets increased or his net indebtedness diminished. So long as net liabilities remained above the initial level, or the level when non-deductible repayments had been made, all changes in net assets would be treated in accordance with the new rules.

#### **The Credit Method**

17.34 Another transitional method which would allow a direct expenditure tax to be introduced with immediate effect would be through the

credit method. If the taxpayer had net savings, he would be given a tax credit, obtained by applying an average rate of tax to the amount of savings. He could use this credit subsequently by setting it off against expenditure tax liability incurred later as a result of dissaving. Conversely, in the case of net indebtedness, the taxpayer would be debited with a tax liability which would be set off against future savings or repayments of debts. Both credits and debits would be indexed. This method, which is similar to the net assets method, has the advantage that the transitional period required is shorter than with either of the other methods.

#### **The Capital Gains Tax Method**

17.35 The final method<sup>7</sup> does not require initial statements of net worth at the transition date. Assets and liabilities are treated separately. The method takes account of assets and liabilities when they were disposed of. In many cases disposal would involve returns for capital gains tax purposes — hence the name capital gains tax method.

17.36 To make things clearer, the date of introduction of the direct expenditure tax is referred to as 'E day'. Qualifying assets are those held by the taxpayer before E day. Taxpayers would be allowed to deduct from gross expenditure the value of qualifying assets sold after E day. The value of qualifying assets is the original cost less any depreciation allowed for tax purposes indexed from E day. Indexation removes any incentive to sell qualifying assets for tax reasons immediately after E day.

17.37 Qualifying loans are those held by the taxpayer on E day. Repayments of the indexed amount of these loans are disregarded as savings after E day.

#### **The Transitional Period**

17.38 None of the transitional methods outlined above needs to be used after a person's death. This is because, in assessing the taxation of heirs, there is no need to take account of the extent to which the deceased had taxed savings or untaxed loans. In other cases some form of time limit would be desirable. In general, we favour as short a transitional period as possible.

17.39 It is, of course, possible to introduce a direct expenditure tax without any relief for taxed savings and untaxed loans. In this case, all forms of consumption after the introduction of the new tax would be treated equally. We do not think that such an approach causes unacceptable

<sup>7</sup> 'Assessing Tax Reforms'. Henry J. Aaron and Harvey Galper. The Brookings Institution, Washington, 1985, pps. 99 to 100.

problems of equity between taxpayers, bearing in mind that so much saving has already been untaxed by virtue of income tax concessions and reliefs. We believe that the transitional method should be the one which offers the fewest administrative problems, provides the greatest protection against avoidance and the least possible disruption to economic life. We emphasise that the direct expenditure tax would apply over a single rate of tax on all income and not in the existing context of progressive rates of tax on inadequately defined income.

### **Conclusion**

17.40 Following the publication of first report, there were criticisms that the proposals to introduce a progressive expenditure tax for a relatively small number of taxpayers at the top of the scale was impracticable on administrative grounds. We remain convinced that a progressive expenditure tax is desirable and feasible. The problems of transition may be solved in different ways. It has also been argued that proposals for an expenditure tax for other countries have not been implemented and it would therefore be unwise to introduce even a limited expenditure tax here. The possibility that Ireland could be in the vanguard of tax reform should not be discounted as impossible. Otherwise we condemn ourselves to perpetual copying and/or revision of systems designed for other countries and other conditions.

## **CHAPTER 18**

### **ADMINISTRATION OF VALUE-ADDED TAX**

#### **Introduction**

18.1 In our third report we dealt with the goods and services which should form the base for value-added tax. Here we consider a number of administrative issues which have caused particular difficulties:

- (i) the determination and settlement of VAT liabilities, including the appropriate taxable period,
- (ii) VAT on imports,
- (iii) registration for VAT, and
- (iv) VAT on second-hand goods.

#### **ACCOUNTING FOR VALUE-ADDED TAX**

18.2 In general, VAT liabilities are determined on the basis of invoiced sales. However, some traders may opt to account for tax on the basis of cash receipts instead of invoiced sales. These are persons

- (i) who provide services, and
- (ii) those who sell goods almost exclusively to final consumers.

18.3 A number of submissions claimed that the use of the invoice basis creates a cash flow problem for those firms which make a large proportion of their sales on credit because VAT may have to be paid to the Revenue Commissioners before payment is received from the customer. The proposals put forward to offset this disadvantage included an extension of the time allowed for payment of VAT, an extension of the interval between submission of VAT returns and a suggestion that the cash receipts basis be extended to all traders.

18.4 Value-added tax on an invoice basis does not of itself directly affect the cash flow position of taxable persons. However, a trader's credit terms

and the taxable period for VAT, when combined with the invoice method, may affect his cash flow either to his advantage or disadvantage. This arises because VAT is paid on the basis of a trader's sales and purchase invoices but there is no requirement that the tax charged on sales has actually been collected or that the tax invoiced on purchases has actually been paid. In general, a trader accounting for VAT on cash receipts' benefits because he accounts for the tax an average of fifty days<sup>1</sup> after collection from his customers.

18.5 We sought the views of the Revenue Commissioners on extending the cash receipts basis to all traders. They advised us that

"If the cash receipts basis were made available to *all* traders there would be a serious change-over problem in that traders would have to pay tax on all moneys received after the date of change notwithstanding that the transactions to which the moneys referred may have been the subject of taxation on the invoiced sales basis."<sup>2</sup>

18.6 The alternative is to grant a 'tax holiday' during the transition from the invoice basis to the sales basis. Besides the transitional problems, there are other revenue implications for the Exchequer. In general, a charge to tax on cash receipts would arise later than the present charge on invoice sales; in effect, there would be a deferral of the VAT liability on sales compared with the present situation. However, traders would continue to claim credit for VAT paid to suppliers on the basis of invoices received. It would be impracticable to allow the credit by reference to the actual payment of the tax to the suppliers. Thus, the Exchequer would be required to finance claims for VAT refunds to traders before the due date for payment of the tax charged by their suppliers. At present, a refund or credit to one trader is matched by a payment from another. The operation of the cash receipts basis also gives rise to greater control problems, particularly in group companies.

18.7 While some traders may have an adverse cash flow with VAT payments because they give extended credit, the private sector as a whole enjoys a very large cash flow benefit under existing arrangements. Where extended credit is given, the recipient of the credit gets the cash flow benefit and one would expect this to be taken into account in relation to all the circumstances surrounding competitive marketing. We do not favour any extension of the cash receipts basis of accounting for VAT.

<sup>1</sup>Nineteen days and half the taxable period of two months.

<sup>2</sup>Material supplied at meeting with the Revenue Commissioners, 12 December, 1984.

## VAT Accounting Periods

18.8 The taxable period for VAT purposes is two calendar months (January/February, March/April, etc). Returns for each taxable period are required to be lodged with the Collector General by the 19th day of the month following the end of a taxable period. Persons continuously entitled to repayments (mostly exporters and traders selling zero-rated goods) are allowed to make monthly returns. Small traders dealing mainly in zero-rated goods may be permitted to lodge returns annually.

18.9 The appropriate VAT accounting periods and the timing of the payments should take account of

- (i) the constraints imposed by the Sixth Directive of the European Economic Community,
- (ii) the compliance cost of traders, and
- (iii) the administrative costs of the Revenue Commissioners.

18.10 The Sixth Directive provides that the frequency of VAT returns is at the discretion of each member state but returns may not be made less than once each year. The timing of payments of any VAT liability is also at the discretion of member states.

18.11 A major study<sup>3</sup> in the United Kingdom of the costs and benefits of VAT estimated the effects of cash flow benefits for VAT-registered traders. The distribution of benefits and costs varied between businesses of different sizes and between different sectors. The greatest advantage in absolute terms accrued to the largest firms, that is, those with a turnover in excess of £1 million. The benefits to such firms accounted for over 90 per cent of the overall benefits. The sectors which gained most were manufacturing and utilities and the retail sector which had mainly cash sales. The study showed that many large firms obtained a substantial net benefit from VAT — the value of their cash flow benefit greatly exceeded their compliance costs. Because of this, the study suggested that monthly payments might be appropriate for such firms. Despite the cash flow and managerial advantages for some smaller firms, compliance costs remained a real burden for most of them. Annual accounting for small traders was considered as a means of cutting compliance costs.

18.12 No similar study has been carried out in Ireland to establish the

<sup>3</sup>Sandford and Others, 'Costs and Benefits of VAT', 1981.

costs and benefits of VAT.<sup>4</sup> The United Kingdom study provides an indication of the likely distribution of the costs and benefits but the taxable periods for VAT and the length of time allowed for payment of tax in the United Kingdom differ from Ireland. The distribution of commercial credit in the United Kingdom may, also, be very different. The research findings in the United Kingdom are, therefore, of limited value in deciding the appropriate taxable periods and the timing of tax payments for businesses in Ireland.

18.13 The Working Party on Simplified Accounts also favoured annual accounting for some traders. They recommended that

“the Revenue Commissioners should examine whether those traders with VAT liabilities of up to £50 per two-month period might be given the option of making an annual return for VAT whilst those paying between £50 and £500 per period might be allowed to pay tax for the current two-month period by reference to the turnover of the same period of the preceding year with an adjustment on the agreement of their trading accounts.”<sup>5</sup>

18.14 The Working Party acknowledged that the proprietors of small businesses devote long hours to the preparation of VAT returns and in this recommendation they sought to relieve small traders of the obligation to submit six VAT returns annually. The recommendation envisaged that very small businesses would be allowed to account for VAT in a lump sum at the end of the year; other small businesses would have to make provisional payments on the normal due dates for VAT, with a settling up at the end of the year. The recommendation does not set out whether the period of a year is to be the calendar year, some other period of a year determined by the Revenue Commissioners or the normal accounting year of the trader for income tax purposes.

18.15 Annual accounting would reduce the number of returns but the volume of information summarised in each return would be multiplied, even with a single rate of VAT. Many traders have difficulty in completing two-monthly returns based on information which is reasonably current. These difficulties must surely increase if similar returns are to be prepared annually by inserting information relating to events which took place many months earlier.

<sup>4</sup>In 1976, the National Prices Commission engaged consultants to examine ways in which information and data required from firms by state agencies could be simplified. The consultants estimated that savings of over £0.5 million could be made by simplifying VAT records and bi-monthly returns.

<sup>5</sup>The Working Party on Simplified Accounts was set up by the Minister for Finance on 26 April, 1983. A report was recently presented to the Minister but it has not yet been published.

18.16 The suggestion that there should be a longer accounting period for small traders as a means of alleviating the burden of compliance costs is less relevant in the context of the single rate value-added tax system proposed in our third report. The single rate would significantly reduce the compliance costs of all businesses selling goods at different rates of VAT and in particular the compliance of small traders.

18.17 We have also considered whether the accounting period should be reduced to one month for large traders. While a case could be made for changing to a monthly accounting period for the one thousand or so cases which account for 70 per cent of the total VAT revenue under the present three rate system, these cases are now monitored to ensure that payments are made as they become due.

18.18 Any increase in the number of payment dates for VAT would increase the volume of work and hence the administrative costs of the Revenue Commissioners. There would be some administrative savings if the number of payment dates in a year was reduced from six to, say, four by extending the VAT accounting period to three months.

18.19 In the light of the foregoing, we consider that a two-monthly accounting system strikes a reasonable balance between the interests of traders, the workload of the Revenue Commissioners and the needs of the Exchequer. We make no recommendation for change in the VAT accounting periods.

#### VAT ON IMPORTS

18.20 In general, imported goods are liable to VAT at the same rate as applies within the state to the sales of similar goods. Manufacturing firms which export 75 per cent of their production are allowed to import their raw materials and components without making VAT payments. VAT on taxable imports is payable before the goods are released by the Customs, unless the importer is using the deferred payment scheme. This scheme enables VAT-registered traders to defer payment of VAT to the 15th of the month following the month in which the goods are imported. The deferred payment arrangements were devised originally for customs duties. VAT payable on imports is treated as a duty of customs. A full description of the operation of VAT on imported goods, together with details of the deferred payment scheme, is in Appendix 9.

18.21 VAT on imports at the point of entry was introduced on 1 September, 1982. This means that VAT-registered traders have to pay VAT before the goods are released, thus losing the advantage of the earlier arrangements whereby a VAT liability did not arise until the goods were sold. It was estimated that earlier payment of VAT would result in a cash

flow gain of about £140 million for the Exchequer in 1982. While there is no continuing net revenue yield from the new system any change back to the old system would delay the flow of funds to the Exchequer with a loss of revenue in the year of change. This could be offset to some extent by gradual re-introduction of the former system. However, the postponed accounting system for imports would continue to delay the flow of funds to the Exchequer because VAT liability on imports would not arise until the goods are sold. This system also weakens the control of VAT and could lead to evasion and fraud in relation to imported goods.

18.22 VAT on imports removes a bias in favour of certain imports. A system in which traders import goods without payment of VAT means that the importer has an advantage in buying goods free of tax from a foreign supplier rather than on a taxed basis from a home supplier but the extent of such benefit depends on the amount of credit allowed to him by his suppliers and on the length of the VAT accounting period. Since the VAT accounting period is two months and returns have to be lodged by the 19th of the third month, a trader whose purchases are made on a regular basis has to wait, on average, fifty days to claim credit for tax invoiced to him. Thus, if less than an average of fifty days' credit were being allowed by both the foreign and home supplier, there would be an incentive to buy from the foreign supplier. If more than fifty days' credit were allowed, it would favour the home supplier because a tax credit would on average be allowed to the trader before he had paid the tax invoiced by the supplier. Any gain to the trader would of course be at the expense of the home supplier and would not represent a gain to the community. To compete with foreign suppliers, Irish manufacturers would, in general, have to give longer credit terms to their customers.

18.23 Any discussion of VAT must have regard to the EEC context. It is clear that much of the future development of VAT will inevitably flow from EEC attempts to move closer to the realisation of the long-standing objective to abolish fiscal frontiers between member countries. The proposed Fourteenth Directive favours the system of postponed accounting for VAT on imports because it shifts the accountancy procedures for VAT from frontiers to inland tax offices. However, all member states, apart from the Benelux countries, operate some form of VAT at the point of entry at present. After the common basis of assessment specified in the Sixth Directive is fully operational, further movements towards the removal of fiscal frontiers would involve the imposition of a common rate structure. When both the common base and rate structure have been implemented throughout the Community the way will then be open for the abolition of fiscal frontiers. This implies a move from the present destination basis to an origin basis for intra-Community trade. In other words, a sale would be taxable in the hands of the vendor and the VAT incurred by the purchaser would be deductible irrespective of the member state in which it has been

charged. It seems likely at this stage that such a move will require a uniform rate of VAT within the Community. However, progress in this direction is likely to be slow.<sup>6</sup>

18.24 We recommend that VAT should continue to apply to imports at the point of entry subject to compliance with EEC obligations. We now consider three associated administrative issues:

- (i) VAT waiver for imports for re-export,
- (ii) Deferred VAT payments for imports, and
- (iii) VAT waiver for imports worth £200 or less.

#### **Vat Waiver on Imports for Re-export**

18.25 We noted earlier that manufacturing firms which export 75 per cent of their production may import their raw materials and components without payment of VAT. However, VAT applies to the imports of other export firms and to all other purchases of raw materials imported into Ireland.

18.26 The Confederation of Irish Industry advised us that

"The anomalous situation created by the collection of VAT at the point of entry is illustrated by the fact that the relief on raw materials imported by firms who export more than 75 per cent of their output, while very welcome to our major exporting firms, does discriminate against indigenous Irish firms and distorts competition on the domestic market in respect of those goods produced by qualifying firms which are not exported. The very high level of 75 per cent requires an indigenous firm to have developed an export market some three times its domestic market which is an unrealistic expectation."

18.27 By keeping the export requirement high, the distortion of competition created by sales on the home market by qualifying export firms is minimised. There are also administrative reasons why the export requirement should be high. Export sales are zero-rated. Thus, a manufacturing firm exporting 75 per cent or more of its production might not have sufficient VAT liability on sales to absorb the tax credits on imported purchases of raw materials if they were to be taxed at importation. This would give rise to repayments of tax with an increase in the workload of the Revenue Commissioners. A firm exporting less than 75 per cent of its production would be more likely to have a net VAT liability.

<sup>6</sup>The White Paper from the EEC Commission to the European Council of Milan, July, 1985 proposes measures to complete the internal market of the Community which include the removal of physical, technical and fiscal barriers within the Community.

18.28 A further consideration is the possible competitive distortion in favour of qualifying export firms which rely on imported raw materials. This would arise where the average credit period allowed by Irish suppliers is less than thirty four days,<sup>7</sup> that is, the average period an export firm paying tax on Irish raw materials would have to wait to claim a repayment of tax. Because of the limited period involved, any distortion is not likely to be significant. The impact is further reduced by the fact that most companies receive some credit from their suppliers. Any attempt to remove this possible distortion by treating the imported inputs of export firms in the same way as other imports would not be effective and would only add to administrative and compliance costs.

18.29 We consider that export manufacturing firms should continue to be allowed to import raw materials and components without payment of VAT. We do not recommend a relaxation of the 75 per cent exporting condition.

#### Deferred Payment of VAT on Imports

18.30 VAT is treated as a duty of customs when payable on imports. Accordingly, it must be paid or otherwise accounted for before the imported goods are released by the customs authorities. Facilities for deferred payment of VAT are normally given on application to the Collector of Customs and Excise. Under the scheme VAT is deferred until the 15th of the month following importation.

18.31 Payment of deferred taxes and duties is made through the banks' direct debiting scheme. The essential feature of this scheme is that the creditor, with the authority of the debtor, makes payments by the issue of a direct debit voucher drawn on the debtor's bank. To avail of the VAT and customs scheme (both taxes may be deferred at the same time, provided sufficient guarantee has been given to the Collector), the importer must apply to his local Collector of Customs and Excise by providing

- (i) a standard application showing the maximum amount of VAT and customs duties to be deferred in any one month. The amount must be broken down on the form and allocated over the various customs stations through which the importer intends importing his goods,
- (ii) a guarantee by the importer's bank (which is established in Ireland) that it will pay to the Collector on demand, VAT and customs duties deferred by the company in any one month up to the amount stated on the application,

<sup>7</sup>Repayments to export companies are normally dealt with on the basis of monthly rather than the usual two-monthly returns. The thirty four days is half of a month plus nineteen days.

- (iii) a debit mandate signed by the importer's bank enabling the Collector to debit the importer's bank account on the 15th of each month for VAT and customs duties deferred during the previous month, and
- (iv) an undertaking from the importer not to terminate the agreement without giving one week's notice.

18.32 If the importer exceeds the amount of guarantee in any port, then he must pay VAT and customs duties on all further imports through that port during the remainder of the month. There is an arrangement to 'top up' the guarantee by cash or cheque if it is short at the end of a month. In addition, an amount of guarantee may be moved from one import station to another. If the guarantee is exhausted in, say, Limerick and the importer does not wish to use the 'top up' facility, he may get the import documents (i.e. customs entry) passed in, say, Dublin where the guarantee is not exhausted and use those documents to clear the consignment in Limerick. In addition, permission may be obtained to use another person's deferral arrangement. However, in these circumstances, it is the importer and not the person with the deferred payment facility who can reclaim the VAT. Further details of the deferred payment scheme are in Appendix 9.

18.33 The bank guarantees required under the deferred payment scheme impose a cost on traders but the scheme allows traders to defer their VAT liability on imports for up to forty five days. The need to allocate the bank guarantee between different points of entry and the control of the guarantees causes some problems for traders. The Revenue Commissioners acknowledge that there have been complaints about this. They told us that

"the problem is essentially one of communications. A computer could deal with this problem but there are financial constraints and such a system would be expensive."

We consider in Chapter 19 the advantages of a computerised customs clearance system which would also deal with VAT at the point of entry.

18.34 There are practical difficulties in attempting to remove the system of bank guarantees for the deferred payment of VAT on imports. The essence of VAT at the point of entry is that the tax should be paid before credit can be taken for it in the normal way. Otherwise, the system would be undermined because VAT on imports, like any other VAT on purchases, is all reclaimable by VAT-registered traders. It would be impracticable to require traders to make separate returns and remittances for imports before the usual VAT returns for the same accounting period are made. The only way to minimise the administration and the inconvenience to traders is to have the VAT payments on imports made by direct debit to the importer's bank account. Under the direct debit system, it is necessary for the Revenue

Commissioners to have some assurance that adequate funds are available to cover the tax payments due. This can only be achieved by insisting on a guarantee from the importer's bank to meet the tax liabilities as they become due.

18.35 It would not be possible to abandon the system of guarantees for deferred payment of VAT on imports unless the deferred payment scheme itself were abolished or VAT on imports were removed. The abolition of the deferred payment scheme would mean that importers would have to pay VAT on imports before the goods were released. This would impose its own additional costs on importers. We have already outlined the advantages of VAT at the point of entry and we have recommended that it should be retained. We see no satisfactory alternative to the system of guarantees for deferred payment of VAT on imports.

#### **Imported Goods of £200 or Less**

18.36 VAT is not payable on parcel post importations of taxable goods by VAT-registered traders for the purposes of their business, provided the value of such goods is £200 or less. Goods of up to £200 may also be imported free of VAT if the VAT registration number is quoted and the goods are accompanied by the trader or a courier. These arrangements do not apply to commercial freight operators.

18.37 The Institute of Freight Forwarders of Ireland and the Irish Air Cargo Institute advised us that

"Multinational courier companies regularly bring in 600-700 items on a flight into Dublin Airport and they can be cleared by customs within an hour. No VAT is payable. This is undermining the business of established Irish customs clearance agents. The same goods imported by the commercial clearance agents would be subject to the normal entry procedures and would be subject to VAT not only on the cost of the goods but also on the freight costs which are added to the value of the goods before calculating VAT."<sup>8</sup>

18.38 We asked the Revenue Commissioners for their views on the operation of this special procedure for goods with a value of less than £200. They told us that

"Couriers are allowed to bring in goods without making entry only if the aggregate value of all the goods in their possession does not exceed £200. In such cases invoices are retained by customs and the goods are released without payment of VAT at import and after a

<sup>8</sup>Agreed note of meeting, 21 January, 1985.

certain proportion of the goods have been examined. Where a courier brings in goods with an aggregate value in excess of £200, each consignment involved must be the subject of a formal entry, the duty, and VAT being secured under a deferred arrangement. A special investigation which we have carried out reveals no evidence of such abuse."<sup>9</sup>

18.39 There is a clear conflict of evidence here which we have not been able to resolve. However, the fundamental question is whether there is a justification for this scheme. In principle, all imports should be subject to VAT irrespective of how they are imported. Nevertheless, there are administrative reasons for allowing VAT to be waived on goods of limited value. It is also convenient for traders. We recommend that the waiver of VAT for goods of £200 or less should be retained but the operation of the scheme should be subject to regular monitoring. The limit should be increased only in line with inflation.

#### **REGISTRATION FOR VAT**

18.40 Traders are obliged to register for VAT if their annual turnover exceeds or is likely to exceed the following amounts:

- (i) £25,000 a year for traders selling goods only and for traders who obtain not less than 90 per cent of their turnover from the sale of goods, and
- (ii) £12,000 a year for other traders, including traders supplying services.

Further details of the persons who must register for VAT including the special provisions which apply to farmers and fishermen are in Appendix 5 of our third report.

18.41 High value-added tax exemption thresholds for small businesses lead to a loss of VAT revenue, increased opportunities for income tax evasion and unfair competition between registered and unregistered traders. Different exemption limits for different trades cause confusion among traders, particularly where more than one activity is carried on. The initial loss of revenue as a result of an exemption threshold may, therefore, be increased by traders failing to register for VAT when their turnover is in excess of the appropriate limits.

18.42 Traders who are not within the VAT system are more likely to be outside the income tax records of the Revenue Commissioners. Even where such traders are known to the Revenue Commissioners, the standard of

<sup>9</sup>Letter of 15 April, 1985.

records maintained and the possibilities of verifying transactions by cross-checking invoices are likely to be less than in businesses accounting for VAT. However, registration for value-added tax purposes does provide traders with an opportunity to evade tax by reclaiming the VAT on purchases of personal consumer durables.

18.43 There is undoubtedly competitive distortion between a trader just above the registration limit and obliged to register and one just below the limit and not obliged to register. In effect the non-registered trader pays tax on his purchases while the VAT-registered trader accounts for VAT on his sales. The greatest benefits accrue to unregistered businesses with high rates of gross profit. The example below illustrates the difference in treatment between two retailers, one being registered and the other being unregistered, with similar turnover from dealing in the same goods.

### Example

	Registered Trader	Unregistered Trader
Annual turnover (tax inclusive)	£ 25,001	£ 25,000
VAT at 23 per cent	4,675	Nil
Purchases (tax exclusive)	12,000	12,000
VAT on purchases	Nil <sup>1</sup>	2,760
Total tax paid	4,675	2,760
Difference in VAT payable		£1,915

Note:

<sup>1</sup>The registered trader pays £2,760 on purchases but can recover this sum.

The discrimination of £1,915 in this example in favour of the unregistered trader would be aggravated by an increase in the registration threshold, an increase in the rate of gross profit or an increase in the rate of tax.

18.44 The distortion of competition between registered traders just above the limit and unregistered traders on or just below the limit, is even more marked in the case of services because of the relatively low level of purchases and the high rates of gross profit. The lower registration threshold of £12,000 reduces the distortions in the service sector. However, it should be borne in mind that the registered trader has an advantage over the unregistered in relation to zero-rated goods sold because, while there is no tax liability in respect of sales, the trader is entitled to claim input VAT. Even under our proposals, zero-rating would apply to exports and some agricultural raw materials. There is also a more general advantage in that registered traders will want to buy from registered suppliers (not from unregistered) in order to obtain input tax credit.

18.45 Attitudes of traders on registration limits are conflicting. On the

one hand, associations representing small traders seek increases in the registration limits to remove certain small traders from the scope of VAT and on the other, there is pressure to extend the scope of VAT to curtail the 'black economy'. The attempt to remove small traders from the scope of VAT is understandable under the multi-rate value-added tax system we have in Ireland. The reduction in the number of rates from six to four announced by the Minister for Finance in his 1985 Budget Statement should be of some assistance to small traders required to operate VAT. The situation would be further improved by the adoption of the single rate of VAT proposed in our third report.

18.46 It is intended that VAT should eventually become a fully harmonised tax within the EEC and the scope for national adjustments is restricted by various directives. The Irish registration limit of £25,000 is the highest in the EEC, the next highest being the UK limit of £19,500 sterling. The EEC Sixth VAT Directive prescribes a very low registration limit of approximately £3,600 but permits member states to retain their existing limits and, pending full harmonisation, to increase them to maintain their real value. Ireland's present thresholds are, it would appear, only barely acceptable to the EEC. The value-added tax registration thresholds for small businesses in EEC countries are shown in Table 26.

TABLE 26

Value-Added Tax Registration Thresholds for Small Businesses in EEC Countries, October, 1983

Country <sup>1</sup>	Annual limit £ <sup>2</sup>	Type of limit <sup>3</sup>
United Kingdom	22,690	Taxable turnover
Luxembourg	3,158	Tax-exclusive turnover
Denmark	895	Turnover
Ireland		Turnover
Businesses mainly involved in supplying services	12,000	
Other businesses	25,000	
Germany	6,473	Tax-inclusive turnover
Netherlands	592	Tax
France	142	Tax
Belgium	no exemption	
Italy	no exemption	

Notes:

<sup>1</sup>Greece does not yet have a value-added tax.

<sup>2</sup>Exchange rates as at 11 October, 1983.

<sup>3</sup>As shown in the table, registration limits differ in kind between EEC countries. In addition they are often operated in conjunction with special schemes for small traders.

18.47 The answer to the problems of small traders would seem to lie not in excluding them from the VAT system but in modifying the system to reduce the burden that falls on them. In our third report we concluded that

considerable savings in administrative and compliance costs would arise from reducing the number of different rates of value-added tax and by having one single rate applied to all goods and services. The proposed new structure provides the most efficient means of relieving small traders of the burden of compliance costs and the difficulties of complying with their obligations. In principle, we consider that all persons carrying on a business activity should be registered for value-added tax. In practice, some threshold below which businesses would not have to be registered would almost certainly have to be provided, though at a level substantially lower than the existing limits of £25,000 and £12,000. In the context of our proposed rationalisation of the value-added tax system, we recommend that there should be a single registration limit for all businesses below the existing limit of £12,000 for traders supplying services. Some reduction in the existing exemption thresholds could be achieved during the transition period involving a two-tier rate structure.

### **Anomalies in VAT Registration**

18.48 The letting of immovable property is generally exempt from value-added tax, except in the course of carrying on a hotel business or operating a car park. This exemption gives rise to a number of anomalies and inconsistencies in the businesses required to register and account for VAT. In our third report we stated that rented residential accommodation should continue to be exempt from value-added tax. However, the existing exemption is much wider than that and a number of business activities is excluded from the scope of VAT or has more favourable registration limits because of the exemption of the letting of immovable property.

18.49 Under existing VAT legislation, a bed-and-breakfast business, registered as a guest house by Bord Fáilte,<sup>10</sup> has a VAT registration threshold of £12,000 but for other bed-and-breakfast establishments the threshold is £48,000. This goes down to £24,000 if an evening meal is provided. The differentiation between registered guest houses and other bed-and-breakfast establishments arises because a guest house is included in the definition of a hotel for VAT purposes and, as in the case of a hotel, it must account for VAT on all revenue if the turnover exceeds £12,000. However, because of the domestic character of other bed and breakfast

<sup>10</sup>The approval of accommodation for tourists by Bord Fáilte has two different forms. The commercial categories (for example hotels, guesthouses, caravan parks, etc) are dealt with under a very formal process of 'registration' under the Tourist Traffic Acts 1939-83. The approval of 'Irish Homes Accommodation' is dealt with under a less formal process of 'listing' which is more suitable to the mainly domestic character of the premises concerned. These are divided into three different categories — Farmhouses, Country Homes and Town Homes. Approximately 2,100 are listed by Bord Fáilte under this process. Listing is done on a voluntary basis. Bord Fáilte estimates that there could be 4,000-6,000 premises operating on a 'bed-and-breakfast' basis without any approval system.

accommodation, revenue from letting the bedrooms is not liable to VAT; only that proportion of the revenue relating to the meals or sales of wine is reckonable for VAT purposes. In 1978, the Revenue Commissioners decided that it would be essential to have a basic apportionment of the inclusive bed/breakfast, partial and full board charges. Following consultations with Bord Fáilte and other representative organisations, they decided on apportionments of 25 per cent of the bed and breakfast charge and 50 per cent of the partial and full board charges as VAT-liable turnover. Hence the registration thresholds of £48,000 and £24,000.

18.50 The application of different registration limits to businesses providing similar services, even though the scale of the business may be very much less, gives rise to unfair competition. We have recommended in paragraph 18.44 that the same registration limit should apply to all businesses.

18.51 The general exemption of the letting of immovable property also means that subscriptions to sports clubs and other entertainment complexes are generally outside the scope of VAT and the operators do not have to register and account for VAT. There are one or two exceptions, for example, the revenue of snooker halls is regarded as arising from the letting of the tables and not the rooms and thus is liable to VAT. A bar or shop operated as part of a club would be required to register for VAT and to account for VAT on its sales in the same way as any other business.

18.52 We do not think that this form of expenditure should be exempt from VAT. The exemption of the letting of immovable property should be confined to rented residential accommodation. The case for this is argued in our third report.<sup>11</sup> All other activities involving the letting of immovable property should be chargeable to VAT, subject to the registration limits applying to other businesses.

### **SECOND-HAND GOODS**

18.53 Sales of second-hand goods (other than zero-rated goods) are liable at the 23 per cent rate, regardless of the rate which would apply to the same article if sold as new. In order to qualify as second-hand for this purpose, an article must have been the subject of substantial use. Shop-soiled or damaged goods or goods returned as defective do not qualify. This treatment gives rise to an element of double taxation because a trader is liable on the full selling price of goods purchased from final consumers but he is not entitled to a credit for any residual VAT in the purchase price paid.

<sup>11</sup>Paragraphs 5.68-5.70.

18.54 Where second-hand goods are traded in against goods of the same kind, only the actual amount of money paid is taxable. For example, if a customer is allowed £1,000 on his old car against a new car selling for £6,000, the dealer's VAT liability is related to the £5,000 cash he receives. The dealer is, of course, accountable for tax on the traded-in car when he sells it and his liability will be based on the actual selling price, not the traded-in value. This treatment of trade-ins overcomes the problem of double taxation in such transactions by taxing the trader only on the money received, thus in effect granting him a deduction for tax included in the trade-in allowances.

18.55 The Commission of the European Communities has initiated an action against Ireland in the Court of Justice because of Ireland's failure to charge the full sale consideration where trade-ins are accepted. The Commission contends that traders should be taxable on the full price of the goods sold in accordance with the Sixth Directive. This would include the value of a trade-in accepted in part-exchange for the goods sold. Any deduction for the residual VAT in the amount allowed for the trade-in is a separate issue which is addressed in the Commission's proposals for a Seventh Directive.

18.56 The Commission's proposal for a Seventh Directive envisages a special scheme to apply VAT to works of art, collectors' items, antiques and used goods. The taxable amount in respect of sales of works of art, collectors' items, antiques and used goods other than cars, pleasure boats, private aircraft etc. would be 30 per cent of the selling price. This is an attempt to tax only the gross margin of the trader, that is, the value-added. The full selling price would be taxable in the case of cars and boats but the trader would be allowed to deduct an amount of value-added tax based on the purchase price of the item at the rate in force at the time of purchase. The deduction would only arise, however, when the item is sold. Although presented to the Council in 1978, the proposals in the draft Seventh Directive have not yet been agreed and there has been no attempt to introduce the scheme.

18.57 In principle, we believe that second-hand goods sold by businesses and taxable persons registered for VAT should be charged to VAT and that the trader should be allowed a credit in respect of the residual VAT in the purchase price paid for second-hand goods. We are satisfied that the existing arrangements for the treatment of trade-ins grant in effect a credit for the residual VAT in second-hand goods acquired in this way. Despite the fact that there is no provision for a credit where second-hand goods are acquired other than by accepting goods in part exchange, we see no compelling reason to change the existing arrangements, unless it is shown that these conflict with our EEC obligations. Pending developments in the

European Community we make no recommendation for change in the treatment of second-hand goods.

### Recommendations

18.58 We make the following recommendations in the context of the general proposals for reform of value-added tax in our third report:

1. There should be no change in the length of the VAT accounting period or the timing of VAT payments.
2. VAT should continue to be charged on imports at the point of entry, subject to recommendations 3 and 4 below.
3. Firms primarily involved in manufacturing for export should continue to be allowed to import raw materials and components without payment of VAT. There should be no relaxation of the 75 per cent exporting condition.
4. The waiver of VAT on imports of up to £200 by registered traders should be retained but the operation of the scheme should be subject to regular monitoring. The limit should be increased only in line with inflation.
5. There should be a single registration limit for all businesses. This should be set below the existing lower limit of £12,000. Some reduction in the existing exemption thresholds could be achieved during the transition to a single rate of VAT.
6. The anomaly in the treatment of hotels, guest houses and bed-and-breakfast establishments should be removed.
7. The exemption of the letting of immovable property should be confined to rented residential accommodation. All other activities involving the letting of immovable property should be chargeable to VAT, subject to the registration limits applying to other businesses.
8. In principle, we believe that second-hand goods sold by businesses registered for VAT should be charged to VAT and that the trader should be allowed a credit in respect of the residual VAT in the purchase price paid for second-hand goods. However, pending developments in the European Economic Community, we make no recommendation for change in the existing treatment of second-hand goods.

## CHAPTER 19

# ADMINISTRATION OF CUSTOMS AND EXCISE DUTIES

### Introduction

19.1 In this chapter we examine the general administration of customs and excise duties. We received relatively few submissions about customs and excise matters but some issues were raised in discussions with various bodies. Customs did not form part of the review of indirect taxes in our third report because these duties are now largely Community taxes over which Ireland has no independent control. Many customs procedures are also governed by EEC rules. However, VAT at the point of entry is administered as a customs duty and this led us to examine a number of procedures. The issues we consider are

- (i) the consolidation of customs and excise legislation,
- (ii) appeal procedures,
- (iii) customs clearance procedures, and
- (iv) enforcement and penalties.

A brief description of the organisation and procedures of the customs and excise service is in Appendix 10.

### Broad Impressions

19.2 We have been struck by the complete dissimilarity of customs and excise to any other area of tax. The questions of assessment, collection and appeals arise in a different way from direct taxes and there is a high degree of physical control. It is often difficult to find the basis, legal or otherwise, for a particular practice or procedure. In part, the impenetrability of customs and excise stems from its antiquity as a form of taxation. The rules that govern the assessment and collection of customs and excise are contained in old legislation which has been added to and amended for over one

hundred and fifty years. Administrative procedures have also developed over a long period of time.

19.3 The key to the administration of customs and excise duties is control. The goods subject to duty are almost always physically present for examination by a customs and excise officer. Without adequate control of these goods, large amounts of revenue are at risk. Over the past few years effective control has been hampered by failure to redeploy existing staff, to streamline procedures and to introduce computerised back-up control and information systems. We were told, for instance, that the scale of physical examination prescribed in regulations is not being followed. There seems little impetus towards reform and improvement of the administration.

19.4 Public dissatisfaction with the tax system has not been directed towards customs and excise because it is only occasionally that the general public comes into contact with the customs and excise authorities. The administration of customs and excise is not subject to checks which exist in other tax areas. We believe that this arbitrary character can be counteracted by making the rules and procedures of administration clearer and better known and by improving the existing appeal procedures.

19.5 Despite the fact that there is a relatively small number of people involved with customs regarding commercial transactions, there seems to be a lack of communication and consultation between the customs authorities and their 'clients'. As a result, we were faced with conflicting evidence. We think communication should be improved.

### Legislation

19.6 There are very extensive legislative and administrative provisions for the collection and management of customs and excise duties, many dating from the early nineteenth century. A brief description of these provisions is in Appendix 11.

19.7 Over thirty five years ago the United Kingdom initiated a thorough examination of the customs and excise legislation with a view to consolidation resulting in the Customs and Excise Act, 1952. This Act repealed and amended about two hundred Acts of Parliament for a period of over one hundred and fifty years. Many of these Acts are still in force in Ireland. The main purpose of the 1952 Act was to simplify the law relating to customs and excise and to make it conform with modern requirements. A further consolidation took place in 1979 when the Customs and Excise Management Act, 1979 was passed. This consolidated but did not change the substance of the law or any customs and excise practice or procedure.

19.8 In the absence of consolidating legislation in Ireland, the provisions governing customs and excise are widely scattered. All customs regulations made by the EEC are published in the Official Journal of the European Communities. National customs and excise law has been published but some of it is so old that it is no longer in print. Other customs and excise information is contained in the Customs and Excise Tariff of Ireland and in public notices issued periodically.

19.9 We asked the Revenue Commissioners whether there was a need to review customs and excise legislation. They replied that

"We would not object to a consolidation of customs and excise legislation but it would demand a lot of time and resources. We also believe there is little demand for it since it is only a small number of large traders and manufacturers who are affected by excise legislation and these people make it their business to be acquainted with the legislation related to their own businesses. Customs and excise officers are given a variety of specific operating instructions rather than a grounding in legislation. EEC codification of customs law is in course of preparation. This will bring together the present scattered legislative provisions. However, the volume of legislation will remain large and highly complex. Some national legislation will remain in force despite the EEC consolidation."<sup>1</sup>

19.10 We have already stated that one of the principles of tax administration is clear and precise legislation. This is patently not the case with customs and excise legislation in Ireland. In our review of customs and excise we frequently found ourselves greatly handicapped by the lack of a single coherent body of legislation. We recommend that a review of legislation be undertaken in this area to update, simplify and consolidate the law relating to customs and excise.

### Appeal Procedures

19.11 The method of resolving disputes with the Revenue Commissioners on customs and excise matters differs from the procedure regarding inland revenue. The principal difference is that there is no independent Appeal Tribunal, other than the High Court, where disputes with the customs authorities may be taken. There is, however, an administrative appeal procedure. The initial appeal is made to the local customs and excise staff. If the dispute cannot be resolved locally, it is referred to the Office of the Revenue Commissioners. Consideration will be at Board level, if this is warranted and any type of case may come before the Board. In certain

<sup>1</sup>Meeting with the Revenue Commissioners, 19 March, 1985.

cases, goods may be released subject to payment of the higher duty 'on deposit' pending a determination on appeal. If on appeal a lower duty is found to be due there is a provision for the difference between the 'deposit' and the duty found to be due, or the whole deposit to be returned with interest at 5 per cent.

19.12 Most disputes which arise in the commercial area relate to classifications and valuation of goods. Since customs matters are now governed by EEC rules, disputes on these issues can be referred to various EEC management committees. An individual can appeal directly to the EEC Commission on a dispute over valuation and have the matter considered by the relevant EEC Committee. In practice, it is understood that a person who makes a direct appeal to the EEC Commission on a classification matter would be referred by the Commission to the Revenue Commissioners. If the question was not resolved at that stage, it would then be referred by the Commissioners to the EEC Nomenclature Committee. In each case, the relevant committee would require background information and views from the national administration. The Revenue Commissioners may, on their own initiative, refer a difficult case to the Valuation or Nomenclature Committees or they may do so at the request of a trader.

19.13 There are no independent appeal procedures in other EEC countries. In 1981, the Commission of the European Communities put forward a proposal for a council directive to harmonise the exercise of the right of appeal in respect of customs matters.<sup>2</sup> The proposal envisaged that an appeal would be lodged initially with the customs authority itself and subsequently with an independent authority. No progress has been made in agreeing the proposals put forward.

19.14 We are satisfied with the present administrative appeal procedures in relation to disputes on classification and valuation. The administration is best suited to deal with these issues and there is a right of appeal to the High Court. Further appeal may be made under certain conditions to the European Court. Where sums are paid 'on deposit' pending a determination on administrative appeal, they should be repaid with interest at a commercial rate if they are found not to be due.

19.15 The question remains whether there should be an independent appeal procedure for disputes other than those over classification and valuation. Such disputes would generally concern penalties imposed for evasion of duty or infringement of regulations.

19.16 Most customs and excise offences are criminal rather than civil

<sup>2</sup>EEC Draft Directive on the right of appeal in customs matters. (OJ No. C33/2, 14 February 1981).

matters, although there is also a range of monetary penalties. The criminal nature of the offences would preclude them for consideration by an appeals tribunal such as the Appeal Commissioners. In practice, minor offences of a non-commercial nature are generally settled on the basis of compromise settlements as an alternative to legal proceedings and forfeiture of the goods. Many larger cases are also settled by the acceptance of compromise settlements in lieu of court proceedings. These compromise settlements are made possible because of the power of the Revenue Commissioners to mitigate the monetary penalties. The majority of offenders seeks to settle cases.

19.17 We considered the possibility of decriminalising customs and excise offences and allowing the Revenue Commissioners to impose statutory civil penalties for less serious offences, subject to a right of appeal along the lines of the system described in Chapter 14 for other taxes. The nature of customs and excise offences is such that any appeal would require consideration of evidence relating to possession of goods without payment of duty and the concealment of goods. Such matters are closely related to the laws of evidence and criminal law.

19.18 We favour the retention of criminal offences for customs and excise offences. In practice, criminal proceedings are invoked as a last resort but they are a necessary ultimate sanction where there is persistent failure to comply with obligations and to evade large amounts of duty. This means that there can be no independent appeal other than to a judicial authority.

19.19 We conclude that the existing appeal arrangements are sufficient to deal with any appeals which might occur in the customs and excise area. However, we believe that the procedures need some review and we deal with this later in the section on seizures (paragraphs 19.33-19.42).

### **CUSTOMS CLEARANCE PROCEDURES**

19.20 Two issues arose in our discussions with various bodies regarding the clearance of goods by customs. These are

- (i) inland clearance depots, and
- (ii) computerisation

#### **Inland Clearance Depots**

19.21 Imported goods may be cleared at an approved premises of the consignee, an inland clearance depot, rather than at the port. An importer or clearance agent must apply to the Revenue Commissioners to open such a premises. In order to be permitted to remove goods to this approved premises, the consignee (or his agent) must present customs with a manifest.

If the documentation is in order, the container is allowed to proceed under bond and seal to the approved premises. The goods may be unloaded from the container at the approved premises if not selected for examination. The formal entry document to secure the release of the goods from bond must, however, be presented at a recognised customs office and may not be cleared at the premises.

19.22 The use of inland clearance depots has many advantages for both the Customs and the importers and agents. Customs officers have the opportunity of examining goods in detail if they decide to do a physical check. Importers and agents are not delayed at ports, their handling and storage charges are reduced and the transport and containers are freed for use again much more quickly.

19.23 However, the operation of these depots is not entirely satisfactory. The number of depots has mushroomed over the past few years to a point where there are now over sixty in Dublin alone. The number of customs entries has also increased substantially in recent years and there are now enormous pressures from businesses to have their goods cleared immediately. As a result inland clearance depots are not being controlled adequately by the customs authorities. In recent years some of the larger operators were permitted to present customs entries at these approved depots rather than at a recognised customs office. This temporary measure has now been withdrawn by the Revenue Commissioners. The present system of inland clearance depots makes it impossible to exercise effective control without increasing the staff of the Revenue Commissioners to unacceptably high levels.

19.24 We consider that the proliferation of inland clearance depots has seriously reduced the degree of physical control by the Revenue Commissioners. While we fully accept the need for physical checks we also acknowledge that there is a balance to be struck between the cost to importers of delays in getting goods cleared by customs and the control function of the Revenue Commissioners.

19.25 We believe that a small number of large inland clearance depots with permanent customs staff and all other facilities on site is the only solution to the conflicting needs of the customs authorities and the importers for adequate control and quick clearance. Such a system is operated successfully in other European countries, particularly in the United Kingdom and France. While it is mainly up to the importers to provide such premises, the Revenue Commissioners could provide the encouragement by refusing applications for unsuitable premises and limiting clearance facilities to a few big depots. We recommend that the number of inland clearance depots be limited to a few which have full customs clearance facilities on site.

## Computerisation

19.26 Some of the complaints we received about customs and excise related to the outdated procedures operated by the Revenue Commissioners in checking and clearing goods. Such procedures cause delays and increase the cost to the importers, are inefficient and wasteful of valuable manpower resources. Most of the difficulties with these procedures could be resolved by computerisation.

19.27 The EEC has approved a plan for computerisation of Community customs procedures.<sup>3</sup> It is estimated that customs formalities add significant costs averaging 6 per cent to trade in manufactured goods. The plan aims to automate customs procedures and speed up the preparation of information.

19.28 The Revenue Commissioners told us that they have been planning for the installation of a computerised clearance system. The problem is mainly one of cost. Customs and excise trade union representatives told us that computerisation would considerably ease the burden of paperwork on them. It would free them to improve their physical control of goods and would improve enforcement generally.

## ENFORCEMENT AND PENALTIES

19.29 The Customs and Excise authorities have very wide enforcement powers. These include the power to interrogate, require production of documentation, enter and search, arrest and charge and seize goods. The statutory basis of these powers are scattered over many acts, orders and regulations; some of great antiquity.

19.30 Powers such as arrest and charge may be exercised by the customs and excise authorities in their role as a law enforcement agency in the control of various classes of prohibited or restricted goods, for example, drugs, firearms and indecent or obscene books etc. These powers are rarely used in practice. We do not propose to consider these law enforcement powers other than to say that they should be exercised subject to the same controls as apply to the Gardaí and customs and excise officers should be accountable in the same way as the Gardaí.

19.31 One of the features of customs and excise enforcement is the high degree of physical control. Imported goods are subjected to selective physical examination. Excise duty controls for home-produced goods take

<sup>3</sup>CADDIA: Co-operation in Automation of Data and Documentation for Imports/Exports and the Financial Control and Management of the Agricultural Markets.

the form of both physical and documentary checks with greater emphasis placed on physical checks for commodities which bear high excise charges. Some examples of the various control methods used to check excise duties are given in Appendix 10. Adequate powers to require production of documentation and to enter and search premises are a necessary part of this physical control.

19.32 Because customs and excise legislation is not consolidated, it is exceedingly difficult to know the precise extent of the enforcement powers of customs and excise officers and the penalty provisions for various infringements. This has led to the exercise of considerable administrative discretion in the interpretation and application of customs and excise law. The scope of the discretion is governed to some extent by administrative provisions which are in General Orders and Customs Codes. These orders are not published and the public perception is that procedures are arbitrary and open to abuse, particularly in relation to powers of seizure.

## Seizure

19.33 Under customs and excise legislation any goods which are liable to forfeiture may be seized. The legislative authority for seizing smuggled goods is contained in the Customs Consolidation Act, 1876 for goods liable to customs duties (these would also include goods liable to VAT at importation and agricultural levies) and in the Finance Act, 1946 for goods liable to excise duties. Specific instructions are also given to customs and excise officers and these are not available for public scrutiny.

19.34 Table 27 shows details of the total seizures, excluding cars, for 1983. Seizures at the border and in border areas account for only 21 per cent of all seizures but for 63 per cent of the duty paid value<sup>4</sup> of smuggled goods. The average duty paid value of a seizure at the border is £1,475 compared with £217 elsewhere, that is mainly the ports and airports. These figures seem to confirm that, in addition to the legitimate duty free importations in baggage by travellers to Northern Ireland, there is a significant problem of evasion. The duty content in the 1983 seizures is £1.3 million making the average duty evaded £266.

19.35 The power of seizure is the same for all smuggled goods, irrespective of the amount of duty evaded. The duty evaded can vary: a few pounds on a bottle of spirits, a hundred pounds or more on a television set, a few thousand pounds on a motor vehicle or a large consignment of alcohol or tobacco. Seizures of prohibited or restricted goods such as drugs, arms or ammunition are also made by customs and excise officers. In the case of serious smuggling where large amounts of duty are involved or where the goods are prohibited, the power of seizure is one which has to be exercised to ensure that the goods do not circulate freely while legal proceedings are

<sup>4</sup>Duty paid value is the retail price of a good, i.e. the price of the good plus the amount of duty.

initiated. In cases of less serious smuggling, where only small amounts of duty are involved, the power of seizure often appears excessive in relation to the revenue at risk. It may also be inefficient in terms of the handling costs of goods seized. The Revenue Commissioners regard the power of seizure as a vital and essential part of the control of evasion.

**TABLE 27**

**Details of Total Customs Seizures (Excluding Cars) for 1983**

	Number of Seizures <sup>1</sup>	Proportion of Total Seizures %	Duty Paid Value IRE	Proportion of Value of Total Seizures %	Average Value of Seizures IRE
Seizures at Border and Border Areas	1,040	21	1,533,500	63	1,475
Seizures elsewhere	3,800	78	825,400	34	217
Fraud Cases [Customs Investigation Branch]	35 <sup>2</sup>	1	78,100	3	2,231
Total Seizures	4,875	100	2,437,000	100	500 <sup>3</sup>

Source: The Revenue Commissioners.

Notes: (1) Refers to seizures of goods on which duty is payable. Figures for seizures of prohibited goods such as pornographic books, obscene articles etc. are not included.

(2) In addition, there were fifty five cases of commercial fraud where no goods were seized by Investigation Branch.

(3) This figure represents the average value of all seizures.

19.36 The Ombudsman advised us that

“the procedures (for appeals in customs and excise) can be arbitrary and the compromise settlements may be open to abuse. There is a procedure known as ‘condemnation proceedings’ which can be used to bring a case before a court but people are generally unaware of this”.<sup>5</sup>

19.37 Under the Customs Consolidation Act, a person may dispute a seizure if he gives notice in writing to the Revenue Commissioners within one month of the seizure. If no notice is received within a month, the seized goods are duly condemned as forfeited. If notice is given, the Revenue Commissioners are obliged to take proceedings for the condemnation of the seized goods by the court. If the court finds that the goods were liable to forfeiture, the court shall condemn them as forfeited and this transfers the whole property of the goods to customs and excise, extinguishing third

<sup>5</sup>Meeting with the Ombudsman, 19 September, 1984.

party interests, if any. If the court finds in favour of the claimant, the goods are returned to him. Such proceedings are rarely taken.

19.38 Despite the existence of some genuine cases of wrongful seizures and the fact that the seizure of goods sometimes appears excessive in relation to the duty being evaded, we see no alternative to granting a general power of seizure to the customs and excise authorities. Any attempt to remove this power, even where relatively small amounts of duty are due on individual items, would give rise to further delays at ports, airports and other points of entry, increased documentation and possible abuse. However, if the power of seizure is to be maintained it should be operated within stated guidelines which are made known to the public.

19.39 The guidelines we recommend are as follows:

- (i) upon seizure of any goods other than prohibited goods, the owner should be issued with a receipt for the items seized. At present, customs and excise officers are not obliged under statute to issue receipts for goods seized unless the seizure is done in the absence of the owner in which case a notice of seizure is sent to the owner,
- (ii) persons from whom goods are seized should be informed that they may appeal or, if they do not wish to contest the validity of the seizure, how they may have the goods restored, and
- (iii) court proceedings for the imposition of a penalty should be initiated within six months of the seizure.

19.40 We asked the Revenue Commissioners to comment on the publication of a general code of procedure for seizures. They told us that a public general code of procedure appeared to be unnecessary for two reasons:

“In regard to the importation and exportation of goods, traders are already familiar with procedures. Traders and private importers/exporters are informed of their legal entitlements and of the law and regulations by various means, for example, information leaflets, public notices, display notices, newspaper advertisements which also caution, where necessary, about consequences if legal obligations are not fulfilled.

“Persons from whom goods are seized are informed that they may appeal to the Commissioners, and it rarely happens that appeals are not made either directly or through legal advisers or public representatives.”<sup>6</sup>

19.41 We believe it is not enough to assume that traders and citizens in

<sup>6</sup>Meeting with the Revenue Commissioners, 19 March, 1985.

general know their entitlements. At present, the citizen has to depend too much on the co-operation and goodwill of the customs and excise authorities to initiate and finalise their enquiries before they return goods wrongfully seized and even then goods are only released on the basis that no claim is made for damage while the goods are in official custody. We recommend that a general code of procedure for seized goods be published and made available to all persons at the time of seizure.

19.42 Under Section 213 of the 1876 Customs Consolidation Act, a reward is paid for every seizure made. The rewards are based on the amount of duty that might have been lost, and the money raised by the disposal of the seized goods. A total of £86,961 was paid to customs officers in 1984. The value of the reward to the individual customs officer is somewhat reduced by the fact that it is shared between all officers on duty at the time and there is a maximum of 'something in excess of £100' which may be paid for any one seizure. Nevertheless, there is a direct financial incentive to customs officials to seize goods. Rewards are regarded by the Revenue Commissioners as being a desirable incentive to customs officers. We believe that rewards are an anomaly. They do not apply to any other taxes. We think that they should be abolished.

### **Offences and Penalties**

19.43 Customs and excise legislation provides for a large range of offences and penalties. Many of these are set out in the original Victorian legislation. Other specific offences, for example, irregular use of rebated hydrocarbon oil, evasion of betting duty, breach of the Motor Vehicles (Temporary Importation) Regulations, are dealt with in the act introducing the excise duty. Most finance acts since the foundation of the state contain updated penalties for various offences. In addition to the normal penalties under the customs acts, the Finance Act, 1983 applied new penalties to tax offences including offences involving customs duties, excise duties and VAT. These provisions allow for fines up to £10,000 and jail sentences up to five years. A small range of various offences and penalties is listed in Appendix 12.

19.44 In the absence of any consolidated legislation in the customs and excise area it is extremely difficult to ascertain the full range of offences and the exact penalty which is due. In the consolidation of customs and excise legislation which we have recommended in paragraph 19.10, we recommend that particular attention be given to revising and consolidating offences and penalties.

19.45 In Chapter 14 we set out a number of general principles which relates to tax offences and penalties. All of these principles can and should

apply to offences and penalties in the customs and excise area. We recommend that offences be set down in legislation which would incorporate these principles.

19.46 In any revision of offence and penalty codes the objective should be to create modern, consistent and more readily understandable enforcement provisions. One means of achieving this standard is to band and categorize the whole range of offences and penalties. In Chapter 14 we proposed three categories of offences with specific penalties for each category in relation to direct taxes. We believe it is possible to follow similar lines in categorising offences and penalties for customs and excise and we recommend that such banding be adopted in the general revision of legislation.

19.47 Many of the monetary penalties in customs and excise legislation relate to the duty paid value of the goods i.e. the price of the goods, rather than the amount of duty evaded. The basic penalty of treble the duty paid value of goods is unrealistic given the level of compromise settlements. For example, a £600 TV set smuggled into Ireland from Northern Ireland would carry a penalty of £1,800 while the duty evaded might only be £230. The wide difference between the duty evaded and the penalty of treble the duty paid value gives considerable discretion to the Revenue Commissioners to mitigate the penalty. We believe this discretion should be limited. We recommend therefore that penalties be related to the duty evaded rather than the value of the goods. We do not recommend that any particular multiple of the duty evaded should be fixed as the penalty. However, it should be set sufficiently high to be a deterrent without being unrealistic. In the case of prohibited goods where no duty is evaded, the penalty might be fixed or might be related to the value of the goods whichever is more appropriate. If the goods have little or no commercial value, for example budgerigars or meat sandwiches, a fixed penalty might be appropriate. If the goods have a commercial value such as textiles or footwear from certain countries, a monetary penalty related to the value of the goods might be appropriate.

### **Recommendations**

19.48 We make the following recommendations:

1. A review of customs and excise legislation should be undertaken to update, simplify and consolidate the law relating to customs and excise.
2. A small number of inland clearance depots should be set up with full time customs and excise staff and facilities available on site.
3. The power of seizure should be retained but a general code of

practice for seized goods should be published and made available to persons concerned at the time of seizure.

4. Offences and penalties in the customs and excise area should be revised as part of the consolidation of legislation. This revision should take account of the general principles which we have laid down in respect of other tax offences.
5. Customs and excise offences and penalties should be banded and categorised.
6. Monetary penalties should be related to the duty evaded rather than to the duty paid value of the goods. In the case of prohibited goods, a fixed penalty or a penalty related to the value of the goods, whichever is the more appropriate, should be imposed.

## CHAPTER 20

### ADMINISTRATION OF MOTOR VEHICLE DUTIES

#### Introduction

20.1 In our third report, we made recommendations for the simplification of the unnecessarily complex system of motor vehicle duties. The present system substantially increases compliance costs as taxpayers rarely know the appropriate rate of tax on their cars or other vehicles. The cost of administration is also high at over 5 per cent of the total revenue. We believe that the simplification we have proposed would radically improve the administration of motor vehicle duties. In the rest of this chapter we discuss additional ways of improving administration.

#### Problems of Present System

20.2 The main problems with the present system of motor vehicle duties are

- (i) the complex structure of the rates,
- (ii) the high administrative and compliance costs, and
- (iii) the high level of evasion.

#### Rates

20.3 There is a total of thirteen classes of vehicle for duty purposes and there are five different rates of duty on private cars and nine different rates on motor cycles. A detailed description of the structure and rates of these duties is in Appendix 20 to our third report. We concluded in our third report that these structures were unnecessarily complex and we recommended considerable simplification. Simplification would improve administration, collection and enforcement.

## Administration

20.4 Since 1982 the cost of administration has fallen from 6.1 per cent to 5.4 per cent in 1984. We think this cost is still too high. In our third report we raised the question of handing over the collection of motor vehicle duties to motor insurers on an agency basis.<sup>1</sup> We now examine this proposal together with the possibility of the agency being given to An Post. Since the Gardaí are involved in the enforcement of motor vehicle duties, we also looked at whether they should be involved in the administration of the duties. However, we do not favour any proposal which would add to the administrative duties of the Gardaí.

## Motor Insurers

20.5 Under this proposal, motor vehicle duties would be collected at the same time as insurance premiums. There would be a single payment to the insurance company or broker. A disc covering both insurance and tax would be issued to the driver for display on the windscreen. Responsibility for remitting motor vehicle duties to the Exchequer would be imposed on the insurer or broker in the same manner as traders are now obliged to remit PAYE and VAT. The same audit procedures which apply to the collection of other taxes would apply to motor vehicle duties. Registration which is used by the Garda and customs authorities, would continue to be operated by local authorities.

20.6 The reaction of the insurance industry to this proposal was negative. The Irish Insurance Association advised us that

“Members could not envisage any worthwhile saving to the Government in operating a collection system via insurance companies”.<sup>2</sup>

20.7 There is a number of problems with this proposal. Firstly, a considerable amount of motor insurance business is done through brokers or agents. These brokers usually retain the premium collected for a period of ninety days. This type of structure would complicate the collection of tax and would militate against accountability. It would also put revenue at risk.

20.8 Secondly, the renewal dates of insurance and motor vehicle duty would have to be aligned for this scheme to operate. Under the present system of motor vehicle duty, the vehicle owner may opt for annual, semi-annual or quarterly payments. An increasing proportion of motorists is opting to renew motor tax on a quarterly or half-yearly basis. Insurance

<sup>1</sup>Paragraphs 10.27 to 10.50.

<sup>2</sup>Letter of 15 November, 1984.

premiums are so high that the payment of motor vehicle duty on the same date would represent a substantial financial burden on the motorist, unless an easy payments' scheme were introduced. Such schemes are currently operated by some insurance companies.

20.9 Thirdly, changes of vehicle ownership would impose special administrative burdens and legal difficulties. Under the present system, motor vehicle duty stays with the vehicle and transfers to the new owner. Insurance remains with the owner and transfers to the new vehicle. In order to avoid the administrative complexity of additional transactions, further realignment arrangements, refunds and motor vehicle duty would have to transfer in the same way as insurance. There are legal problems with this arrangement because insurance covers the driver or drivers while the motor vehicle duty covers the vehicle.

20.10 It is argued that despite the legal and administrative difficulties involved in aligning the two payments, there would be some gains through reducing the opportunity for evasion of both payments. At present, the law only requires that the insurance be current on the date of motor vehicle duty renewal. The insurance, therefore, may lapse some time before the motor vehicle duty runs out. The synchronisation of insurance and motor vehicle duties would rule out that possibility. A report into the motor insurance industry concluded that adopting the same date for payment of insurance and motor vehicle duties would

“entail administrative and legal problems which we do not think it would be worth incurring because the system would fail to catch those uninsured drivers, whom we believe to be the great majority, who do not licence their vehicles either”.<sup>3</sup>

20.11 It is more than likely that those who fail to pay tax are largely those who also fail to pay insurance. We do not accept therefore, that aligning insurance and motor vehicle duty would yield significant benefits through a reduction in evasion.

20.12 The major benefit that would result from the proposal is a reduction in costs of the public sector. To the extent that insurers or brokers would collect the duty at a marginal cost less than total public sector costs, there would be an increase in overall efficiency. In all the circumstances we conclude that motor insurers should not be asked to collect motor vehicle duties on an agency basis.

<sup>3</sup>Report of Enquiry into the Cost and Methods of Providing Motor Insurance, 1982.

## An Post

20.13 We believe that a better solution lies with An Post which already provides agency services to other government departments and state-sponsored bodies, handling TV licences, children's allowances and dog licences. It has a network of offices and staff through the country and a large number of offices in the Dublin area where difficulties with the payment of motor vehicle duties have been experienced. If the agency were handled by An Post, no legal difficulties would arise as insurance and motor taxation would remain separate. There would also be no need to align the dates of renewal of insurance and tax.

20.14 It could be difficult to implement this proposal under the present system with thirteen different classes of vehicle duty and five different rates. Our recommendation to simplify the system by reducing to one the number of classes and rates as well as abolishing some minor classes would overcome this difficulty.

20.15 Post office staff could not be expected to advise about motor vehicle registration. They can only be expected to deal with the completed form and the remittance. The present form has a rate of error of 25 per cent. The Department of the Environment told us<sup>4</sup> that its Vehicle Registration Unit at Shannon will soon be able to issue computerised motor tax renewal notices in advance of the renewal date. The notices will have all the registered particulars of the vehicle as well as the rate of tax payable. The applicant will confirm these details by signing the form. This will simplify form completion for the public and enable payment to be handled by an agent.

20.16 Finally, we do not envisage the complete abolition of motor taxation offices if An Post acts as the agent. New cars will always have to be registered at the motor taxation office, changes of ownership and verification of claims for exemption would also have to be handled there. In addition, the motor taxation office would deal with general public enquiries and keep all the records. We recommend that An Post take over the collection of motor vehicle duties on an agency basis.

## Evasion

20.17 There is a very high level of evasion of motor vehicle duties in Ireland. Latest estimates from the Department of the Environment reveal that the level of evasion is about 20 per cent.

20.18 To deal with the high level of evasion in the United Kingdom, a

<sup>4</sup>Letter of 17 May, 1985.

system of continuous liability for tax was proposed, whether a vehicle was on the road or not.

20.19 The case for continuous liability for motor vehicle duties rests on the simplification that this would allow in the administration of the duties and the degree to which it would facilitate the collection and enforcement of the existing duties.

20.20 A system of continuous liability was abandoned in the United Kingdom because it was seen as inequitable. We agree with this assessment and see no case for its application here. The justification for special taxes on transport is to cover the depreciation on the roads, to offset the costs imposed on the community by motoring and to regulate the imports of private cars. The first two elements do not apply when motor vehicles are not being used on the roads. Given that the excise duties on motor vehicles are payable irrespective of the degree of use, it is reasonable in principle not to levy motor vehicle duties in respect of periods when vehicles are not in use.

20.21 We consider that evasion could be reduced if the law were enforced more vigorously. Enforcement of the legal requirements relating to motor tax is generally a matter for the Garda Síochána. Table 28 shows the sharp upward trend in the numbers of prosecutions for motor tax offences.

TABLE 28  
Prosecutions for Motor Tax Offences, 1974-1983

Year	Number of Offences in which Proceedings Taken '000	Number of Convictions '000	Proceedings Taken as a Proportion of Vehicles Licensed %
1974	44	30	6.6
1978	57	37	6.9
1980	65	44	7.1
1981	76	48	8.0
1982	97	58	11.0
1983	174	88	19.0
1984	226	95	25.0

Source: Garda Commissioner, Annual Reports on Crime.

Note: The difference between numbers of proceedings taken and convictions is accounted for by cases where charges were dropped or dismissed, charges proved and an order made without convictions or where cases were adjourned or otherwise disposed of.

20.22 The upward trend in the number of proceedings taken is matched by the increase in the number of on-the-spot fine notices issued for non-display of tax disc, as Table 29 shows.

**TABLE 29**  
**Number of On-the-Spot Fine Notices Issued for Non-Display of Tax Discs**

Year	Number '000
1978	38
1980	58
1981	83
1982	94
1983	149
1984	161

Source: Garda Commissioner, Annual Reports on Crime.

20.23 Under present law, the maximum fine for driving an untaxed vehicle is £200 or three times the appropriate annual tax rate, whichever is the greater. The Department of Justice has supplied the details in Table 30 of motor tax offences for the period June, 1984 to November, 1984.

**TABLE 30**  
**Convictions for Motor Tax Offences, June to November, 1984.**

Type of Offence	Total Prosecutions	Average Fine £
No Tax Paid by Driver/Owner	434	91
No Tax Paid where Driver is not Owner	63	88
Prosecutions where Owners Fail to Pay Fines on-the-Spot	2773	35

Source: Department of Justice.

20.24 The average fine is well below the £200 level. However, no information is available on the number of cases where defendants produced evidence that arrears of duty had been paid to cover the dates of offences. It is the view of the Department of Justice that such payment would have a mitigating effect in the determination of the level of fines by the courts.

20.25 We believe that the penalty for non-payment of motor vehicle duty should be strengthened. A minimum penalty should be prescribed and some of the protection of the Criminal Jurisdiction Act, 1914 should be withdrawn. This requires a court, when fixing the amount of a fine, to take into consideration the means of the offender in so far as they are known to the court. The justification for this withdrawal is that anyone who has sufficient resources to put a car on the road should be deemed capable of paying road tax fines. There can be no sense in requiring a motorist by law

to pay, say, £300 annually in car insurance and £90 annually in taxation and then holding him unable to pay £200 by way of a fine when he fails to pay the legally due amounts.

20.26 We also considered the penalty of seizure. This penalty is used under customs and excise legislation, sometimes for a lesser offence than non-payment of motor vehicle duty, for example, inadvertently driving a foreign registered car. Seizure would present practical problems at the present high level of evasion. We think, therefore, that seizure might be considered for a second offence. A number of well publicised seizures would have a considerable impact on the level of evasion. We recommend that seizure be introduced as a penalty for non-payment of motor vehicle duty.

### Recommendations

20.27 We make the following recommendations:

1. The recommendations in our third report to simplify the rates of motor vehicle duties should be implemented.
2. An Post should be given the agency to collect motor vehicle duties.
3. The level of penalties imposed for non-payment of motor vehicle duties should be reviewed and seizure of the vehicle should be introduced as a penalty.

## CHAPTER 21

### RE-STRUCTURING THE SYSTEM OF TAXATION

#### Introduction

21.1 In this chapter we draw together the implications of our proposals for the structure of taxation and give our views on the considerations which arise in allocating the overall burden of taxation between the various taxes. We also set out the estimated revenue effects of the reforms we have proposed in our reports and we comment on certain aspects of the income distribution effects of our proposals.

#### Classification of Taxes

21.2 There is a number of classifications of taxes. The most commonly known and understood is that of direct and indirect taxes. As we noted in our third report<sup>1</sup>, apart from the fairly clear cases of personal income taxes and consumption taxes, it is difficult to classify taxes as either direct or indirect. The classification of taxes as taxes on income and wealth, taxes on capital, and taxes on expenditure also causes problems. For example, capital gains tax is regarded as a capital tax, while we would clearly see it (when there is full indexation) as a tax on income. Given these definitional problems we consider that the distinctions between direct and indirect taxes and between taxes on income and taxes on capital are not very helpful in analysing tax structures.

21.3 Almost any proposition can be proved about the direction of tax policy if a particular classification of taxes is chosen to support the argument. Given that reductions, or increases, in particular classes of taxes give rise to considerable political debate, we believe that great care must be exercised here. For that reason, we do not propose to offer guiding principles concerning the aggregate amount of revenue it is appropriate to raise from various groups of taxes. However, we do indicate certain levels appropriate

<sup>1</sup>Third Report, Appendix 2.

to individual taxes and we identify the constraints both on the overall level of taxation and on the level of some particular taxes.

#### Rising Level of Taxation

21.4 The level of taxation in Ireland is high and has been rising over the last thirty years. Table 31 shows that the share of taxation in gross domestic product has almost doubled in the past twenty five years.

**TABLE 31**  
Share of Total Taxation in Gross Domestic Product in Ireland

Year	Share %
1955	22.5
1960	21.9
1965	26.0
1970	31.2
1975	32.1
1980	36.5
1984	40.6

*Source:* Revenue Statistics of OECD Member Countries and Department of Finance.

#### Constraints

21.5 Ireland is a poorer country than most of its neighbours in Western Europe. In the absence of significant transfers of income from abroad, Ireland's relative poverty must be reflected in lower private consumption, lower public expenditure, high taxation or some combination of these elements. If any of these elements gets seriously out of line with neighbouring countries to which there is reasonably free access, there will be movement from Ireland to other countries. This movement may take the form of emigration of individuals, diversion of trade, transfer of capital, or loss of foreign investment.

21.6 Therefore, a major constraint on the overall level of taxation in Ireland and of its distribution between various taxes is the position in other countries, particularly the United Kingdom. Irish governments may find this inconvenient, but they can ignore it only at the cost of increasing Ireland's relative poverty.

21.7 The international constraint is very severe in relation to some taxes and less so for others. Ireland has little or no freedom in relation to the level of value-added tax and excise duties on certain goods. This also applies to taxes which enter into industrial costs, such as employers' social insurance

contributions. Corporation tax payable by the exposed market sector is also subject to some constraints. However, there is more freedom in relation to the level of income tax and capital taxes. There is considerable freedom in setting the level of property taxes and motor vehicle duties (car tax) where the external constraint is virtually non-existent. The lack of external constraints is one of the factors which makes property taxes suitable sources of local revenue.

## REVENUE EFFECTS OF OUR PROPOSALS

21.8 In this section we set out the estimated revenue effects of the reforms we have proposed in our reports. This follows from our terms of reference which required us to consider an adequate revenue yield in making our recommendations. One of the advantages of our proposed system is its flexibility. The same revenue yield could be raised by a number of different combinations of a single rate of income tax, personal tax credits and a single rate of VAT. It is clear that there is scope to alter the structure of taxation while maintaining an adequate revenue yield.

### Timing

21.9 We have set out a timetable for implementing our proposals on direct and indirect taxation. Some proposals could be implemented at the start of the next tax year, others would have to be phased in. If implementation started in 1986/87 we would not expect our proposals to be fully operational until at least 1990. In assessing the revenue effects of our proposals we have had to assume a situation in which all our proposals are operational in the year 1983/84. This is the latest year for which an accurate tax base is available. It is also a period during which taxation as a share of gross domestic product was at very high levels.

### Possible Tax Structures

21.10 Some of the possible single rates of income tax and VAT and the level of personal credits for a given rate structure are set out in Table 32. We emphasise that these alternative tax structures are intended to show only that there is a relationship between the rate of income tax, the level of credit and the amount of revenue raised in VAT. We use four illustrations but many others could equally be made since they merely provide indications of the choices available in a particular year. We did not recommend any rate of tax or tax credit in our first report. These must be determined together and are matters for political decision. The higher the credit — the higher the rate — if the same revenue is to be raised. An increase in VAT revenue would allow an increase in tax credits or a reduction in the rate of income tax.

TABLE 32

Possible Tax Structures under Proposed New System, 1983/84

Single Rate of Tax (including 5 per cent Social Security Tax)	Credits Equivalent to Personal Allowances for a Given Rate of Tax	Credits Equivalent to Personal Allowances, Less Adjustment for Social Insurance Contributions	Single Rate of VAT
%	£	£	%
35	—	385/770	13.4
35	508/1016	—	16.0
38	550/1100	—	13.4
40	580/1160	—	11.75

Note: The net revenue effects of these tax structures are set out in Tables 13.1 to 13.4 in Appendix 13.

21.11 The net revenue effect of our proposals, assuming a single rate of income tax of 35 per cent (including 5 per cent social security tax) with a personal credit for a single person of £385 and £770 for a married person, a single rate of value-added tax of 13.4 per cent and other taxes set at levels which would be consistent with our proposals, is shown in Table 13.1. (Appendix 13).

21.12 The VAT yield for 1983, on which our estimates are based, is broadly equivalent to a single rate of 13.4 per cent, arithmetically calculated. The tax credits represent the amounts necessary to ensure that persons who are not liable to income tax but who pay social insurance contributions would pay only an amount of tax equal to the PRSI contributions which they pay now. For example, in 1983/84 a married employee earning £2,900 was exempt from income tax but was liable for £248 in social insurance contributions. The tax credit of £770 is computed on the basis that he would still be liable for that amount of tax while all employees earning less than that would gain. If it were desired to grant tax credits equivalent to personal allowances, without any adjustment for the savings to taxpayers from abolishing social insurance contributions, higher credits would be needed. The additional revenue required could be raised by increasing the rate of income tax to 38 per cent or the rate of VAT to 16 per cent.

21.13 If it were desired to reduce the income tax rate below 35 per cent to, say, 34 per cent, this could be done without any loss of revenue by allowing tax credits of £370/£740 and adopting a VAT rate of 14.5 per cent. The higher VAT rate would increase VAT revenue by some £90 million.

21.14 Alternatively, it is possible to reduce the revenue from indirect taxation by setting the income tax rate at 40 per cent and allowing tax credits equivalent to personal allowances. If this were done, a single VAT rate of 11.75 per cent could be achieved without a loss of revenue.

### **Basis of Estimates**

21.15 We have based our figures on estimates supplied by the Revenue Commissioners where they could supply them. The data on which to calculate estimates of changes in tax policy of the type we proposed are variable. In some instances the data are inadequate and make reliable estimates difficult. However, the figures provide an indication of the orders of magnitude involved. In most cases we have taken the figures supplied and the assumptions made by the Revenue Commissioners. We have used our own estimates in a very small number of cases in which we are satisfied that the Revenue Commissioners have both insufficient data and are being unduly pessimistic in their assumptions. We specifically identify these areas of disagreement. The bases on which our revenue estimates are made are set out in Appendix 13.

21.16 In making calculations about the revenue effects of implementing our proposals, we have taken no account of any increase in revenue which would arise from adopting a tax system that encourages economic growth in place of one which inhibits it. It would be naive to assume that just because we are unable to measure it, the present tax system has no cost in lost growth. To take one example: there is great concern about the fact that the efficiency of investment in Ireland is very low by international standards. Much of this may be related to tax which distorts investment decisions to an extraordinary degree. By changing to a system which encourages productive rather than just tax-efficient investment, we could reasonably expect an increase in the efficiency of investment.

21.17 In our second report we considered the possible approaches to a change from free depreciation to normal depreciation of assets on an indexed basis. If the new system were related to the written down value of assets for tax purposes, there would be a significant flow of cash to the Exchequer in the transitional period. If the change in the basis of depreciation were confined to new investment only, special provisions would be necessary to allow relief for assets which had not been fully written off. We recommended that normal depreciation on an indexed basis should be extended to existing assets on the basis of their written down values, assuming normal depreciation. The costings in Appendix 13 take account of this scheme which would benefit those who had invested in the past by re-instating investment in plant and machinery and other assets for capital allowances under the proposed new system of taxation.

21.18 Our proposals involve a significant change in the structure of VAT. The present structure with rates ranging from zero to 23 per cent would be replaced by a single rate. The VAT yield for 1983, on which our estimates are based, is broadly equivalent to a single rate of 13.4 per cent, arithmetically calculated. The Revenue Commissioners told us that some

allowance should be made for the increased efficiency and better compliance which could be expected under a single rate. We have not taken account of this in our calculations. In addition, some goods and services would benefit under our proposals from a reduction in value-added tax. This could lead to increased demand for certain types of goods. Most excise goods would benefit from a reduction in VAT. The question arises as to whether or not excise duties should be increased to compensate. We would have no objection in principle, provided the excise duties conform to the criteria we laid down in our third report.

21.19 It should also be borne in mind that under our proposals the existing employers' social insurance contributions would be abolished. We take the view that this is mainly passed on to consumers in the form of higher prices. Therefore, if the basis of employers' social insurance contributions is changed from payroll to profits, we believe that indirect taxation could be raised by up to £400 million without any net increase in prices.

21.20 We have assumed for the purposes of these calculations that there will be no revenue from stamp duties, which we recommended should be abolished. We have also said that we do not regard the abolition of stamp duties as a priority matter but rather as a change that should be implemented in the longer term, as resources permit. The introduction of a property tax would involve the removal of stamp duties on conveyances of residential property. However, during the transition to the proposed new system of taxation there would be an annual revenue yield of some £20 million from other stamp duties and fees.

### **INCOME DISTRIBUTION EFFECTS OF OUR PROPOSALS**

21.21 In this section we comment on certain aspects of the income distribution effects of our proposals. We have noted that our proposed system is flexible. Various combinations of tax rates and credits in the direct tax system, variations in the yield of direct expenditure tax and progressive accessions tax, changes in the balance of direct and indirect taxation and adjustments in the application of public expenditure schemes provide the scope for a total tax and public expenditure system which is capable of satisfying the distributional preferences of all parts of the political spectrum. This enables the structure of the system to be taken outside the political debate, thereby ensuring a stability which is essential if investment decisions are not to be inhibited and if administration of the tax system is to be efficient.

## Incidence

21.22 In our reports we have paid particular attention to the effective incidence of taxes rather than to their formal incidence. Following our analysis we are unable to put any reliance on simple assumptions about incidence of certain taxes which underlie published studies in this area. For this reason, it can be misleading to construct examples which would purport to show the income distribution effects of our proposals. The assumptions necessary before such examples could be constructed would be clearly unrealistic.

21.23 In most income distribution models, no attempt is made to allocate the burden of taxes such as corporation taxes and employers' social insurance contributions. These taxes are paid, in effect, by individual taxpayers rather than by institutions which cannot, by definition, bear the burden of any tax. Our proposals generally imply a shift from these 'invisible' taxes to taxes which are more clearly borne by the personal sector. Any income distribution analysis of our system compared to the existing system, which fails to allocate the burden of invisible taxes, will give a false impression that the real burden on the personal sector has been increased.

## Equity

21.24 In looking at equity, the tax system cannot be judged in isolation but must be examined in conjunction with government expenditure which is financed ultimately from tax revenue.

21.25 In this context we agree with the view that

"The tax system is only one part of the redistributive process, the other main element of which is public expenditure. Given the increasing extent to which current public expenditure has been financed by borrowing and the growth in the current budget deficit relative to GNP, the impact of public expenditure on the distribution on income is now greater than that of the tax system. In the pursuit of equity and of reducing inequality in living standards, the tax system must therefore be judged in conjunction with the composition of Government expenditures. In pursuing greater equity, the Board believe that a greater contribution should come in the years immediately ahead from the side of Government expenditure"<sup>2</sup>.

<sup>2</sup>Proposals for Plan 1984-87 p.69.

21.26 Our recommendations have been consistent with such an approach. The main areas in which we have pursued this strategy are

- the substitution of a nominally progressive direct tax code by a clearer and fairer system applicable to all — not merely some — forms of income,
- the substantial reduction in the number of income tax payers liable at the higher rates,
- the elimination of many secondary income tax allowances and their consolidation, when necessary, with direct social welfare payments,
- the discontinuing of futile and inefficient attempts to make the indirect tax structure progressive, and
- the placing of full responsibility for income maintenance on the system of direct payments.

21.27 The question about the impact of our proposals has been frequently put to us over the last three years — who gains and who loses? Unfortunately there is no simple answer to that question. It depends very much on how the system is applied. The first thing to be said is that we could all gain because steps to reduce tax rates by widening the tax base, even without any reduction in revenue, could in themselves make a major contribution to the growth in national output. By removing the distortions which now exist, the efficiency of investment would be improved.

21.28 Secondly, those who have ordered their affairs to take maximum advantage of reliefs and allowances in the existing system may well change their behaviour while the new regime is being phased in. It would be foolish to assume that taxpayers will not adjust to face the changed conditions under the new system.

21.29 Thirdly, we proposed a system of taxation which is, like any good system, capable of producing widely different income distribution effects. Different tax credits can be associated with various single tax rates — the higher the rate, the higher the credits can be. Variations in the yield of direct expenditure tax and progressive accessions tax will alter the redistributive impact of the system. Changes in the balance of direct and indirect taxation also allow further freedom on distributional issues.

21.30 When these factors are associated with possible adjustments in the application of public expenditure schemes, it is clear that the tax system we propose, taken in conjunction with the distribution of public expenditure, is capable of satisfying a very wide range of distributional aspirations. This should be sufficient to enable the structure of the system to remain outside the political arena. The political debate could concentrate on adjustments

within the same overall system to achieve different objectives. The discussion on the level of taxation, the distribution of its burden and the way in which its yield should be spent could then be pursued in a more open and effective way.

Miriam Hederman O'Brien (Chairman)  
Donal S. A. Carroll  
Derek Chambers  
James R. Gallagher  
Daniel Murphy\*  
Donal Murphy  
Donal Nevin  
Patrick P. O'Neill  
Raymond O'Neill  
W. J. Loudon Ryan

Séamus P. Reic  
Secretary  
Deirdre Dowdall  
Assistant Secretary  
30 July, 1985

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\*Subject to Reservation — See page 301.

## RESERVATION

by

**Mr Daniel Murphy**

1. While I am in general agreement with the other members of the Commission on the recommendations contained in this report, there are two aspects of the recommendations with which I do not agree.
2. One concerns the recommendation for a change in the administration of Motor Taxation. The report recommends that the collection of Motor Taxation should be handled by the Post Office on an agency basis. The report also envisages that it would be necessary to retain Motor Taxation Offices to carry out functions relating to the registration of new vehicles and changes of registration. Thus there would be two separate agencies involved. There is no assessment made of the likely cost of the new system of administration which might very well turn out to be greater than the existing cost. I have no strong feeling of principle as to whether the function should be transferred to the Post Office or not but, unless it can be shown that it would be more economic to do so and the report has not done this, I would be opposed to the change recommended.
3. The other issue on which I must part company with the report is the suggestion to the effect that the system of seizure rewards payable to Customs Officers should be discontinued. I consider that this is outside our terms of reference since it concerns a matter of conditions of employment of some staff in the Revenue Commissioners which is an issue we have not dealt with in any other respect. It is completely inappropriate for the Commission to deal with issues relating to Conditions of Employment of the staff of the Revenue Commissioners which are a matter for regulation in accordance with the normal industrial relations procedures.

DANIEL MURPHY

*15th August, 1985*

## Appendices

## APPENDIX 1

### CONSTRUCTION INDUSTRY : TAX DEDUCTION SCHEME

#### Introduction

1. In this appendix we outline the operation of the scheme for deduction of tax from certain self-employed sub-contractors in the construction industry.

#### Background

2. The original tax deduction scheme for the construction industry was introduced in 1970 and was intended to curb tax evasion by self-employed sub-contractors in the industry. It imposed an obligation on persons making payments under construction contracts to sub-contractors to deduct and pay over to the Revenue Commissioners tax amounting to 35 per cent of the gross payment. It was accepted that this scheme of deduction ought not to apply to well-established sub-contractors who had been making regular returns for tax purposes and who complied with their tax obligations. Provision was made for the issue to them of certificates which enabled them to obtain payment without deduction of tax. This scheme of certificates was abused in many ways and on an extensive scale. A new scheme was introduced in 1976 with the object of eliminating these abuses and tightening controls generally.

#### Construction Contracts

3. The legislation applies to payments made as part of a 'construction contract' to a sub-contractor. The definition of 'construction contract' is fundamental to the operation of the legislation. Contracts of employment are excluded and, in effect, a construction contract is one under which a contractor is liable to a principal to carry out construction operations or to be answerable for carrying out these operations by others. The definition of 'construction operations' is framed in very wide terms so as to include most operations related to the construction industry.

### Principals

4. The legislation requires a principal to deduct tax at 35 per cent from payments which he makes to a sub-contractor and to pay the tax over to the Collector General. In general, a principal is a person who is himself a contractor under another construction contract or who is what is popularly known as a builder. The definition also extends to local authorities, Ministers of State and statutory bodies of various kinds. As a result, the legislation covers most sub-contract work in the construction industry. It does not apply, however, to a client and his contractor and, therefore, does not affect the ordinary householder.

### Sub-contractors

5. When the profits of the sub-contractor are being computed for tax purposes, the gross amount of any payment is included in his accounts and not merely the net sum which he receives after deduction of tax. He is given credit against his tax liability for the tax deducted, less any tax which has been repaid to him.

6. Tax deduction from a payment may be repaid after the end of the income tax month in which the payment was made. The refund is based on the estimated income tax liability for the year and the proportion of it corresponding to the proportion of the year from 6 April to the end of the period covered by the claim is taken. To this is added any other amount of tax for which the sub-contractor is liable, plus any amounts of VAT, PAYE and PRSI contributions which he is liable to remit. If the tax deducted in the period of claim exceeds this amount, then the excess is repaid.

### Certificate of Authorisation

7. A sub-contractor may apply to the Revenue Commissioners for a certificate of authorisation to receive payments in full. The conditions for the issue of such a certificate are

- (i) that the applicant is, or is about to become, a sub-contractor in the construction industry,
- (ii) that the business is, or will be, carried on from a fixed place of business established in a permanent building with such equipment, stock and other facilities as are, in the opinion of the Revenue Commissioners, required for the purposes of the business,
- (iii) that records which will enable true returns to be made for the

purposes of computing the profits or gains of the trade will be kept,

- (iv) that the applicant has, throughout the qualifying period of three years, complied with his tax obligation in relation to
  - (a) the payment of tax,
  - (b) the delivery of returns of income,
  - (c) the supply of accounts or other information to the inspector of taxes, and
- (v) that there is good reason to expect that the applicant will continue to keep proper records in respect of periods ending after the end of the qualifying period.

8. The Revenue Commissioners have discretion to disregard the failure to fulfil any of the conditions for the granting of a certificate if they consider that the failure ought to be so disregarded. A sub-contractor has no right of appeal against a refusal by the Revenue Commissioners to issue a certificate.

9. There is also provision for the cancellation of a certificate in certain circumstances. Where it is considered that a certificate of authorisation should be withdrawn from a sub-contractor on the grounds that he no longer complies with the statutory requirements, he is given advance notice to enable him to arrange his affairs so as to continue to qualify for a certificate.

10. When a sub-contractor's certificate of authorisation has been cancelled, the principal contractor is notified to this effect and informed that thereafter he is required to deduct tax from any payments made to that sub-contractor.

### Construction Payments' Card

11. To obtain payment in full, a sub-contractor must produce his certificate to the principal, who in turn applies to the Revenue Commissioners for a construction payments' card. On the first occasion in each year of assessment in which an authorised sub-contractor produces his certificate of authorisation to a principal, the latter prepares a form signed by both himself and the sub-contractor. The principal sends the form to the local inspector of taxes requesting a construction payments' card in respect of the sub-contractor. The form indicates where the work is to be done and whether the payment is to be made in respect of a group of persons and whether payment is to be made

- (i) by cash on the site,
- (ii) by cheque on the site, or

(iii) by cheque to a given postal address.

The inspector compares the sub-contractor's signature on the form with that on the office file and, if satisfied, he prepares and issues a construction payments' card to the principal.

12. The principal is not entitled to make the payment without deduction of tax until he receives the construction payments' card. He is required to obtain the signature of the sub-contractor on the card before making the first payment. As further payments are made to the sub-contractor during the year, he enters details of the payments on the card. The card at all times remains in the possession of the principal until he returns it to the inspector with the end-of-year balancing documents.

## APPENDIX 2

### THE PAYE SYSTEM

#### Introduction

1. In this appendix we set out the historical background to the introduction of PAYE in Ireland. We also describe the main features of the present system.

#### Historical Background

2. Up to 1960, remuneration in the form of wages, salaries, fees and certain pensions was charged to tax by direct assessment under Schedule E. Leaving aside commencement and cessation of employment, the taxpayer was normally charged to tax by reference to his earnings in the previous income tax year. The tax due was payable in two equal instalments. Many wage-earners found it extremely difficult to make provision out of their earnings for payments on that basis. The problem was aggravated by the increasing numbers of employees who became liable to tax for the first time in the years leading up to 1960. This situation created a demand, especially from employees and their trade union representatives, for the introduction of a statutory system of tax deduction which would ensure as far as possible that the correct amount of tax was deducted during the course of the tax year.

3. Following receipt of the First Report of the Commission on Income Taxation, the Minister for Finance on 3 April, 1959, announced that the Government had decided to introduce a scheme of deduction of income tax from remuneration which would spread the payment of tax more evenly over the year.

4. The scheme devised is fundamentally similar to the 'Pay As You Earn' (PAYE) scheme operated in the United Kingdom<sup>1</sup> but it was modified to suit Irish conditions. The characteristic of the system is that it is 'cumulative' and is designed to ensure that the employee's tax is corrected on each pay-day to be accurate to that date. The principal difference between the Irish and the British systems is the manner in which the amount of the tax-free

<sup>1</sup>The PAYE system was introduced in the United Kingdom on 6 April, 1944.

allowance is notified. In the British system, code numbers are used. Each employee is allotted a code number representing the allowances and reliefs due to him for the tax year. When used in conjunction with tax tables produced by the Revenue Commissioners, the code ensures that at the end of each pay period the employee receives the appropriate proportion of the total tax allowances and reliefs to which he is entitled for that year. Under the Irish system the actual monetary total of tax-free allowances is notified to the employee and the employer. The figures of cumulative tax-free allowances for each week/month of the tax year are printed on the employee's tax deduction card.

5. When the PAYE system came into effect in Ireland on 6 October, 1960 it was welcomed by employers and employees alike because it was thought easier for the taxpayer, imposing less hardship. In view of the developments which have taken place since 1960, it is ironic that opposition to the introduction of PAYE should have come from the Revenue Commissioners.<sup>2</sup>

### The Present System

6. People in receipt of wages, salaries and certain pensions pay tax on them by deduction at source under the PAYE system. The total tax is calculated on current year income. The employee provides details of his personal circumstances to the Revenue Commissioners by completing a tax return when he commences employment and from time to time thereafter. The allowances due in any pay period (that is, weekly or monthly) and the rate of tax or tax table are determined by the inspector of taxes. A notice showing how his allowances have been calculated (Notice of Determination of Tax-Free Allowances) together with a detachable certificate showing his total allowances (Certificate of Tax-Free Allowances) are sent to the employee. It is the employee's responsibility to pass this certificate to his employer. In practice, however, employers receive copies of the certificates of tax-free allowances in respect of their employees direct from the inspector of taxes. Official tax deduction cards are also supplied to employers by the tax office in respect of all employees unless an employer has been authorised to use some other system (usually computers) in lieu of tax deduction cards.

7. Where a taxpayer has additional income to his main source of earnings, particularly a state pension, his tax-free allowances can be so reduced that the amount of tax due on both sources of income can be collected from his earnings. Similarly, if an employee has underpaid tax for a previous year, that too can be collected by reducing his tax-free allowances for the current

<sup>2</sup>Commission on Income Taxation First Report, pr 4891, Chapter 6.

year or for some future year. Thus, underpayments 'coded-in' in this way are collected by easy instalments some time in the future rather than in a lump sum. This arrangement for the collection of underpayments also suits the Revenue Commissioners who might otherwise find it very difficult to collect such tax.

8. PAYE is a 'cumulative' system of deductions, under which the tax deducted in any week or month does not depend solely on the pay of that week or month but is arrived at after taking account of total pay received and tax deducted since the start of the tax year, so ensuring that the correct amount of tax is withheld over the year as a whole. Because PAYE is a cumulative system, employers need to take into account an employee's earnings from a previous employment during the year in order to be able to withhold the correct amount of tax. Form P.45 provides the information needed. When an employee leaves an employment during the tax year his employer must fill in form P.45 summarising his pay and tax deducted and give it to him. The employer must also notify the tax office. On taking up a new employment, the employee gives the form P.45 to his new employer who in turn notifies the tax office. During a period of unemployment an employee may claim refunds from the Revenue Commissioners as his tax-free allowances accumulate, there being no income to place against them. If a new employee has neither a tax-free allowance certificate nor a P.45, tax is deducted on an 'emergency basis' until such time as regular tax deductions can be organised.

## APPENDIX 3

### ANTI-AVOIDANCE — TRANSFER OF ASSETS ABROAD

#### Introduction

1. In this appendix we reproduce a copy of a specimen notice issued under Section 59 of the Finance Act, 1974 in connection with the transfer of assets abroad. This legislation enables the Revenue Commissioners to seek information about possible avoidance transactions.

#### Notice under Section 59, Finance Act, 1974. [Specimen]

1. I, \_\_\_\_\_, being an officer duly appointed by the Revenue Commissioners by virtue of the powers vested in them by Section 59 (1) and (2) (b) of the Finance Act 1974 and of any other powers then so enabling in exercise of that appointment hereby require you to furnish within ... days from the date of this notice, at the address given above the information indicated in paragraph 3 below.

#### Interpretation

2. For the purposes of this notice—

- (i) "the company" means
- (ii) reference to things done by you are to things done by you or by the company or by any director of the company or by staff employed by the company; and references to matters within your knowledge are to matters coming within your knowledge or within the knowledge of directors or of staff employed by the company or recorded in any records maintained by you, by the directors or by the company.
- (iii) references to the company "acting in or in connection with" a specified transaction or operation include—
  - (a) the giving of advice to a customer if, but only if, a specified transaction or operation has within your knowledge been carried out as a result of the advice, and
  - (b) the introducing of a customer to the company or to any other person with a view to the carrying out of a specified transaction or operation.
- (iv) "customer" includes any person (whether or not a customer of the company

for other purposes) for whom you have acted in or in connection with any specified transaction or operation; and "Republic of Ireland customer" means any customer with whom you dealt, not being a customer who is known to you to have had at all times during your dealings with him since \_\_\_\_\_ a permanent address outside the Republic of Ireland but no permanent address in the Republic of Ireland;

- (v) "foreign company" means any company incorporated in a specified territory, and any other company which within your knowledge was, or was intended at any time in the future to be, so managed and controlled that it qualified or would qualify for purposes of Republic of Ireland income tax as resident in a specified territory, but does not include a company, or the subsidiary of a company, of which the ordinary shares have at all times since \_\_\_\_\_ (or, if later, since the first anniversary of such a company's incorporation) been quoted on a stock exchange;
- (vi) "foreign partnership" means any partnership constituted under the laws of a specified territory and any other partnership which within your knowledge was, or was intended at any time in the future to be, so managed and controlled that it qualified or would qualify for purposes of Republic of Ireland income tax as resident in a specified territory;
- (vii) "foreign settlement" means any settlement or trust expressed to be governed by the law of a specified territory, and any other settlement or trust which within your knowledge was, or was intended at any time in the future to be, so constituted that income arising under the settlement or trust qualified or would qualify for purposes of Republic of Ireland income tax as the income of a person resident in a specified territory;
- (viii) "specified territory" means any of the following territories:—  
Bahama Islands, Barbados, Bermuda, British Virgin Islands, Cayman Islands, Channel Islands, Isle of Man, Netherlands Antilles, Gibraltar, Republic of Panama;
- (ix) "specified transaction or operation" means a transaction or operation of any kind mentioned in the first column in paragraph 3 below.

#### Information required

3. (i) In any case where you have since \_\_\_\_\_ acted for a Republic of Ireland customer in or in connection with any transaction or operation of a kind mentioned in the first column below you are hereby required to give—
- (a) the name and address of the customer (or, where that is not known, the name and address of any agent who has dealt with you on the customer's behalf),
  - (b) the respective particulars specified in the second column below so far as within your knowledge, and
  - (c) the name and address of any other person to whom you introduced the customer for the purpose of completing or carrying out the transaction or operation.
- (ii) You are also required to state whether you have taken or are taking any, and if so what, part in any, and if so what, transactions of a description specified in the first column below.

<i>Transaction or Operation</i>	<i>Particulars</i>
(1) The formation or management of a foreign company.	The name of the foreign company, the date and place of its incorporation, its registered or other known address.
(2) The formation or management of a foreign partnership.	The name and address of the partnership, the country in which it is constituted, the names and addresses of the partners, the date of any deed or other document regulating the partnership.
(3) The creation, or the execution of the trusts of, a foreign settlement.	The name and address of the settlor, the date and nature of any document or other act constituting or regulating the settlement, the names and addresses of the trustees.
(4) The transfer of assets to any foreign company, foreign partnership or foreign settlement.	Description of the assets transferred, particulars relating to the foreign company, partnership or settlement as required under (1), (2) or (3) above.
(5) The acquisition (by purchase or otherwise) of any interest (or option to acquire capital) of any foreign company, or in or under any foreign partnership or foreign settlement. (In the case of such a company having no share capital the reference to any interest in share capital shall be taken as a reference to any corresponding interest in that company).	Description of the interest acquired, particulars relating to the foreign company, partnership or settlement as required under (1), (2) or (3) above.

Nothing in this Notice shall impose on any bank the obligation to furnish any particulars of any ordinary banking transactions between the bank and a customer carried out in the ordinary course of banking business, unless the bank has acted or is acting on behalf of the customer in connection with the formation or management of any such body corporate as is mentioned in subsection (3) (b) of Section 59 Finance Act, 1974 or in connection with the execution of the trusts of any such settlement as is mentioned in subsection (3) (c) of that Act.

Dated

(Signed)

## APPENDIX 4

### MAINTENANCE AND PRESERVATION OF RECORDS

#### Introduction

1. In this appendix we set out the provisions governing the maintenance and preservation of records for income tax, corporation tax, VAT and PAYE.

#### Income Tax and Corporation Tax

2. Section 6 of the Finance Act, 1968, which is reproduced here, provides that every person carrying on a trade or profession shall keep such records as will enable true returns to be made for the purposes of income tax and retain them for six years. Section 147 of the Corporation Tax Act, 1976 applies the same provision to companies in respect of corporation tax.

#### Section 6, Finance Act, 1968

“(1) In this section ‘records’ includes books of account relating to

- (a) all sums of money received and expended in the course of the carrying on or exercising of a trade, profession or other activity and the matters in respect of which the receipt and expenditure takes place, and
  - (b) all sales and purchases of goods and services where the carrying on or exercising of a trade, profession or other activity involves the purchase or sale of goods or services.
- (2) (a) every person who, on his own behalf or on behalf of any other person, carries on or exercises any trade, profession or other activity the profits or gains of which are chargeable under Schedule D shall keep such records as will enable true returns to be made, for the purposes of income tax of such profits or gains.
- (b) where any such trade, profession or other activity is carried on in partnership, the precedent partner, within the meaning of section 69 of the Income Tax Act, 1967, shall, for the purposes of this section, be deemed to be the person carrying on that trade, profession or other activity.
- (3) Subsection (2) shall
- (a) in the case of a trade, profession or other activity which is commenced after

the passing of this Act, have effect on and from the date of such commencement, and

(b) in any other case, have effect on and from the 1st day of September 1968.

(4) Records kept pursuant to the preceding provisions of this section shall be retained by the person required to keep the records for a period of six years after the completion of the transactions, acts or operations to which they relate:

Provided that this subsection shall not require the retention of records in respect of which the inspector notifies the person who is required to keep them that retention is not required, nor shall it apply to the books and papers of a company which have been disposed of in accordance with section 305 (1) of the Companies Act, 1963.

(5) Any person who contravenes subsection (2) in respect of any records in relation to a return for any year of assessment or contravenes subsection (4) in relation to those records shall be liable to a penalty of £800:

Provided that a penalty shall not be imposed under this subsection if it is proved that no person is chargeable to tax in respect of the said profits or gains for that year of assessment.

(6) Section 508 of the Income Tax Act, 1967, is hereby amended by the insertion in subsection (1) after '240 or 296' of 'or section 6 of the Finance Act, 1968'.

### Value-Added Tax

3. The provisions governing the records to be kept for value-added tax are contained in Section 16 of the Value-Added Tax Act, 1972 and Regulation 9. The provisions are reproduced here.

#### Section 16, Value-Added Tax Act, 1972

"(1) Every taxable person shall, in accordance with regulations, keep full and true records of all transactions which affect or may affect his liability to tax.

#### Retention of invoices by unregistered persons

(2) Every person, other than a taxable person, who supplies goods or services in the course of furtherance of any business shall keep all invoices issued to him in connection with the supply of goods or services to him for the purpose of such business and, in respect of goods imported by him, copies stamped on behalf of the Revenue Commissioners, of the relevant customs entries.

#### Period of retention

(3) Records kept by a person pursuant to this section and any books, invoices, copies, stamped on behalf of the Revenue Commissioners, of customs entries, credit notes, debit notes, receipts, accounts, vouchers, bank statements or other documents whatsoever which relate to the supply of goods or services, or the importation of goods, by the person and are in the power, possession or procurement of the person and, in the case of any such book, invoice, credit note, debit note, receipt, account, voucher or other document which has been issued by the person or another person, any copy thereof which is in the power, possession or procurement of the person shall be retained

in his power, possession or procurement for a period of six years from the date of the latest transaction to which the records or invoices or any of the other documents relate:

Provided that this section shall not require the retention of records or invoices or any of the other documents in respect of which the Revenue Commissioners notify the person concerned that retention is not required, nor shall it apply to the books and papers of a company which have been disposed of in accordance with section 305 (1) of the Companies Act, 1963."

#### Regulation 9 — Statutory Instrument No. 63 of 1979

"(1) Every taxable person shall keep full and true accounts entered up to date of

- (a) in relation to consideration receivable from registered persons, the amount receivable from each such person in respect of each transaction for which an invoice is required to be issued under section 17 of the Act together with a cross-reference to the copy of the relevant invoice,
- (b) in relation to consideration receivable from unregistered persons, a daily total of the consideration receivable from all such persons together with a cross-reference to the relevant counter books, copies of sales dockets, cash register tally rolls or other documents which are in use for the purposes of the business,
- (c) in relation to importations, a description of the goods imported together with particulars of the value thereof as determined in accordance with section 15 of the Act, the amount of the consideration relating to the purchase of the goods if purchased in connection with the importation, the amount of tax, if any, paid on importation and a cross-reference to the invoices and customs documents used in connection with the importation,
- (d) in relation to goods, being goods developed, constructed, assembled, manufactured, produced, extracted, purchased or imported by the taxable person or by another person on his behalf and applied by him (otherwise than by way of disposal to another person) for the purposes of any business carried on by him, a description of the goods in question and the cost excluding tax, to the taxable person of acquiring or producing them except where tax chargeable in relation to the application of the goods would, if it were charged, be wholly deductible under section 12 of the Act,
- (e) in relation to goods, being goods which were appropriated by a taxable person for any purpose other than the purpose of his business or disposed of free of charge, where tax chargeable in relation to the goods, upon their acquisition by the taxable person, if they had been so acquired, or upon their development, construction, assembly, manufacture, production, extraction, importation or application in accordance with paragraph (d), as the case may be, was wholly or partly deductible under section 12 of the Act, a description of the goods in question and the cost, excluding tax, to the taxable person, of acquiring or producing them,
- (f) in relation to services regarded in accordance with section 5 (3) of the Act as supplied by a person in the course of furtherance of business, a description of the services in question together with particulars of the cost, excluding tax, to the taxable person of supplying the services and of the consideration, if any, receivable by him in respect of the supply,
- (g) in relation to services referred to in section 5 (6) (c) (ii) of the Act in respect of which a person is liable to pay tax in accordance with section 8 (2) of the Act,

a description of the services in question together with particulars of the cost to the person of acquiring the service,

- (h) in the case of services deemed, in accordance with clause (i) or (ii) of subparagraph 5 (6) (c) of the Act to be supplied at places outside the State, the name and address of the person to whom the service is supplied, the nature of the service and the amount of the consideration receivable in respect of the supply,
- (i) in relation to discounts allowed or price reductions made to a registered person subsequent to the issue of an invoice to such person, the amount credited to such person and, except in a case in which section 17 (9) (a) of the Act applies, a cross-reference to the corresponding credit note,
- (j) in relation to discounts allowed or price reductions made to unregistered persons, a daily total of the amount so allowed together with a cross-reference to the goods returned book, cash book or other record used in connection with the matter,
- (k) in relation to bad debts written off, particulars of the name and address of the debtor, the nature of the goods or services to which the debt relates and the date or dates upon which the debt was incurred,
- (l) in relation to goods and services supplied to the taxable person by another taxable person, the amount of the consideration, the corresponding tax invoiced by the other taxable person and a cross-reference to the corresponding invoice,
- (m) in relation to goods and services supplied by unregistered persons, other than goods and services in respect of which flat-rate farmers are required, in accordance with section 12A (1) of the Act to issue invoices, a daily total of the consideration payable to such persons and a cross-reference to the purchases book, cash book, purchases dockets or other records which are in use in connection with the business,
- (n) in relation to goods and services supplied by flat-rate farmers but in respect of which such persons are required, in accordance with section 12A (1) of the Act, to issue invoices, the amount of the consideration (exclusive of the flat-rate addition) and of the flat-rate addition invoiced by each such person and a cross-reference to the corresponding invoice,
- (o) in relation to discounts or price reductions received from registered persons, subsequent to the receipt of invoices from such persons, except in a case in which section 17 (9) (a) of the Act applies, the amount of the discount or price reduction and the corresponding tax received from each such person and a cross-reference to the corresponding credit note,
- (p) in relation to discounts or price reductions in relation to goods and services referred to in subparagraph (n), the amount of the discount or price reduction (exclusive of the flat-rate addition) and of the flat-rate addition and a cross-reference to the invoice issued in connection with the goods and services in question,
- (q) in relation to discounts or price reductions (received other than those referred to in subparagraphs (o) and (p)), a daily total of the amounts so received and a cross-reference to the cash book or other record used in connection with such matters,
- (r) in relation to dances
  - (i) the date upon which each dance was held and the address of the place at which it was held,

- (ii) the charge for admission to each dance,
  - (iii) the number of persons admitted to each dance,
  - (iv) the total amount of money received or receivable from the persons admitted to each dance in respect of admission, and
  - (v) where goods or services are supplied in connection with a dance and payment of the consideration therefor is a condition of admission to the dance, the amount of such consideration in respect of each dance,
- (s) in respect of supplies of goods specified in paragraph (i) of the Second Schedule to the Act, the name and address of the person to whom the goods are supplied, a description of the goods supplied, the amount of the consideration, a cross-reference to the copy of the relevant invoice and a cross-reference to the relevant Customs and transport documents, and
  - (t) in the case of the supply of services in circumstances that, by virtue of any of the provisions of section 5 of the Act, are deemed to be supplied outside the State, the name and address of the person to whom the services are supplied, the amount of the consideration and a cross-reference to the copy of the relevant invoice or other document.

(2) The accounts kept in accordance with paragraph (1) shall set out separately, the consideration, discounts, price reductions, bad debts and values at importation under separate headings in relation to

- (a) exempted activities,
- (b) goods and services chargeable at each rate of tax, including the zero rate, and
- (c) goods and services a percentage only of the consideration for the supply of which is chargeable to tax.

(3) (a) In relation to a person for the time being authorised in accordance with section 14 (1) (a) of the Act to determine the amount of tax which becomes due by him by reference to the amount of moneys which he receives, references in this Regulation to consideration in respect of the supply of goods or services shall be construed as references to the moneys received in respect of such supply, whether made before, on or after the specified day.

(b) In relation to a person for the time being authorised, in accordance with section 14 (1) (b) of the Act, to determine the amount of tax referable to taxable services which becomes due by him by reference to the amount of moneys which he receives in respect of such supply, references in this Regulation to consideration in respect of the supply of services shall be construed as references to the moneys received in respect of such supply, whether made before, on or after the specified day.

(4) Where the Revenue Commissioners are satisfied that the accounts of a taxable person are kept in such a form as to enable his liability to tax to be computed accurately and verified by them, they may, by notice in writing given to the taxable person, dispense him from keeping accounts in the form prescribed by paragraphs (1) and (2), and any such dispensation may be cancelled by them by notice in writing given to the taxable person."

## PAYE

4. The provisions governing the records to be kept for PAYE are in Regulation 37 of the Income Tax (Employments) Regulations, 1960 (Statutory Instrument No. 28 of 1960). This regulation is reproduced here.

"(1) Upon request made to him at any premises of an employer by an authorised officer, any person, being the employer or a person employed by the employer at the premises, shall produce to the authorised officer for inspection all such wages sheets, certificates of tax-free allowances, tax deduction cards and other documents and records whatsoever relating to the calculation or payment of the emoluments of employees of the employer or the deduction of tax therefrom as may be in such person's powers, possession or procurement.

(2) Where in pursuance of this Regulation an authorised officer requests production of any documents or records, he shall, on request, show his authorisation for the purposes of this Regulation to the person concerned.

(3) In this Regulation 'authorised officer' means an officer of the Revenue Commissioners authorised by them in writing for the purposes of this Regulation.

4. The documents and records specified in paragraph (1) of this Regulation, other than certificates of tax-free allowances and the temporary tax deduction forms, and emergency cards, and the documents corresponding to such forms and cards, referred to in Regulation 35, shall be retained by the employer for a period of six years after the end of the year to which they refer, or for such shorter period as the Revenue Commissioners may authorise by notice in writing to the employer."

## APPENDIX 5

### TAX OFFENCES AND PENALTIES

1. In this appendix we set out the full range of tax offences in relation to income tax, capital gains tax, corporation tax and value-added tax, together with the statutory penalties.

TABLE 5.1 — Income Tax and Capital Gains Tax Penalties

TABLE 5.2 — Corporation Tax Penalties

TABLE 5.3 — Value-Added Tax Penalties

TABLE 5.4 — Criminal Penalties

TABLE 5.1

#### Income Tax and Capital Gains Tax Penalties

(Penalty provisions of the income tax acts are applied where appropriate for capital gains tax by Schedule 4 of the Capital Gains Tax Act 1975)

Section of the Taxes Acts	Offence	Present Penalty (Finance Act, 1982)
128 Income Tax Act (ITA), 1967	Failure to remit PAYE tax or documents.	£800
173 ITA '67	Failure to supply returns of fees or commissions	£800
238 ITA '67	False statement in respect of retirement annuities.	£500
240 ITA '67	False statement in respect of purchased life annuities.	£500
296 ITA '67	False statement in respect of annual allowances (capital expenditure).	£500
339 ITA '67	False claim, for example, charitable exemption.	£100
426 ITA '67	Refusal to attend or answer at an appeal meeting.	£500
500 (1) ITA '67	Person failing to make return.	£500

Section of the Taxes Acts	Offence	Present Penalty (Finance Act, 1982)
458 ITA '67	Failure to annex proper statements to warrants for payment of interest not regarded as a distribution under CTA 1976.	£10 each offence. £100 max aggregate.
500 (2) ITA '67	Person failing to make return after end of year of assessment.	£800
501 (1) ITA '67	Person making incorrect return (Sch. 15 Col. 1).	£100 plus amount evaded, if negligence. £100 plus twice amount evaded if fraud.
501 (2) ITA '67	Person making incorrect return (Sch. 15 Col. 2+3)	£100 if negligence. £250 if fraud.
503 (1) (a) (i) ITA '67	Body of persons failing to make return after end of year of assessment.	£1,000 plus £50 per day after judgement.
503 (1) (a) (ii) ITA '67	Body of persons failing to make return.	£500 plus £50 per day after judgement.
503 (1) (b) (i) ITA '67	Secretary of body of persons failing to make return after end of year of assessment.	£200
503 (1) (b) (ii) ITA '67	Secretary of body of persons failing to make return.	£100
503 (2) (a) (i) ITA '67	Body of persons negligently or fraudulently making incorrect return (Sch. 15 Col. 1).	£500 plus amount evaded if negligence. £1,000 plus twice amount evaded if fraud.
503 (2) (a) (ii) ITA '67	Secretary of body of persons negligently or fraudulently making incorrect return (Sch. 15 Col. 1).	£100 if negligence. £200 if fraud.
503 (2) (b) (i) ITA '67	Body of persons negligently or fraudulently making incorrect return (Sch. 15 Col 2+3).	£500 if negligence. £1,000 if fraud.
503 (2) (b) (ii) ITA '67	Secretary of body of persons negligently or fraudulently making incorrect return (Sch. 15 Col. 2+3)	£100 if negligence. £200 if fraud.
505 ITA '67	Person assisting/inducing return etc. known to be incorrect.	£500
515 ITA '67	Person obstructing etc. Revenue Officer.	£100
520 ITA '67	Person refusing to allow deduction of tax.	£50
539 (1) ITA '67	Failure to deliver books or papers relating to tax after notice by Revenue Commissioners.	£50

Section of the Taxes Acts	Offence	Present Penalty (Finance Act, 1982)
6 (5) Finance Act (FA), 1968	Failure to keep records (Sch. D) and/or retain them for 6 years.	£800
7 (10) (a) FA '70	Misuse of sub-contractor's certificate.	£500 (and/or 6 months' imprisonment)
7 (10) (b) FA '70	Person assisting misuse of sub-contractor's certificate	£500 (and/or 6 months' imprisonment)
7 (10) (c) FA '70	Failure to keep or produce records (construction industry).	£500
34 (4) FA '76	Obstructing an authorised officer during visit to place of business.	£800
31 (5) FA '79	Failure to comply with notice requiring information about business transactions with a taxpayer.	£800
19 (5) FA '82	Obstruction of authorised person — significant building relief.	£500
20 FA '83	Failure to make a return of property.	£500
21 FA '83	Failure to make a return of nominee holders of securities.	£500
22 FA '83	Obligation to show tax reference number on receipts.	£500

**TABLE 5.2**  
**Corporation Tax Penalties**

Section of the Taxes Acts	Offence	Present Penalty (Finance Act 1982)
5 (2) Corporation Tax Act (CTA) 1976	Failure to annex explanation of tax credit to interest and dividend warrants.	£10 each offence (£100 maximum)
63 (2) CTA '76	Failure to produce documents and records (exports sales relief).	£100
64 (9) CTA '76	Failure to furnish information about distributions (exports sales relief).	£800
141 (2) CTA '76	Failure by a company to notify commencement of business.	Company £500 plus £50 per day after judgement. Secretary £100.
142 (2) CTA '76	Failure to give notice of liability to corporation tax.	Company £500 plus £50 per day after judgement. Secretary £100.
143 (8) (a) (i) CTA '76	Failure by company to comply with notice requiring delivery of a return.	Company £500 plus £50 per day after judgement.

Section of the Taxes Acts	Offence	Present Penalty (Finance Act, 1982)
143 (8) (a) (ii) CTA '76	Failure by secretary of company to comply with notice requesting delivery of a return.	Secretary £100
143 (8) (b) CTA '76	Failure continuing for more than 1 year to comply with notice requiring delivery of a return.	Company £1,000. Secretary £200.
143 (9) CTA '76	Company fraudulently or negligently making incorrect return or accounts.  Secretary of company fraudulently or negligently making incorrect return or accounts.	Company: £500 plus amount evaded if negligence. £1,000 plus twice amount evaded if fraud. Secretary: £100 if negligence. £200 if fraud
149 (1) CTA '76	Failure by individual to comply with notice requiring information.	£100 plus £10 per day after judgement
149 (2) CTA '76	Individual fraudulently or negligently furnishing incorrect information.	£100 if negligence. £200 if fraud.
149 (3) (a) CTA '76	Failure by company to comply with notice requiring information.	Company: £500 plus £50 per day after judgement.
149 (3) (b) CTA '76	Failure by secretary of company to comply with notice requiring information.	Secretary £100
149 (4) (a) CTA '76	Company fraudulently or negligently furnishing incorrect information.	Company: £500 if negligence £1,000 if fraud.
149 (4) (b) CTA '76	Secretary of company fraudulently or negligently furnishing incorrect information.	Secretary: £100 if negligence. £200 if fraud.
45 (8) Finance Act 1980	Failure to furnish information about distributions (manufacturing companies).	£800

**TABLE 5.3**  
**Value-added Tax Penalties**

Section of Value-Added Tax Act, 1972	Offence	Penalty
26 (1)	Failure to register for tax	£800
26 (1)	Failure to supply information regarding holding of dances.	£800
26 (1)	Failure to issue invoice by flat-rate farmer.	£800
26 (1)	Failure to keep proper records and/or retain them for six years.	£800

Section of the Taxes Acts	Offence	Present Penalty (Finance Act, 1982)
26 (1)	Non-compliance with obligations to issue invoices, credit notes etc.	£800
26 (1)	Non-compliance with obligation to produce records to authorised officer.	£800
26 (1)	Non-compliance with obligation to furnish two-monthly returns and remit tax payable.	£800
26 (1)	Non-compliance with any VAT regulation where a provision therein is related to an obligation imposed by the VAT Acts and breach of which is an offence mentioned above.	£800
26 (2)	Non-registered person issuing invoice which states an amount of tax.	£500
26 (2A)	Person improperly issuing invoice which states an amount of flat-rate addition.	£500
26 (3)	Secretary's liability where any of the offences mentioned above are committed by a body of persons.	£500
26 (3A)	Obstruction of an authorised officer.	£800
27 (1)	Fraudulent or negligent use of incorrect return or invoice.	£100 plus amount evaded, if negligence; £100 plus twice amount evaded, if fraud.
27 (2)	Fraudulent or negligent use of incorrect return or invoice by body of persons.	£500 plus amount evaded, if negligence; £1,000 plus twice amount evaded, if fraud.
27 (2)	Secretary's liability where body of persons makes use of incorrect return or invoice, fraudulently or negligently.	£100 if negligence. £200 if fraud.
27 (4)	Misrepresentation to procure improper tax-free importation of goods.	£500
27 (5)	Fraudulent or negligent issue of invoice or credit note.	£100 plus amount of liability in respect of issue of invoice or credit note, if negligence; £100 plus twice the amount of the liability, if fraud.
28	Assisting in or including the making or delivery of incorrect return, invoice, etc.	£500

**TABLE 5.4**

**Criminal Penalties**

**(Income Tax, Capital Gains Tax, Corporation Tax and Value-Added Tax)**

Section of the Taxes Acts	Offence	Penalty
Section 516 ITA 1967.	Persons knowingly making or assisting another person to make a false statement with reference to tax to obtain an allowance	On summary conviction — six months' imprisonment
Section 94 FA 1983.	<p>(i) Refusal to comply with statutory provisions designed to enable tax liabilities to be determined, for example, keeping proper business records and producing them when asked and furnishing returns and other documents when obliged to do so.</p> <p>(ii) Deliberate furnishing of incorrect information in returns and other documents or assisting another person to furnish such information.</p> <p>(iii) Failure to make PAYE and VAT remittances when due.</p> <p>(iv) Obstruction of persons exercising statutory powers for tax purposes.</p>	<p>On summary conviction £1,000 or twelve months' imprisonment, or both.</p> <p>On conviction on indictment — £10,000 or five years' imprisonment, or both.</p>

**APPENDIX 6**

**COLLECTION PROCEDURES**

1. In this appendix we describe the collection procedures for the main taxes.

**Income Tax (non-PAYE)**

2. Assessments for income tax are raised mainly during the months May to July preceding the due date. As the income tax assessments are virtually all estimated, there are appeals in the vast majority of cases.

3. When an assessment is appealed, the appellant is expected to specify the amount he considers will be payable on determination of the appeal. Where this is done, only this amount is collectable pending the outcome of the appeal and collection of the balance is suspended. In order to avoid interest, the amount specified must be at least 85 per cent of the liability eventually found to be due and it must be paid within two months of the due date. Any balance found to be payable on settlement of the appeal is payable within two months of agreement; failing timely payment, interest charges arise. Interest will not arise in cases where the full amount of the original assessment is paid on time even if this amount is not 85 per cent (80 per cent for Corporation Tax) of the final liability.

4. Where an appeal is made and no amount is specified, the tax charge is merely marked as appealed on the record and remains open for collection.

5. Where a nil amount is specified on appeal, collection of the entire charge is suspended pending disposal of the appeal.

6. The Collector General's demand follows in September/October and the surge in receipts in October/December reflects, in the main, payment of specified amounts.

7. In addition to the main assessment referred to in paragraph 2, there is a continuing assessment process during the year. Such assessments are known as additional assessments and most refer to tax due in respect of years earlier than the current year. This is tax which arises on the basis of

new information becoming available to the inspector. Additional assessments are made in about 50,000 cases per annum.

8. The raising of additional assessments and the settlement of appeals and completion of enquiries give rise to a continuous flow of income tax for collection during the year, notwithstanding that the bulk of each year's income tax is due on 1 October.

9. Where, despite the issue of demands, tax remains unpaid, the case is sent to one of the enforcement agencies for collection. At the stage where the certificate of the amount of tax for enforcement is being produced by the computer, the interest due at that point is calculated and included on the certificate for collection by the enforcement agency.

### **Corporation Tax and Capital Gains Tax**

10. In the case of Corporation Tax and Capital Gains Tax there is no standardised due date corresponding to 1 October for income tax. In Corporation Tax the due date is dependent on the financial year of the company. In Capital Gains Tax the tax is due three months after the end of the year of assessment, i.e. on 6 July or two months after the date of assessment if later. The collection system is similar to that applying to income tax.

11. The number of assessments made annually for corporation tax and capital gains tax is about 45,000 and 6,500 respectively. The number of demands issued annually is about 120,000 and 10,000 respectively.

12. Interest provisions apply where tax is paid more than two months after the due date or one month in respect of corporation tax assessments raised on or after 17 July, 1982. In the case of appealed Corporation Tax assessments where the specified amount is adequate (80 per cent) and is paid on time (i.e. within one month), the due date for any balance found to be payable on settlement of the appeal is advanced to the date of agreement of the liability and the taxpayer has a further two months in which to pay the balance without incurring an interest penalty. Where, however, the specified amount was paid late, was inadequate or was not paid at all, no advancement of the due date is provided in respect of the balance payable on settlement of the appeal.

### **Value Added Tax**

13. The VAT return (Form VAT 3) is issued automatically to registered traders every two months. The trader is required to complete the form showing trading details and the amount of tax payable or repayable and to

forward it to the Collector General with a remittance of any tax payable. A comparison of collection of VAT periods is in Annex 1.

14. If a trader fails to submit a return, an estimate of his liability is raised and a notice is issued to the trader. This is followed, if necessary, by a demand and enforcement by the sheriff or county registrar or through the courts. Another sanction against a trader for failure to submit a return is the taking of penalty proceedings. If, following an examination of a trader's accounts, the inspector of taxes considers that the total tax liability has not been paid, he may raise an estimate.

15. Approximately 65 per cent of internal VAT comes from some 1,200 cases. These cases are specially monitored outside the normal collection system. Forty four of them are extremely large (remitting 34 per cent of total collection) and their progress is under direct personal supervision. Some returns, showing liabilities, are received with partial payment or without payment and these generate underpayment charges. Prior to a recent redesign of the computerised VAT collection system, such underpayments had to be pursued manually on a very selective basis. The redesigned system allows automatic pursuit of these underpayments by way of computer-produced demand notices. The bulk automatic issue of demands for underpayments commenced towards the end of May, 1984.

### **PAYE/PRSI**

16. Persons and companies who have liable employees are obliged to register as employers for PAYE and PRSI purposes. There are currently some 100,000 live employers on the PAYE/PRSI register.

17. There are two major obligations on employers. The first of these is to pay each month the tax and contributions due in respect of employees and the second is to make an annual detailed account at the end of the tax year of their operation of PAYE and PRSI in the course of the year.

18. Employers are obliged to remit to the Collector General, within nine days of the end of each income tax month, the tax and pay-related contributions appropriate to employees' earnings in the month. In the event that no amount is due, the employer is obliged to make a declaration to this effect. In cases where there is a very small monthly liability, the employer may be permitted to remit the contributions on a less frequent basis. To enable employers to make the monthly payments, payment/declaration forms (P.30s) are issued before the end of the income tax month.

19. When amounts of tax/contributions due for any month are received after the due date, simple interest at 1.25 per cent per month or part of a

month is payable in accordance with Section 129 of the Income Tax Act, 1967, as amended.

20. Where the employer fails to make a payment or to furnish a declaration that no amount is due, an estimate of the tax and contributions due for the month may be made under Section 7 of the Finance Act, 1968 on the basis of the payments and declared liabilities already on record and a formal notice of estimation is issued. If the default continues, a demand for payment of the estimated liability, plus interest at the rate of 1.25 per cent per month, may then be issued after fourteen days. If there is still no response from the employer, the estimated amounts plus interest may then be referred for enforcement by the issue of a certificate to the sheriff/county registrar or by legal action through the courts.

21. The elapsed time from the due date of payment each month to the date of referral for enforcement varies in relation to the amount of the expected monthly payment. Approximately 75 per cent of the yield of PAYE/PRSI is paid by some nine hundred employers. Defaulters in this category, who are few in number, are pursued separately in respect of each month and usually reach enforcement within two months of the due date. The remaining defaulters are divided into further categories for collection purposes by reference to the size of the normal monthly payment. Defaulters in these further categories are pursued at appropriately longer intervals.

22. Within twenty five days of the end of the tax year, employers are obliged to submit an annual return to the Collector General on Form P35, declaring the total liability for the year and providing details of the pay, tax, contributions and social insurance data relating to each employee. P35 returns are used to identify those employers who have either underpaid or overpaid their liabilities for the year and to highlight instances of under-declaration in making monthly payments. In recent years, there have been on average some 17,000 underpayment cases and some 10,000 overpayment cases each year. The PRSI particulars on the P35 returns are supplied to the Department of Social Welfare where they are used to determine entitlement to social welfare benefits. Employers who fail to lodge the end-of-year returns are issued with reminders and warnings of court proceedings for the imposition of penalties. Suitable cases are selected for proceedings, particular attention being paid to the larger employers. In addition, the Revenue Commissioners mount a press and TV advertising campaign emphasising the importance of the P35 and drawing attention to the penalties which may be invoked against non-compliance.

23. The Revenue Commissioners are empowered under Section 8 of the Finance Act, 1968 to make estimates on an annual basis where there is reason to believe that liability for a year or a number of years has not been

met in full. Such estimates are raised in approximately 15,000 cases each year. Discrepancies between an employer's PAYE/PRSI returns and his business accounts can result in the raising of such estimates by inspectors of taxes. There is provision for appeal against these annual estimates and where this occurs, collection of the balance due is suspended until the liability is finalised. Payments made on foot of annual estimates or of underpayments disclosed on P35s attract interest at 1.25 per cent per month from the last day of the tax year in question. The procedures for collection of underpayments disclosed on P35s and of balances due on foot of annual estimates are similar to those described for monthly payments and the same considerations in relation to the amounts of money and number of cases involved dictate the speed with which the charges reach the enforcement stage.

## ANNEX 1

### COMPARISON OF THE HISTORY OF COLLECTION OF VAT PERIODS, MARCH/APRIL, 1982, MARCH/APRIL, 1983 AND MARCH/APRIL, 1984

**TABLE 6.1**

TAXABLE PERIOD MARCH/APRIL, 1982: Total number of VAT3s issued for period = 78,648

	Returns received or no longer outstanding	Paid £m	Returns received as % of issued	Amount paid as % of total paid at 31 May of following year
Position at 31 May, 1982	19,772	102.8	25	54
Position at 30 June, 1982	33,008	150.5	42	79
Position at 31 July, 1982	39,093	164.5	50	87
Position at 31 August, 1982	43,819	171.2	56	90
Position at 31 December, 1982	52,277	184.0	67	97
Position at 31 May, 1983	57,535	189.4	73	

**TABLE 6.2**

TAXABLE PERIOD MARCH/APRIL, 1983: Total number of VAT3s issued for period = 82,000

	Returns received or no longer outstanding	Paid £m	Returns received as % of issued	Amount paid as % of total paid at 31 May of following year
Position at 31 May, 1983	19,866	78.4	24	57
Position at 30 June, 1983	33,384	107.4	41	77
Position at 31 July, 1983	39,220	118.0	48	85
Position at 31 August, 1983	43,986	123.9	54	89
Position at 31 December, 1983	52,522	133.3	64	96
Position at 31 May, 1984	59,679	138.6	73	

**TABLE 6.3**

TAXABLE PERIOD MARCH/APRIL, 1984: Total number of VAT3s issued for period = 89,000

	Returns received or no longer outstanding	Paid £m	Returns received as % of issued	Amount paid as % of total paid at 31 May of following year
Position at 31 May, 1984	24,018	98.3	27	61
Position at 30 June, 1984	37,347	130.2	42	81
Position at 31 July, 1984	45,051	142.1	51	88
Position at 31 August, 1984	49,862	147.8	56	92
Position at 31 December, 1984	59,672	155.9	67	97
Position at 31 May, 1985	66,475	161.3	75	

## APPENDIX 7

### SOLICITOR ENFORCEMENT

1. The principal method of enforcing the collection of unpaid taxes is through the issue of certificates to sheriffs and county registrars. However, where action by way of these certificates has been unsuccessful, cases are processed through the courts. Examples of such cases are where the goods in possession of the defaulter are perishable, sold under licence or are the property of a third party. In still other cases, where the amount of the arrears is clearly far greater than the realisable value of the assets of a defaulter available to be seized, enforcement collection is by way of court proceedings, as the threat of publication of the judgement in such cases often secures payment without having to complete the legal process.

2. The Revenue Commissioners have available to them, for the recovery of the various taxes through the courts, the services of the Revenue Solicitor and of two external solicitors (one in Dublin and one in Cork) who are contracted on a fee and commission basis.

3. All cases where the debt exceeds £15,000 are referred to the Revenue Solicitor for High Court action. The external solicitors deal with cases appropriate to the Circuit Court (where the debt exceeds £2,500 but does not exceed £15,000) and the District Court (where the debt does not exceed £2,500). The solicitor based in Cork takes cases in Cork, Kerry, Limerick, Tipperary, Waterford and Wexford and the Dublin solicitor covers the rest of the country. In the second half of 1985, a limited number of High Court cases where the debt exceeds £15,000 but does not exceed £100,000 will be referred to the two external solicitors who already deal with District and Circuit Court cases on behalf of the Revenue Commissioners.

4. Before a case is reported, a final warning that legal action is imminent is issued to the defaulter. If there is no response, details of the debt and the accrued interest are notified to the solicitor.

5. Proceedings are started by the issue of a Summary Summons in High Court cases, by a Civil Bill in Circuit Court cases and by a Civil Process in District Court cases. The next stage in the process is an application for judgement. Where there is a defence, the case is heard in court, otherwise the judgement is given out of court. The application for judgement must

be supported by affidavits furnished by the Collector General and inspector of taxes.

6. The sequence of events where there is continued failure to pay is, firstly, formal notice of the issue of the judgement, then registration and finally the issue of an execution order to the sheriff or county registrar to collect the amount due or to seize goods to its value.

7. Where the sheriff or county registrar is unable to secure satisfaction of the debt a *nulla bona* return is filed. The Revenue Commissioners may then register a judgement mortgage. This is feasible only if the defaulter owns property. Alternatively, they may return to the court where the available options are

- (i) petitions to bankrupt in the case of individuals.
- (ii) petitions to wind them up in the case of companies.
- (iii) enforcement of Court Order Acts proceedings which involves examination by the court of the defaulter's means, the making of an instalment order and, eventually, if the instalments are not paid, committal to prison. The experience of the Revenue Commissioners is that the results to be expected from these proceedings are not worth the time and expense they entail and this course is not generally availed of.

8. In 1982, a total of 3,215 cases was referred to the solicitors. The total in 1983 was 7,209 comprised of 62 per cent for PAYE/PRSI and VAT cases and 38 per cent income tax and corporation tax. In 1983, 250 judgements were registered in both the Circuit and High Courts. The total amount included was £9.7 million. There were some further judgements obtained in the District Court but details are not readily available. A total of 949 cases in which the arrears totalled £12.7 million was closed in that year either by payment at a stage in the proceedings prior to judgement or by other action such as withdrawal to allow investigation of returns and accounts lodged. The total payment received in 1983 as a result of court proceedings was £3.037 million.

#### Costs of Solicitor Enforcement

9. The costs of collection through court proceedings are considerably higher than through summary distraint as Table 7.1 indicates.

TABLE 7.1

Cost of Enforcement by County Registrars/Sheriffs Compared with Solicitor Enforcement, 1983 and 1984

	Sheriff/Registrar		Solicitor	
	1983	1984	1983	1984
Total Cost (£m)	0.58	0.57	0.65	0.83
Total Collected (£m)	30.60	32.10	3.04	6.09
Cost as % of total collected	2%	1.79%	21.2%	13.6%

Source: The Revenue Commissioners

10. Proceedings through the courts frequently have to be terminated when the defaulting company goes into liquidation as a direct result of the Revenue Commissioners' action. This distorts to some degree the ratio between costs and results expressed in terms of money collected. Also, the initial stages of proceedings, i.e. issue of summons, may of itself provoke a response resulting in the case being taken back for negotiation of clearance of arrears in the Collector General's Office. Any money paid on foot of such negotiation is not treated as having been collected by way of court proceedings.

## APPENDIX 8

### COUNTY REGISTRARS AND SHERIFFS

#### County Registrars

1. Every county has a county registrar responsible for the administrative functions of a registrar in the Circuit Court on both its civil and criminal sides. County registrars also act as under-sheriffs with powers to enforce an execution order issued by a court in a civil matter directing or authorising the execution of an order of the court by seizure and sale of a person's property. The certificates issued by the Collector General are enforceable in the same manner as an execution order issued by a court.

2. The county registrars are officers of the Department of Justice and as such they are paid a salary for their services. Any fees collected in respect of the enforcement of execution orders or other certificates are paid to the Department of Justice.

#### Sheriffs

3. The functions of an under-sheriff are exercised by county registrars everywhere except in Dublin County and Dublin Borough and Cork County and Cork Borough where they are performed by sheriffs appointed by the government. The sheriff is answerable only to the courts.

4. The county and borough sheriffs are paid a small retainer (£600/£400 per annum) and make up their income by way of a levy for fees and expenses in connection with the enforcement of execution orders and other certificates. The scale of fees and expenses to be charged by and paid to the sheriffs is set by the Minister for Justice with the consent of the Minister for Finance under the Sheriff's Fees Order, 1965. The fee for carrying out an execution order is 5 per cent of the first £100 collected and 2½ per cent of the portion exceeding £100.

#### Number of Certificates for Enforcement

5. Under Section 485 of the Income Tax Act, 1967, arrears of tax are collectable by the same process as court orders. County registrars/sheriffs estimate that tax certificates now account for 50-70 per cent of all orders

issued to them.<sup>1</sup> Table 8.1 shows the number of certificates referred to sheriffs and county registrars during the period 1980 to 1984. In 1980 and 1981, the certificates issued to county registrars accounted for more than 60 per cent of the total. This proportion declined to 48 per cent in 1982. While the proportion rose again in 1983, enforcement activity by county registrars accounted for only 27 per cent of the total number of certificates issued in 1984. According to the Revenue Commissioners, the decrease in 1982 was due to their restraint in issuing certificates to county registrars because of the burden of work on county registrars arising from general elections held in February and November of that year. The issue of certificates is also restricted in some years in order to limit enforcement to cases where agreement on the amount due has been reached between the inspector and the taxpayer. It is clear, however, that more cases are being referred to sheriffs than to county registrars. In order to facilitate county registrars dealing with certificates on hands, issues to them were restricted during 1984 to cases where the amount outstanding was substantial.

TABLE 8.1

Number and Proportion of Certificates Issued by the Collector General in Respect of the Main Taxes to Sheriffs and County Registrars, 1980 to 1984.

Year	Sheriff		Co. Registrar		Total
	Number of Certificates	% of Total	Number of Certificates	% of Total	
1980	17,420	39.8	26,345	60.2	43,765
1981	21,447	39.6	32,738	60.4	54,185
1982	23,823	51.3	22,628	48.7	46,451
1983	37,119	38.4	59,571	61.6	96,690
1984	42,881	73.0	15,875	27.0	58,756

Source: The Revenue Commissioners

Note (1) The taxes covered by the certificates include income tax, corporation tax, PAYE and PRSI and VAT.

6. The sheriffs are also marginally more effective in collecting revenue than are county registrars. Table 8.2 shows the actual amounts collected by the sheriffs and the registrars. The sheriffs collect more tax in absolute terms than the registrars. Tax collected by sheriffs as a proportion of the face value of certificates is also higher. It is interesting to note that the proportion of revenue collected to the face value of certificates is declining for both county registrars and sheriffs. This may be due to an increase in over-estimation of tax due or to a decline in the effectiveness of enforcement. However, great care must be exercised in drawing conclusions based on the face values of certificates which represent estimated liabilities.

<sup>1</sup>Stubbs Gazette Vol XCV No. 15, April, 1985.

TABLE 8.2  
Revenue Collected by County Registrars/Sheriffs as a Proportion of the Face Value of Certificates, 1980 to 1984.

Year	Sheriff		Co. Registrar		Total		
	(1) Face Value of Certificates £m	(2) Revenue Collected £m	(1) Face Value of Certificates £m	(2) Revenue Collected £m	(2) as % of (1)	Face Value of Certificates	Revenue Collected
1980	76.6	12.5	81.8	8.5	10.4	158.4	21.0
1981	99.0	12.8	81.7	9.1	11.1	180.7	21.9
1982	155.1	16.3	114.7	8.7	7.6	269.8	25.0
1983	298.2	20.0	302.0	0.7	3.5	600.2	30.7
1984	312.7	21.4	217.7	0.7	4.9	530.4	32.1

Source: The Revenue Commissioners.

## APPENDIX 9

### VAT ON IMPORTS

#### Introduction

1. As a general rule, imported goods are liable to VAT at the same rate as applies to the sale within the state of similar goods. Accordingly, goods which are liable to VAT on sale within the state (most goods) are liable to VAT at importation and goods which are not liable to VAT on sale within the state (food, books, horses, greyhounds and certain ships and aircraft) are not liable to VAT at importation.

#### Goods not Chargeable to VAT at Importation

2. Goods imported in some circumstances are not chargeable to VAT at importation. These include the following:

- (i) certain goods imported temporarily, such as motor vehicles, caravans, commercial trailers, commercial travellers' samples, goods imported for use in competitions, exhibitions, etc., professional equipment imported by non-residents, aircraft, yachts and boats and goods imported for testing,
- (ii) goods imported under transit arrangements,
- (iii) goods entered for trans-shipment,
- (iv) goods imported into Shannon customs-free airport,
- (v) goods imported by parcel post the value of which is £200 or less. This relief is restricted to imports by VAT-registered persons for business purposes,
- (vi) goods imported in circumstances which entitle them to admission without payment of customs duty, for example, used personal and household effects and portable wedding presents imported on transfer of residence, goods imported within travellers' personal luggage allowance etc, and
- (vii) raw materials and components imported by manufacturers who export at least 75 per cent of goods manufactured by them and incorporating those materials and components.

### **Payment Date**

3. Unless an importer is approved for and is participating in the deferred payment scheme, in which case the tax is payable on the 15th day of the month following the month of importation, VAT (and duty, if any) is payable before imported goods are released by the customs.

### **Value for Tax**

4. The value of imported goods for the purpose of assessment of tax is the value for customs purposes, determined on a delivery to state basis, together with any taxes, duties and other charges levied either outside or, by reason of importation, inside the state (excluding VAT) on the goods and not included in the determination.

5. The value of goods which are imported temporarily (for example, on hire, loan, for processing, etc.) is the same value as applies to goods which are permanently imported.

6. Where data such as invoices used to determine the value of imported goods are expressed in foreign currency, the rate of exchange to be used is the selling rate in this country of the currency in question at the material time for valuation (usually the date of presentation of the relevant customs entry).

### **Deferred Payment**

7. Provision exists under the deferred payment scheme for deferment of payment of VAT to the 15th day of the month following the month in which VAT becomes due. The essential feature of the scheme is that collectors of customs and excise, with the authority of the debtor, initiate payment by the issue of a direct debit voucher drawn on the debtor's bank.

8. Importers and agents wishing to participate in the deferred payment scheme must make prior application to the appropriate collector of customs and excise. Where it is intended to claim deferment in more than one collection, a separate application must be made to each collector concerned (Cork, Dublin, Galway, Limerick, Waterford).

9. Importers and agents who are not approved for deferred payment or who do not fulfil all the conditions of the scheme will be required to pay VAT before imported goods will be released.

10. A valuation declaration form is required if the customs value of the goods, *prima facie*, exceeds £1,000 and the goods are imported by an

unregistered trader. This declaration must be completed by the importer. VAT-registered persons will not normally be required to produce a valuation declaration.

### **Credit in VAT Returns for VAT on Imported Goods**

11. VAT-registered persons are entitled to take credit in their VAT returns for VAT paid or payable in respect of goods imported in the taxable periods covered by the returns and used for the purposes of their taxable businesses. For example, a VAT-registered person who qualifies for the deferred payment facility and who imports goods in, say, January and February will pay the VAT due on the January imports on 15 February and the VAT due on the February imports on 15 March. In his VAT return for the period January/February he is entitled to a credit for all of that tax even though, if he submitted his return before 15 March, he would not have yet paid the VAT due on the February imports. Customs provide importers or agents with proof of amounts of VAT paid or deferred on imported goods in the form of a stamped copy of the entry, as passed.

12. VAT-registered persons who are in a permanent repayment position as a result of VAT paid at importation may be permitted to make monthly returns. This is a matter for arrangement with the inspector of taxes.

### **Bulk Importations**

13. Bulk importations or groupage of taxable goods (that is, the importation of different consignments of goods in one container by several persons) are treated as if each separate consignment was separately imported. In these cases, entitlement to the deferred accounting facility depends on the entitlement of each individual importer or his agent.

### **Parcel Post Importations of Taxable Goods**

14. VAT is not payable on parcel post importations of taxable goods by VAT-registered persons for the purposes of their business, provided the value of such goods is £200 or less. If the registration number is not shown, the tax will be charged by the customs and must be paid before the consignment will be released from official custody. VAT is payable on parcel post importations of taxable goods exceeding £200 in value whether or not the importer is registered for VAT.

### **Import and Export Services**

15. The zero-rating for services related to the import and export of goods is regarded as covering such items as quay rent, demurrage and storage rent on imported goods in an approved bonded transit shed or area, labour

charges for stripping or stuffing groupage containers for customs clearance or for sampling or examining cargo, payments for customs attendance and harbour dues.

### **Shannon Customs-Free Airport**

16. Goods brought into Shannon Customs-Free Airport from outside the state are not liable to VAT.

17. Goods supplied within (but not outside) the customs-free area to a registered person who is trading within the customs-free area by a registered person from outside the customs-free area qualify for zero-rating in certain circumstances. Goods supplied by a registered person who is trading within the customs-free area to another registered person who is trading within the customs-free area also qualify for zero rating. Taxable goods supplied outside the customs-free area by a registered person trading at Shannon Customs-Free Airport are always liable to VAT.

18. Goods brought into another part of the state from the Shannon Customs-Free Airport will not be liable to VAT if they have already been taxed. Goods will already have been taxed if they are supplied by a VAT-registered person trading in the customs-free area to anyone other than another VAT-registered person trading in the area.

19. The supply of taxable services to persons within the duty-free area, whether or not they are registered, does not qualify for zero-rating.

20. Firms operating within the duty-free area are regarded as taxable persons and are required to register and to make returns for VAT in the usual way. They are entitled to have goods supplied to them within (but not outside) the customs-free area at the zero rate by quoting their registration numbers and declaring that they are trading within the duty-free zone. In the case of goods such as cars and petrol, the VAT on which is generally not deductible, these firms are liable for VAT on any such goods acquired free of tax. The tax must be accounted for in VAT returns.

## **APPENDIX 10**

### **ORGANISATION AND PROCEDURES IN CUSTOMS AND EXCISE**

1. In this appendix we outline the organisation and general procedures of the Customs and Excise Branch of the Revenue Commissioners.

#### **ORGANISATION**

2. The Customs and Excise Branch of the Revenue Commissioners is responsible for the administration and collection of customs and excise duties (including VAT on importation and Common Agricultural Policy (CAP) charges on imports and exports) and for the prevention and detection of smuggling. It is also responsible for the enforcement of import and export controls and restrictions (for example, prohibitions on the importation of certain agricultural products, certain textile goods, indecent and obscene publications, drugs, firearms and ammunition) and for the collection of import and export trade statistics. Customs and Excise Officers also perform certain work under the Merchant Shipping Acts on behalf of the Department of Communications.

3. The Customs and Excise headquarters structure is composed of

- (i) the Customs and Excise Secretariat, which is organised in a number of different divisions, each specialising in a sector of the work of the Customs and Excise, and
- (ii) the Office of the Superintendents, Customs and Excise, which is responsible for the efficient working of the ex-headquarters services and which advises the Revenue Board and the Secretariat on practical and technical questions arising out of the work of the service.

4. The ex-headquarters staff, under the direction of the Collectors of Customs and Excise, are responsible for applying the various provisions governing importation and exportation of goods, including collection of duty and for the policing of ports, airports and land frontier. Various excise controls are also operated on a countrywide basis. Matters not covered by the standing instructions and cases of doubt or difficulty as well as all fraud and offence cases are referred to the Secretariat.

5. The ex-headquarters service is divided, on a regional basis, into six areas known as 'collections' — these are the Dublin, Dundalk, Cork, Galway, Limerick and Waterford collections. Each collection is divided into districts controlled by a Surveyor of Customs and Excise and subdivided into a number of stations (which forms the basic unit). There are broadly three types of station:

- (i) customs landing or shipping station—which may cover a wharf, harbour, land frontier point, airport, parcel post depot.
- (ii) station for general excise duties, prevention of illegal use of excisable products, control of goods imported for further manufacture and exportation and control of exporters operating under the Common Agricultural Policy, and
- (iii) specialised excise stations which supervise trade units such as distilleries, breweries, oil refineries and bonded spirits etc. warehouses — officers are usually in full-time attendance.

6. Approximately 2,150 people are employed in the Customs and Excise service (including headquarters staff).

## PROCEDURES

### Customs Duties

7. Customs duties are levied under the EEC Common Customs Tariff on imports originating in third countries, i.e. non-member states of the EEC and not already duty-paid in another member state. The rates of customs duties and the categories covered are set out in the Customs and Excise Tariff of Ireland which conforms to the internationally agreed system of classification of all goods in international trade for customs purposes. Rates of customs duties are set by the EEC and individual member states are not empowered to alter rates unilaterally. Customs duties collected in Ireland are remitted in full to the European Communities as part of their Own Resources. A reimbursement of 10 per cent of the amount paid is made to cover the member state's costs of collection.

8. Certain charges levied at importation are treated as if they were customs duties *viz.* value-added tax (as applied to imports), excise (import) duties and certain charges raised under the Common Agricultural Policy of the EEC. These charges are mentioned individually below but the procedures in relation to customs duties, now described, also apply, *mutatis mutandis*, to these import charges.

9. Goods may be legally imported only through approved places, such as ports, airports and land frontier stations, where facilities for landing and

examination are provided. Each arrival is notified to Customs. For example, the master of each ship must, by law, formally report his vessel and cargo to Customs. In turn, the overall cargo's contents are accounted for by the presentation, by the importers or their agents, of customs entries for all the goods making up the cargo. The customs entry is a signed declaration form which includes a description of the goods and their relative Tariff Code Number and a statement of their origin, quantity and value. An invoice showing the value of the goods normally accompanies the entry; a separate valuation declaration is required in respect of high-value items. Where the goods are of a kind subject to import restriction, for example, import surveillance, a further document may also be required.

10. When the entry is lodged, any customs duty due must be paid at that point unless deferred payment arrangements apply. Such arrangements enable payment to be deferred, generally until the 15th day of the month following the month of importation. Details of the deferred payment arrangements for customs and excise duties and VAT at importation are in Annex 1 to this appendix.

11. On lodgment of the entry, there are, broadly speaking, two procedures available for clearance of the goods from the place of arrival; special clearance (an accelerated procedure) and standard clearance. Both rely on presentation of complete and correct documentation and appropriate discharge of duty liability and are designed to facilitate speedy delivery of goods. At lodgment, the intended disposal of the goods is declared, i.e. whether for home use, for warehousing, for inward processing or otherwise.

12. Under the special clearance procedure, delivery of goods to the trader's premises directly on lodgment and acceptance of the entry may be obtained, i.e. in advance of full processing of the relevant documentation. Depending on the circumstances of the importation, there is provision for lodgment of such entries at the actual place of landing of the goods. Participation in the procedure is by prior arrangement with Customs and implies a high standard of entry-preparation and presentation. A direct debit provision makes rapid accounting possible for any duties due and for any adjustment found necessary on post-clearance processing of the documentation. Certain conditions, including a mandate for direct debit, must be fulfilled by the trader. Any examination of the goods would be on a selective basis only. It is estimated that over 60 per cent of clearances are dealt with under the special clearance procedure.

13. Apart from the special clearance procedure and depending on the accuracy and comprehensiveness of the documentation produced, Customs are ordinarily in a position to return the entry quickly to the trader for prompt clearance of the goods. Any examination of the goods would be

on a selective basis. Under this standard clearance method, payment or securing of duty is dealt with at the same time as the processing of the documentation; the goods are not cleared until the documentation has been processed satisfactorily. Entries would usually be dealt with in the Customs Houses. There is provision for lodgment of entry at a Customs House remote from the location of the goods — at Cork, for example, for goods which arrived at Dublin.

14. An importer may not wish to take immediate delivery of his goods. In that case there is provision for warehousing the goods, in approved warehouses under Customs control, pending their final disposal.

15. Certain consignees are designated authorised consignees under the Community transit procedure and production of goods to Customs at the authorised consignee's premises is allowed instead of at the point of first arrival. Allied with this, participation by individual importers/agents in the special clearance procedure makes for greater emphasis on the physical clearance of goods inland at authorised premises rather than at the place of first arrival in the state.

16. Whichever method of clearance is used, the same elements of the clearance process are apparent: lodgment of documentation; acceptance/checking procedures; accounting for duties; selective goods examination in association with the documentation; rectification of discrepancies; clearance of goods from the point of landing; certain post-clearance checks and controls. Customs entries are subject to selective post-clearance scrutiny and both original and copy entries are retained for a number of years.

17. Goods arriving by air, rail or road are treated in the same way as goods arriving by ship. There is provision for waiver of entry for low-value packages.

18. Customs control is exercised principally through checks and examinations at ports and airports and at land frontier customs stations and posts. This control is complemented by mobile patrols. Selective investigations are also carried out on a country-wide scale, principally by way of the activities of the Investigation Branch. In addition, control is exercised by means of post-importation checks.

19. The general policy of the Revenue Commissioners is to suit the convenience of traders and the public as far as possible and to keep checks and controls to the minimum consistent with the maintenance of adequate revenue security. Accordingly, imported commercial consignments are subject to selective examination only and, in the case of passenger traffic, the red-green channel system provides for travellers to make their own

declarations, with selective checking of those who opt for the green (nothing-to-declare) channel.

### **Common Agricultural Policy**

20. Criteria for charging and methods of collection applicable to customs duties generally apply to import and export charges on certain goods under the Common Agricultural Policy of the EEC. The customs acts and any instruments made thereunder apply to these charges as if they were duties of Customs.

21. Customs and Excise Officers are responsible for the certification of exports of agricultural products for the purpose of payment of export subsidies out of the EEC Farm Fund.

### **VAT on Imported Goods**

22. Under the Finance Act, 1982, VAT on imports is charged in the same way as customs duties but on the duty-inclusive value.

### **Excise Duties**

23. The present system of excise duties in Ireland is outlined in Appendix 11 of our Third Report. As was indicated in that Appendix, the same rules and methods of collection relating to customs duties also apply generally to excise duties on imported goods.

24. The procedures for the control of excise duties on home-produced goods vary between the different commodities. The following examples illustrate the types of controls applied.

25. *Home-brewed Beer.* Officers are located on the premises of the larger breweries. Small breweries are visited by an officer at least once a week. The excise duty on beer is charged as soon as the worts (unfinished beer) are collected by the brewer by reference to the original specific gravity of the worts. Brewers must keep an officially supplied Brewing Book on the brewery premises and must enter therein for each brewing the materials intended to be used, the times at which brewing will take place and (within one hour after collection of the worts) the quantity of worts produced, together with their gravity. Worts must legally be removed from one approved vessel to another in a prescribed sequence in the course of brewing operations, until finally collected in the vessel in which the official account is taken for charge of duty.

26. Selective control is exercised over each stage of the brewing operations. For example, the officer may check the volume of materials in the

mash tun and the condition of the brewing plant and sample materials used. After the worts have been collected for charge, an official account is taken by the officer in officially gauged vessels of the quantity collected and the apparent gravity of the worts. He checks the apparent gravity by a saccharometer reading. The control of breweries is aimed at preventing the use of materials not entered in the brewing book, the use of substances prohibited on health grounds, the fraudulent mixture of uncharged worts or sugar with worts already charged with duty and, in general, the prevention of any practices which might obstruct the revenue from receiving a true account of the beer produced. A proportion of the brewings is sampled by the officer for analysis as to the accuracy of the declared original gravity. This analysis is carried out in the State Laboratory.

27. *Home-manufactured Table Waters.* Excise duty on table waters is charged on the quantity sent out from the manufacturer's premises. The actual manufacturing processes are not officially supervised. The manufacturer is required to keep an entry book in which must be recorded the quantity of dutiable table waters sent out on the previous day. The entries in the book must be capable of verification by reference to the trader's records, for example, invoices, delivery dockets, credit notes. Manufacturers must furnish periodic returns (usually monthly) of the quantity of dutiable table waters delivered for home consumption. Officers visit the manufacturer's premises at least monthly. Trade records are checked to ensure that the correct quantity of table waters is being returned for duty. The capacity of bottles and other containers in which the table waters are sold is occasionally checked by physical measurement of the content, as a further check on the quantity charged with duty. Normally, table waters are not officially sampled.

#### **Trade Statistics**

28. The Customs and Excise Branch is also responsible for the collection of trade statistical data relating to imports and exports as extracted from customs documentation. The statistical information supplied includes

- (i) the monthly import and export trade statistics for publication by the Central Statistics Office. These statistics are widely used for economic forecasting, planning, etc.,
- (ii) monthly trade statistics (Special Trade) for the Statistical Office of the European Communities in Luxembourg to enable them to compile statistics on Community external trade and trade between member states,
- (iii) statistics required by the EEC for customs supervision purposes, for example, quotas, ceilings, surveillance, associate agreements, etc., and

- (iv) information required at national and international levels for the examination of various proposals, trade negotiations, monitoring of economic trends, balance of payments, etc. and by individual companies for market research purposes, etc.

#### **Cost of Administration of Customs and Excise**

29. The cost of administration of the Customs and Excise service, stated as a percentage of the net yield from the various duties, is approximately 2.5 per cent.

## ANNEX 1

1. In this annex we set out the periods of deferment for customs and excise duties and VAT at importation.

### PERIODS OF DEFERMENT ALLOWED FOR PAYMENT OF EXCISE DUTY ON MAIN EXCISABLE COMMODITIES

#### Beer

- A. Home-brewed beer  
(a) Normal deferment.

Duty may be deferred to a date not later than the 8th day of the second month following that in which the duty is charged. However, in the case of beer charged with duty in the month of November in any year, duty must be paid not later than the 28th day of December in the same year.

- (b) Extended deferment—  
(which applies to bright beers which are kept in the brewery for a period of two months after manufacture for conditioning purposes).

Duty may be deferred to a date not later than the 8th day of the third month following that in which the duty is charged. However, in respect of beer charged with duty in the month of October in any year, duty must be paid not later than the 28th day of December in the same year.

- (c) Special deferment—  
(which applies to lager beer which is kept in the brewery for a period of at least three months after manufacture).

Duty may be deferred to a date not later than the 25th day of the fourth month following that in which the duty is charged.

- B. Imported beer.

Duty may be deferred to a day not later than the 15th day of the month following that in which the duty is charged.

#### Spirits

Home and Imported.

Payment may be deferred to a day not later than the last day of the month following the month in which the spirits are entered for home use. However, in the case of spirits entered for home use between the 1st and 20th December in any year, payment must be made by the last day of that month; and no deferment is permitted in respect of spirits entered for home use on or after 21st December in any year.

#### Tobacco

Home and Imported.

Payment may be deferred to a day not later than the last day of the month following that in which the duty is charged. However, one-half of the duty charged in the month of December (other than on the last working day in that month) in any year must be paid not later than the last day of that month; and payment of the balance of the duty charged in that month may be deferred until the end of the month of January following.

#### Motor Vehicles

Home and Imported.

Duty may be deferred to a day not later than the last day of the month following that in which the duty is charged.

#### Wine

Payment may be deferred to a day not later than the 15th day of the month following the month in which the wine is entered for home use. In the case of wine entered for home use between the 1st and 20th December in any year, payment must be made by the last day of that month; and no deferment is permitted in respect of wine entered for home use on or after 21st December in any year.

## PERIOD OF DEFERMENT ALLOWED FOR PAYMENT OF CUSTOMS DUTIES AND VAT AT IMPORTATION

2. The extent of customs deferral which may be allowed is governed by the EEC. The maximum deferral is forty five days. Because VAT on imports is treated as a customs duty the same period of deferment is allowed.

## APPENDIX 11

### CUSTOMS AND EXCISE LEGISLATION

1. In this appendix we set out the important EEC and national legislation relating to customs and excise. (Amendments to these provisions are not shown).

#### Important Customs Legislation

(i) *EEC*

Common Customs Tariff	Regulation 950/1968
Valuation of Goods	Regulation 1224/80
Non-Preferential Origin	Regulation 802/68
Preferential Origin	Agreements with various countries, for example, Regulation 3390/84 (EEC/Sweden Agreement)
Inward Processing	Directive 69/73/EEC
Warehousing	Directive 69/74/EEC
Free Zones	Directive 69/75/EEC
Outward Processing	Directive 76/119/EEC
Transit	Regulations 222/77
Deferment of Customs Duties	Directive 1978/453/EEC
Harmonisation of Procedures	
Imports:	Directive 1979/695/EEC
Exports:	Directive 1981/177/EEC
Customs Debt	Directive 1979/623/EEC

(ii) *National*

Customs Consolidation Act, 1876

Finance Act, 1932

Customs Free Airport Act, 1947

Customs Act, 1956

European Communities (Customs) Regulations, 1972

**Important Excise Legislation**

Excise Management Acts, 1827, 1934 and 1841

Inland Revenue Act, 1880 (beer)

Spirit Act, 1880

Finance (Tobacco Products) Act, 1977

Imposition of Duties Act, 1957 and orders made thereunder, particularly:

Imposition of Duties (No. 221) (Excise Duties) Order, 1975

Imposition of Duties (No. 236) (Excise Duties on Motor Vehicles, Televisions and Gramophone Records) Order, 1979, as amended by the Imposition of Duties (No. 272) (Excise Duties on Motor Vehicles) Order, 1984.

Various provisions affecting excise duty may also be found in the annual Finance Acts.

**APPENDIX 12**

**CUSTOMS AND EXCISE OFFENCES AND PENALTIES**

1. In this appendix we set out the penalties for certain customs and excise offences.

**Excise Duties**

2. The excise statutes contain a wide range of penalties for infringements of the law and of control regulations. The general penalty and enforcement provisions applicable to excise duties are

- (i) Section 29 of Finance Act, 1935 which provides for a penalty of £500 for false statements in relation to excise duty.
- (ii) Section 23 of Finance Act, 1946, as amended, which provides for forfeiture of (i) goods and (ii) materials etc. used for the making of such goods where the goods/materials etc. are removed or concealed with intent to defraud and for a penalty of £1,000 for any such offence. The section also provides for forfeiture of goods where duty remains unpaid after the due date,
- (iii) Section 11 of Inland Revenue Regulation Act, 1890 and Sections 24 and 39 of the Excise Management Act, 1827 which provide for varying penalties for obstruction of officers in the exercise of their duties,
- (iv) Section 22 of Excise Management Act, 1827 which gives Excise Officers the power to enter any premises engaged in any business subject to the excise law and to inspect and take account of all goods and matters connected with that business, and
- (v) Section 28 of the Excise Management Act 1827 and Section 24 of the Excise Management Act, 1841 which provide, inter alia, that where excise duty is in arrear or owing, all goods subject to excise duties and all materials and preparations from which such goods are made and all vessels, utensils, machines etc. used in the manufacture of such goods, shall be subject and liable to all duties incurred while in the custody of a trader and may, with a view to recovering any such duties, be seized and sold.

In addition, the Act imposing the particular excise duty normally contains specific provisions for penalties. Sections 10 (5) and 11, of the Finance (Excise Duty on Tobacco Products) Act, 1977 and subsections (6), (9) and (10) of Section 65, of the Finance Act, 1982 are fairly typical of such penalties and deal with penalties for contravention of regulations made and obstruction of customs and excise officers in the exercise of their statutory powers.

### Other Customs and Excise Penalties

3. A number of specific penalty provisions for certain customs and excise offences is set out in Table 12.1. Customs and excise duties and penalties may be sued for in the High Court under various statutes, for example, Section 38, Finance Act, 1924. The new penalties applied to tax offences, obstruction, etc. by Section 94, of the Finance Act, 1983 also apply to offences involving customs and excise duties. The 1983 Act provides for fines of up to £1,000 and jail sentences of up to twelve months on summary conviction and for fines of up to £10,000 and jail sentences of up to five years on conviction of indictment. These penalties are additional to the normal penalties under the customs acts.

TABLE 12.1

Customs and Excise Offences and Penalties

Offence	Penalties and relevant statutory authority
Evasion of duty or import prohibitions.	£100 or treble the duty-paid value of goods, whichever is greater (section 186 Customs Consolidation Act, 1876, as amended by section 34, Finance Act, 1963).  Goods are liable to forfeiture (section 177, Customs Consolidation Act, 1876); conveyance is liable to forfeiture (section 202, Customs Consolidation Act, 1876).
Evasion of export prohibitions	£100 or treble the duty-paid value of goods, whichever is greater (section 3, Customs Act, 1956, as amended by section 34, Finance Act, 1963).  Goods and any conveyance are liable to forfeiture (section 5, Customs Act, 1956).
Breach of Customs (Land Frontier) Regulations, 1968 and 1978.	Not exceeding £100. Goods liable to forfeiture (section 13, Adaptation of Enactment Act, 1922).
Fraud e.g. falsification of customs documents, under-declaration of value, false claims to preference etc.	£500 or imprisonment for a term not exceeding 2 years (section 168, Customs Consolidation Act, 1876, as amended by section 16, Finance (No. 2) Act, 1915).
Assault, obstruction, rescuing of seized goods etc.	Not exceeding £100 (section 12, Customs and Inland Revenue Act, 1881)
Breach of the Motor Vehicles (Temporary Importation) Regulations, 1970.	£1,000. Motor vehicle liable to forfeiture (section 29, Finance Act, 1963, as amended by section 79, Finance Act, 1984).

Offence	Penalties and relevant statutory authority
Evasion of, or failure to pay, betting duty; unlicensed bookmaking.	£800. (section 69, Finance Act, 1982).
Bookmaking in unregistered premises	£1,000. (section 76, Finance Act, 1984).
Irregular use of rebated hydrocarbon oil.	£1,000. Section 70, Finance Act, 1983). The vehicle is liable to forfeiture if it is a second or subsequent offence by the same person or if a concealed tank or other container, or any device, contrivance or method of any kind is employed to conceal the presence in the vehicle of rebated hydrocarbon oil intended for use for combustion in the engine of the vehicle.

## APPENDIX 13

### REVENUE EFFECTS OF OUR PROPOSALS

1. In this appendix we set out the revenue effects of our proposals which were summarised in Chapter 21. In the first section we show four possible tax structures with varying single rates, tax credits and rates of value-added tax. The calculations are made on a revenue-neutral basis as required in our terms of reference. In the second section we set out in detail the bases for our estimates and our methodology.

2. We have outlined a timetable for implementing our proposals on direct and indirect taxation. Some proposals could be implemented at the start of the next tax year, others would have to be phased in. If implementation started in 1986/87, we would not expect our proposals to be fully operational until at least 1990. In assessing the revenue effects of our proposals we have had to assume a situation in which all our proposals are operational in the year 1983/84. This is the latest year for which an accurate tax base is available. It is also a period during which taxation as a share of gross domestic product was at very high levels. The exercise is therefore set in a somewhat artificial context and is undertaken to give examples of just some of the options available in a particular year under the tax system we have proposed.

3. We have based our figures on estimates supplied by the Revenue Commissioners where they could supply them. The data on which to calculate estimates of changes in tax policy of the type we proposed are variable. In some instances the data are inadequate and make reliable estimates difficult. However, the figures provide an indication of the orders of magnitude involved. In most cases we have taken the figures supplied and the assumptions made by the Revenue Commissioners. We have used our own estimates in a very small number of cases in which we are satisfied that the Revenue Commissioners have both insufficient data and are being unduly pessimistic in their assumptions. We specifically identify these areas of disagreement. The tax yield from the direct expenditure tax and the property tax recommended in our reports is estimated at 3 per cent and 5 per cent respectively of total tax revenue.

4. The net revenue effect of our proposals, assuming a single rate of tax of 35 per cent (including 5 per cent social security tax) with a personal

credit for a single person of £385 and £770 for a married person, a single rate of value-added tax of 13.4 per cent and other taxes set at levels which would be consistent with our proposals, is shown in Table 13.1. In this tax structure personal allowances have been converted to tax credits which take account of the savings to employees from the abolition of social insurance contributions. A detailed explanation of how personal allowances are converted into tax credits is contained in Annex I.

TABLE 13.1

Revenue Effects of Our Proposals 1983/84, assuming Single Tax Rate 35 per cent, Tax Credits £385/£770, Single VAT Rate 13.4 per cent.

Tax	Net Produce of Tax		
	Present System £m	Proposed System £m <sup>1</sup>	Change £m
Income Tax	1,775	2,396	+ 621
Corporation Tax	246	383	+ 137
Capital Gains Tax	6	7	+ 1
Capital Acquisitions Tax	17	40	+ 23
Direct Expenditure Tax	Nil	176	+ 176
Discretionary Trusts	Nil	3	+ 3
Property Tax	Nil	293	+ 293
Rates	110	Nil	- 110
Social Insurance Contributions	1,074 <sup>2</sup>	6	-1,028
<b>Total Direct Taxes</b>	<b>3,228</b>	<b>3,304</b>	<b>+ 116</b>
Excise Duties	1,182	1,182	—
Customs Duties	78	78	—
VAT	1,193	1,193	—
Stamp Duties	104	Nil	- 104
Motor Vehicle Duties	94	94	—
<b>Total Indirect Taxes</b>	<b>2,651</b>	<b>2,547</b>	<b>- 104</b>
<b>Total Taxes</b>	<b>5,879</b>	<b>5,851</b>	<b>+ 12</b>

Notes: (1) The calculations for the net produce of income tax, corporation tax, capital gains tax, capital acquisitions tax and value-added tax as shown in this column are set out in tables 13.7 to 13.12 of this appendix.

(2) Of this, £617 million is paid by employers including £90 million paid by the state as an employer. The cost of replacing secondary allowances, for example, blind persons' allowance, under the tax code with social welfare payments where appropriate would not exceed £50 million. The Revenue Commissioners estimate that £6 million in PRSI would be paid by export sales relief and Shannon relief companies. The net change on social insurance payments is, therefore, £1,028 million (£1,074-£90+£50-£6 million.).

5. If it were desired to grant tax credits equivalent to personal allowances, without any adjustment for the savings to taxpayers from abolishing social insurance contributions, credits of £508 and £1,016 at a rate of 35 per cent would be needed. The additional revenue required could be raised by increasing the rate of VAT to 16 per cent. The revenue effects of this tax structure are shown in Table 13.2.

TABLE 13.2

Revenue Effects of Our Proposals 1983/84, assuming Single Tax Rate 35 per cent, Tax Credits £508/£1,016, Single VAT Rate 16 per cent.

Tax	Net Produce of Tax		
	Present System £m	Proposed System £m*	Change £m
Income Tax	1,775	2,155	+ 380
Corporation Tax	246	383	+ 137
Capital Gains Tax	6	7	+ 1
Capital Acquisitions Tax	17	40	+ 23
Direct Expenditure Tax	Nil	175	+ 175
Discretionary Trusts	Nil	3	+ 3
Property Tax	Nil	292	+ 292
Rates	110	Nil	- 110
Social Insurance Contributions	1,074*	6	-1,028
Total Direct Taxes	3,228	3,061	- 127
Excise Duties	1,182	1,182	-
Customs Duties	78	78	-
VAT	1,193	1,420	+ 227
Stamp Duties	104	Nil	- 104
Motor Vehicle Duties	94	94	-
Total Indirect Taxes	2,651	2,774	+ 123
Total Taxes	5,879	5,835	- 4

\*See notes to Table 13.1 in this appendix.

6. Alternatively, the additional revenue required to grant tax credits equivalent to personal allowances could be raised by increasing the single rate of tax to 38 per cent. At this rate, credits of £550 and £1,100 would be necessary. If this were done it would be possible to maintain the VAT rate of 13.4 per cent. The revenue effects of such a tax structure are shown in Table 13.3.

TABLE 13.3

Revenue Effects of Our Proposals 1983/84, assuming Single Tax Rate 38 per cent, Tax Credits £550/£1,100, Single VAT Rate 13.4 per cent

Tax	Net Produce of Tax		
	Present System £m	Proposed System £m*	Change £m
Income Tax	1,775	2,347	+ 572
Corporation Tax	246	421	+ 175
Capital Gains Tax	6	8	+ 2
Capital Acquisitions Tax	17	43	+ 26
Direct Expenditure Tax	Nil	175	+ 175
Discretionary Trusts	Nil	3	+ 3
Property Tax	Nil	292	+ 292
Rates	110	Nil	- 110
Social Insurance Contributions	1,074*	6	-1,028
Total Direct Taxes	3,228	3,295	+ 107
Excise Duties	1,182	1,182	-
Customs Duties	78	78	-
VAT	1,193	1,193	-
Stamp Duties	104	Nil	- 104
Motor Vehicle Duties	94	94	-
Total Indirect Taxes	2,651	2,547	- 104
Total Taxes	5,879	5,842	- 3

\*See notes to Table 13.1 in this appendix.

7. Table 13.4 shows that it is possible to reduce the revenue from indirect taxation by setting the single tax rate at 40 per cent and allowing tax credits of £580 and £1,160, that is, equivalent to personal allowances. If this were done, a single VAT rate of 11.75 per cent could be achieved.

TABLE 13.4

Revenue Effects of Our Proposals 1983/84, assuming Single Tax Rate 40 per cent, Tax Credits £580/£1,160, Single VAT Rate 11.75 per cent.

Tax	Net Produce of Tax		
	Present System £m	Proposed System £m*	Change £m
Income Tax	1,775	2,470	+ 695
Corporation Tax	246	447	+ 201
Capital Gains Tax	6	8	+ 2
Capital Acquisitions Tax	17	45	+ 28
Direct Expenditure Tax	Nil	175	+ 175
Discretionary Trusts	Nil	3	+ 3
Property Tax	Nil	292	+ 292
Rates	110	Nil	- 110
Social Insurance Contributions	1,074*	6	-1,028
Total Direct Taxes	3,228	3,446	+ 258
Excise Duties	1,182	1,182	—
Customs Duties	78	78	—
VAT	1,193	1,043	- 150
Stamp Duties	104	Nil	- 104
Motor Vehicle Duties	94	94	—
Total Indirect Taxes	2,651	2,397	- 254
Total Taxes	5,879	5,843	+ 4

\*See notes to Table 13.1 in this appendix

## ESTIMATES AND CALCULATIONS

8. We now set out in more detail the estimates we have used in making our calculations. In Table 13.5 we summarise the estimates of the tax bases and net produce of tax for 1983/84. In the following tables 13.6 to 13.13 we set out in detail the extensions and deductions from these base figures which would arise as a result of our proposals.

9. The figures in Table 13.5 for the tax base and net produce of tax under various headings have been supplied by the Revenue Commissioners.

TABLE 13.5

Estimates of Tax Base and Net Produce of Tax in 1983/84

	Tax Base £m	Net Produce of Tax £m
Income Tax	4,744	1,775
Corporation Tax	729	246
Capital Gains Tax	12	6
Capital Acquisitions Tax	110	17
Social Insurance Contributions and Levies	—	1,074

Source: The Revenue Commissioners.

Note (1): The social insurance contributions and levies of £1,074 million include contributions by employers, employees and the self-employed, as follows: Employees, £457; Employers, £596; Self-employed, £21.

### Income Tax

10. In Table 13.6 we take the base figure supplied by the Revenue Commissioners for income tax of £4,744 million. To this figure we add back the deductions allowed under the existing system but which we propose should be abolished. We deduct from the base nominal interest from bank and building society deposits as this income would not be taxed under our proposals. Estimates of the amount of income exempt under some headings have to be tentative since the information on which to calculate reliable estimates is not collected.

TABLE 13.6

## Extension to Income Tax Base 1983/84

	£m	£m
Taxable Income		4,744
<i>Additions to Base</i>		
Married Persons' Allowance	1,087.5	
Single Persons' Allowance	636.6	
Widowed Persons' Allowance (no Children)	45	
(with Children)	26	
Single Parents' Allowance	32	
Child Allowance	36	
Social Welfare Allowance	196	
Deduction for Schedule E Taxpayers	485	
Exempt Income of Taxpayers Subject to Marginal Relief	112	
Income of Person Exempted Under Exemption Limits plus		802
Short-term Social Welfare Benefits		802
Income of Persons Currently Outside the Tax Net	317	
Interest Paid in Full	167	
Medical Insurance Premiums	27	
Life Assurance	33	
Retirement Pension Lump Sum	90	
Schedule D Current Basis	50	
Rates' Deduction	38	
Age Allowance	3	
Dependent Relative Allowance	12	
Blind Persons' Allowance	0.2	
Allowance for Employed Person to Care for incapacitated individual	3.5	
Expenditure on Residential Premises	5.7	
Health Expenses' Relief <sup>1</sup>	3	
Premiums under Permanent Health Benefit Schemes	1.5	
Loans to Employees at Preferential Rates of Interest	27	
Artists' Relief	2	
Convenanted Subscriptions	7	
Statutory Redundancy Payments	23	
Income from Certain Industrial Companies to Individual Investors	1.5	
Compensation Payments for Loss of Office <sup>2</sup>	25	
Profits of Sweepstakes under Public Hospitals Act, 1933	0.4	
Prize Bond and Sweepstake Winnings by Residents	6	
Fringe Benefits <sup>3</sup>	170	
Employers' Social Insurance Contributions as Deduction <sup>3</sup>	132	
Treat Persons in Year of Marriage as Single	26	
Additions to Base as Result of 1983 Budget	30	
<i>Deductions from Base</i>		
Bank Deposit Interest <sup>4</sup>	166	
Building Society Interest <sup>5</sup>	4	4,539
Adjusted Income Tax Base		9,283

*Notes:*

(1) We recommended in our first report that health expenses' relief be retained for persons who incur substantial expenses in the treatment of long-term or recurrent illness. Expenses in excess of £500 should be allowed. However, we considered that the most appropriate method of helping persons in these categories was through direct expenditure under the health services and that ultimately health expenses' relief should be abolished.

(2) We recommended in our first report that premiums paid under permanent health benefit schemes should not be allowed as a deduction for tax. However, any benefits paid under these policies should be free of tax.

(3) The Revenue Commissioners were unable to supply figures under this heading. We estimated the addition to the base at £25 million.

(4) The Revenue Commissioners regard this figure as high but it was let stand for working purposes.

(5) Employers' contributions for 1983/84 are estimated to be £617 million. Of this amount, £90 million is estimated to be paid by the state as an employer. The balance of £527 million has been divided between corporate and non-corporate employers in the ratio 3:1. The non-corporate employers' contribution is included in this table. The corporate employers' contribution is included in Table 13.9 (Adjusted Corporation Tax Base).

(6) Bank deposit interest and building society interest would be taxable on the basis of real interest only. We are deducting an estimated amount for nominal interest from the tax base because in 1983 the interest rate was less than the rate of inflation. These estimates were supplied by the Revenue Commissioners.

(7) Building society deposit interest, tax on which is levied at the composite rate by the building societies, is not included in the tax base and therefore the only deduction appropriate is an amount in respect of such interest which is subject to tax at the higher rates and which is included in the base.

11. The Revenue Commissioners estimated that a switch to the current year basis would result in an increase in profits of the order of 30 per cent on the basis of a long term rate of inflation of 15 per cent. The 30 per cent addition to the tax base was estimated at £154 million for 1981/82. The rate of inflation is now close to 5 per cent but Schedule D income has increased in the meantime. While there is agreement that a change to current year basis of assessment for Schedule D taxpayers would result in an addition to the tax base, the Revenue Commissioners have estimated that any gain arising would be offset by the loss of revenue resulting from the implementation of the inflation adjustments proposed in recommendations 123 to 133 of our first report. However, the inflation adjustments in respect of capital allowances are included in the Revenue Commissioners' costings of the second report (See Annex 3). We believe that the remaining inflation adjustments have a nil cost. An increase in the tax base of £50 million has been substituted.

12. The net produce of tax for a given rate is calculated by reducing total income tax by the cost of tax credits. The credits to be deducted include personal tax credits for all taxpayers, credits for distributions chargeable under Schedule F and a credit for rates paid by businesses. The net produce of tax on the adjusted income tax base at a rate of 35 per cent with personal tax credits of £385 (single person) and £770 (married person) is shown in Table 13.7.

TABLE 13.7

## Net Produce of Tax at 35 per cent on the Adjusted Tax Base, 1983/84

	£m	£m
Adjusted Income Tax Base		9,283
Total Tax at 35 per cent		3,249
<i>Cost of Credits</i>		
Married Persons (£770×587,000) <sup>1</sup>	452	
Other Persons (£385×763,000) <sup>2</sup>	294	
Credit for Rates Paid (Schedule D) <sup>3</sup>	38	
Credit for Distributions (Schedule F) <sup>3</sup>	59	
Head of Household Credit (£385×25,000)	10	853
Net Produce of Tax		2,396

*Notes:*

(1) Details of the conversion of existing personal allowances to tax credits are in Annex 1. The number of taxpayers under our proposals would increase. Details of how we arrived at the number of taxpayers are in Annex 2.

(2) This is the estimated rates paid by the non-corporate business sector. It corresponds with the figure of £38 million in Table 13.6.

(3) This is the estimated Schedule F credit at a single tax rate of 35 per cent. The credits at single tax rates of 38 per cent and 40 per cent would amount to £63 million and £66 million respectively.

13. The net produce of income tax under our proposals at tax rates of 35 per cent, 38 per cent and 40 per cent with personal tax credits equivalent to 1983/84 personal allowances is summarised in Table 13.8.

TABLE 13.8

## Net Produce of Income Tax at Various Rates on the Adjusted Income Tax Base, 1983/84

Rate of Tax %	Personal Tax Credits £	Total Tax £m	Cost of Credits £m	Net Produce of Tax £m
35	508/1016	3,249	1,094	2,155
38	550/1100	3,528	1,181	2,347
40	580/1160	3,713	1,243	2,470

**Corporation Tax**

14. Table 13.9 contains details of the base for corporation tax in 1983/84 together with additions to the base which arise from our proposals.

TABLE 13.9

## Adjusted Corporation Tax Base, 1983/84

	£m	£m
Amount Chargeable to Corporation Tax		667
<i>Add</i>		
ESR Profits Switched to 10 per cent Rate <sup>1</sup>	62	
Corporate Tax Base		729
<i>Additions due to our proposals</i>		
Rates Deduction	67	
PRSI Deduction <sup>2</sup>	374	
Recommendations in our Second Report <sup>3</sup>	115	556
Adjusted Tax Base		1,285
Produce of Tax at 35 per cent	=	450
Produce of Tax at 38 per cent	=	488
Produce of Tax at 40 per cent	=	514
<i>Deduct</i>		
Rates Credit	67	
Net Produce of Tax at 35 per cent		383 (see Tables 13.1 and 13.2)
Net Produce of Tax at 38 per cent		421 (see Table 13.3)
Net Produce of Tax at 40 per cent		447 (see Table 13.4)

*Notes:*

(1) This figure is no more than a guess supplied by the Revenue Commissioners to cover firms who switch from export sales relief to the 10 per cent manufacturing rate. It is estimated that 20 per cent of profits of export sales relieved companies might become subject to the 10 per cent. Only companies with a mix of home and export sales would make such a switch and then only where the ratio of exports to home sales was less than 4:1.

(2) Employers' contributions for 1983/84 are estimated to be £617 million. Of this amount £90 million is estimated to be paid by the state as an employer. The balance of £527 million has been divided between corporate and non-corporate employers in the ratio of 3:1. A further downward adjustment of £21 million has been made in the corporate element of £395 million to exclude export sales relieved and Shannon relieved companies.

(3) This represents the addition to the tax base as a result of the recommendations in our second report. The addition to the base of £115 million was calculated by the Revenue Commissioners. Full details of the figures are set out in Annex 3.

15. The Revenue Commissioners have estimated that the corporate tax base (£729 million) after the inflation adjustments proposed in recommendations 123 to 133 of our first report would fall to £292 million. This represents a drop of 60 per cent in the corporate tax base. The inflation adjustments in respect of capital allowances have been taken into account in the Revenue Commissioners' costings of our second report (see Annex 3). The information on which to base an estimate of inflation-adjusted profits is sparse. As a result, there is ample room for argument. We believe that the Revenue Commissioners' estimate is too high.

16. Stewart<sup>1</sup> examined six companies in 1979 and found that the difference between inflation adjusted profits and profits as conventionally measured was about 28 per cent. The Revenue Commissioners take the view that Stewart's study is not particularly relevant since it specifically excludes financial and investment companies and "the greatest effects occur in the case of these very companies".

17. A United Kingdom estimate<sup>2</sup> of the cost of changing to a Current Cost Accounting (CCA) basis in the case of financial companies indicated that the profits of such companies would have been reduced by about 21 per cent on average in the years 1976 to 1980.

18. To compute profits on a current cost basis, four adjustments are made to the historical cost profit as follows:

- (i) a cost of sales' adjustment,
- (ii) a depreciation adjustment,
- (iii) a monetary working capital adjustment, and
- (iv) a gearing adjustment.

19. In our first report we recommended the introduction of the equivalent of the first three of these adjustments. We did not recommend the equivalent of a gearing adjustment because we took the view that tax should be charged on profits before deduction of interest. These are higher than CCA profits. In this regard, it is interesting to note the estimate in the U.K. Green Paper 'Corporation Tax' that if corporation tax had been charged on CCA profits on a revenue-neutral basis, the rate would have been on average about 48 per cent compared with 52 per cent on a historical cost basis. There would have been very large variations in the revenue-neutral rate from year to year.

20. The Revenue Commissioners' estimate of the cost of inflation adjustments would add up to 2 per cent to the single tax rate or up to 1.7 per cent to the rate of VAT. However, it is worth noting that their costings were made at a time when the annual rate of inflation was over 17 per cent. Inflation is likely to be about 5.5 per cent on average in 1985.<sup>3</sup>

### Capital Gains Tax

21. Table 13.10 sets out the base for capital gains tax in 1983/84. The base for capital gains tax fell substantially in 1983 with the decline in real terms in the value of assets. Any recovery in asset prices could be expected to lead to a significant increase in these figures.

<sup>1</sup>'Company Tax — Effective Tax Rates on Profits', J. C. Stewart, Paper read to the Statistical and Social Inquiry Society of Ireland, 2 April, 1981.

<sup>2</sup>Corporation Tax, Green Paper, January, 1982, Cmnd 8456 Table 9A.

<sup>3</sup>Central Bank of Ireland, Quarterly Bulletin, Summer 1985.

**TABLE 13.10**  
**Adjusted Capital Gains Tax Base, 1983/84**

	£m	£m
Chargeable Gains		12
<i>Additions to Base</i>		
Roll-over Relief	6	
Disposal of Business or Farm	1	
Death or Disposal of Principal Private Residence	13	
Small Gains	5	
CPO Relief	NI	28
<i>Deductions from Base</i>		
Tax Credit on Company Distributions	1	
Indexation Losses	18	19
Net Addition		9
New Base		21
Net Produce of Tax at 35 per cent		7 (see Table 13.1 and 13.2)
Net Produce of Tax at 38 per cent		8 (see Table 13.3)
Net Produce of Tax at 40 per cent		8 (see Table 13.4)

Note: All of these figures were supplied by the Revenue Commissioners.

### Capital Acquisitions Tax

22. The Revenue Commissioners estimate the taxable value of gifts and inheritances in 1983 to be £110 million. Table 13.11 shows our estimate of the addition and deduction to this base as a result of our recommendations.

**TABLE 13.11**  
**Adjusted Capital Acquisitions Tax Base, 1983**

	£m	£m
Estimate of taxable value of gifts and inheritances		110
<i>Add</i>		
Abolition of agricultural valuation	12	
<i>Deduct</i>		
Exemption of inter-spousal transfers	9	
Net Addition		3
Adjusted Base		113
Net produce of tax at 35 per cent		40 (see Tables 13.1 and 13.2)
Net produce of tax at 38 per cent		43 (see Table 13.3)
Net produce of tax at 40 per cent		45 (see Table 13.4)

### Expenditure Tax

23. In 1983/84, the tax yield from the higher rates of tax was £223 million — representing 14 per cent of total income tax revenue or 4 per cent of total tax revenue. We do not envisage the yield from expenditure tax amounting to more than 3 per cent of total tax revenue.

### Property Tax

24. It is difficult to assess the revenue yield from imposing a property tax. However, it seems possible that based on international comparisons this could account for up to 5 per cent of total tax revenue.

### Other Taxes

25. No figures are available on the amount of capital in discretionary trusts. An estimate of £3 million is included as the likely yield from the annual charge on such capital recommended by us. No yield has been assumed from the accessions' tax put forward by us as the most effective means of achieving redistribution of wealth.

### Indirect Taxes

26. Customs and excise duties as well as motor vehicle duties have been calculated on a revenue-neutral basis. Stamp duties have been completely abolished for the purposes of these calculations. However, we have said that we do not regard them as priority matters but rather as items which should be implemented in the longer term as resources permit.

27. Table 13.12 shows the VAT base for 1983 supplied by the Revenue Commissioners. VAT is calculated on a calendar basis rather than on a tax year basis.

**TABLE 13.12**  
**Value-Added Tax Base, 1983**

	£m	£m
Total Tax Base		9,607
<i>Deduct</i>		
Animal Feed Stuffs, Fertilisers, Seed Plants etc.	726	
Animal Medicines	4	
		730
Total Adjusted Base		8,877
Net Produce of Tax at 16 per cent		1,420 (see Table 13.2)
Net Produce of Tax at 11.75 per cent		1,043 (see Table 13.4)

Source: The Revenue Commissioners

### Social Security Tax Base

28. We recommended in our first report that social insurance contributions should be replaced by a social security tax levied at a uniform rate on all income including realised capital gains and taxable gifts and inheritances. Table 13.13 summarises the tax base for all taxes on income.

**TABLE 13.13**  
**Social Security Tax Base**

	£m
Income Tax Base	9,283
Corporation Tax Base	1,285
Capital Gains Tax Base	21
Capital Acquisitions Tax Base	113
	10,702
Estimated Gross Income of Pension Funds <sup>1</sup>	120
Add possible <sup>2</sup> extra benefits payable to self-employed and civil servants on the introduction of a social security tax	300
	11,122

*Notes:*

(1) We do not envisage that social security tax would be repaid to exempt funds since these effectively bear some of the burden of the present employers' social insurance contribution which the tax is designed to replace. (See paragraph 21.38 of the first report) However, we have not included any revenue from this source in our calculations in this appendix.

(2) It does not necessarily follow that the introduction of a social security tax must inevitably lead to the extension of benefits. There is no longer a close relationship between social insurance contributions and benefits. Many people who have absolutely no entitlement to benefits at present bear the burden of the existing social insurance contributions. Of course, if the benefits were to become payable, they would be included in the tax base. It is assumed that no additional benefits would become payable.

## ANNEX 1

### Personal Allowances and Tax Credits

1. In this Annex we show the conversion of personal allowances into tax credits. The level of tax credit is determined by the level of personal allowances and the rate of tax. For example, in 1983/84 a married employee earning £2,900 was not liable for tax. At a single rate of 35 per cent he would need a tax credit of £1,015 to leave him in a similar situation (£2,900 × 35 per cent). Table 13.14 below shows the tax credits equivalent to 1983/84 personal allowances at various rates of tax for both single and married people.

TABLE 13.14

Personal Allowances and Equivalent Tax Credits, 1983/84

Tax Rate %	Tax Credit equivalent to Single Persons' Allowance (£1,450) £	Tax Credit equivalent to Married Persons' Allowance (£2,900) £
35	508	1,016
38	550	1,100
40	580	1,160

Note: The tax credits have been rounded for working purposes

2. However, the straightforward conversion of personal allowances into tax credits at a single rate of tax does not take into account the savings to employees from the abolition of social insurance contributions. For example, in 1983/84 a married employee earning £2,900 was not liable for income tax but was liable for £248 in social insurance contributions. It is arguable, therefore, that £248 should be deducted from his tax credit when converted from a personal allowance. Taking 1983/84 personal allowances, the equivalent tax credits at a rate of 35 per cent would be as follows:

	Single Person £	Married Person £
Income	1,450	2,900
Tax liability at 35 per cent	508	1,015
Present liability to PRSI at 8.5 per cent	123	247
Credit required	385	768

Note: (1) For working purposes this credit has been rounded to £770 in the calculations.

## ANNEX 2

### Proposed Number of Taxpayers

1. The Revenue Commissioners have estimated that the number of people in the tax net, assuming implementation of our proposals, would be 1,350,000. This figure is based on the estimated labour force for 1983 and includes the abolition of the exemption limits except in the case of those over seventy five. The breakdown is as follows:

Estimated total labour force per 1981 Census	1,260,000
Estimated total labour force for 1983	1,288,000
Add occasional and seasonal workers	30,000
	1,318,000
Less number of working wives counted separately	125,000
	1,193,000
Estimated number of persons aged 65 and over per the 1979 Census	361,000
Less estimated 50,000 included in the labour force figures above	50,000
Balance	311,000
Deduct most of those over 75 on the basis that most would be excluded by virtue of the exemption limits	100,000
	211,000
Of these about 50 per cent are married, 25 per cent are single and 25 per cent are widowed (See Table 1A 1979 Census). Therefore, additional cases for inclusion in the tax net (211,000 × 3/4)	158,000
	1,351,000 <sup>2</sup>
Round to	1,350,000

<sup>1</sup>Per CSO estimate.

<sup>2</sup>This figure does not take into account young persons looking for their first job (not included in the labour force). However, this omission will make little difference since their income, mainly state payments, would not be sufficient to absorb their tax credit. In any event, many of these are likely to be single and living and maintained at home.

2. We have apportioned this number of 1,350,000 taxpayers by marital status in the same ratio as the existing marital status breakdown:

Status	Existing Numbers ('000)	Proposed Numbers ('000)
Married	375	587
Single	439	687
Widowed	37	58
Single Parents	11	18
Total	862	1,350

### ANNEX 3

#### Revenue Yield from Second Report

1. In this annex we show the revenue yield, as estimated by the Revenue Commissioners,<sup>1</sup> from the recommendations in our second report. Table 13.15 sets out the details of the gains and losses to the Exchequer.

TABLE 13.15

#### Revenue Yield from Recommendations in the Second Report

Recommendation Number	Recommendation	Tax Gain £m	Tax Loss £m
3	Taxation of co-operatives	5	
6	Indexation of allowances — machinery and plant		9
7	Indexation of allowances — motor vehicles		1
18	Non-renewal of section 23 relief	1	
20	Confining capital allowances for machinery and plant to cost net of grants	16	
23	Deductions in computing profits in respect of wages should be net of amounts received under employment schemes	0.5	
26	Ending of Preference Share Financing/Section 84 loans	40	
32	Retention of employers' PRSI for firms who insist on retaining their tax relieved status	11	
		<u>73.5</u>	<u>10</u>

Overall implications for Exchequer — Tax Gain of £63.5 million

Note (1): The number relates to the summary of recommendations in the second report.

2. This additional gain of £63.5 million is comprised of £52.5 million in pure corporation tax plus £11 million from employers who retain their tax-relieved status, that is, companies with entitlements to export sales' relief and Shannon relief. It is estimated that such employers will pay £6 million of PRSI and £5 million of corporation tax. The total impact of the recommendations in the second report would be to raise an additional £57.5 million from corporation tax and £6 million from PRSI. The £6 million of PRSI would reduce the revenue requirement by that amount while the

<sup>1</sup>Letter dated 26 July, 1985.

£57.5 million of corporation tax would — at the 50 per cent corporation tax rate upon which the estimates were based — increase the tax base by £115 million.

3. The Revenue Commissioners made the following assumptions in calculating the losses and gains to the Exchequer:

- All 10 per cent manufacturing firms could be expected to opt for normal corporation tax at the new single rate — with their shareholders claiming full relief for the additional corporation tax paid by the companies.
- Export sales-relieved and Shannon-relieved companies could arrange their affairs to minimise their liabilities by channelling their profits into holding companies with very few staff which would remain within the existing system (tax relief plus PRSI). The profit-generating part of the enterprise would opt into the new scheme.

## Index to the First Report of the Commission on Taxation – Direct Taxation

- Ability to pay**  
aspect of equity 8.2
- Advance corporation tax** 28.4 – 28.9
- Agricultural Credit Corporation**  
deposit interest exemption 11.31
- Agriculture**  
determination of prices for agricultural output 5.13
- Allowances, personal tax** (see Personal tax allowances and reliefs)
- Annual payments, definition** 10.95
- Annuities, retirement** (see Retirement annuities)
- Antiques**  
capital gains tax treatment 18.49  
expenditure tax treatment 18.48 – 18.50
- Aosdana payments** 10.60
- Artists' exemption** 10.55 – 10.59
- Asprey Committee**  
unit of taxation 15.10
- Assigned revenues** 21.36  
arguments for and against 22.2 – 22.5  
health contributions system 22.6 – 22.19  
Youth Employment Levy 22.20 – 22.22
- Averaging**  
block averaging 19.15  
expenditure tax 18.47, 18.63  
farmers 19.7 – 19.12  
historical background 19.4  
inflation adjustment 19.24 – 19.27  
introduction 8.15  
length of recommended period 19.23  
lifetime 19.13  
need for 19.2  
scope of recommended provisions 19.21 – 19.22  
tax reserve certificates 19.14  
United States system 19.18 – 19.19
- Avoidance and evasion**  
direct expenditure tax 18.58 – 18.60
- Banks**  
Central Bank of Ireland 30.8 – 30.9 (see also Central Bank of Ireland)  
incidence of bank taxation 30.10 – 30.12  
liquidity ratios 30.13 – 30.18  
present tax situation 30.6  
special levies 30.19 – 30.21  
tax-related lending 30.22 – 30.32  
withholding tax on distributions 30.33 – 30.34
- Benefits-in-kind** (see Fringe benefits)
- Betterment** (see Development gains)
- Beveridge Report**  
children's allowances 16.17
- Borrowing**  
effects of inflation 11.1  
source of government revenue for current budget 1.31 – 1.32
- Building Societies** 30.35 – 30.36  
composite rate arrangement 11.34 – 11.40  
corporation tax rate 25.7
- Building Societies' Association**  
composite rate arrangement 11.36 – 11.37
- Bunching**  
effect on capital gains tax 13.30 – 13.35  
impact on comprehensive tax base 8.15
- Business income**  
cost of sales adjustment (see Stock relief)  
depreciation (see Depreciation)  
essential features of accounting system for tax purposes 26.22  
stock relief 26.40 – 26.47  
stock relief, basis of adjustment 26.48 – 26.52  
stock relief, deficiencies 26.41  
stocks 26.38 – 26.52
- Capital acquisitions tax** (see Gifts' and inheritances' taxes)

**Capital gains**  
 comprehensive definition of income 13.14 - 13.18  
 definition 13.3 - 13.6

**Capital gains tax**  
 accrual versus realisation 13.19 - 13.25  
 bunching problems 13.30 - 13.35  
 compulsory purchase 13.65  
 definition of disposal 13.43 - 13.49  
 description 9.7 - 9.8  
 disposal of business or farm 13.66 - 13.68  
 efficiency 4.5  
 equity 4.5  
 exemption 13.51  
 government securities 13.54  
 inflation 13.26 - 13.29  
 list of exemptions, Appendix 10  
 losses, treatment of 13.36 - 13.43  
 main provisions, Appendix 10  
 personal chattels 13.55  
 present system 13.7 - 13.13  
 private residence 13.57  
 reform 38.14 - 38.15  
 replacement of business assets 13.62 - 13.64  
 roll-over relief 13.60 - 13.61  
 small gains 13.53  
 treatment of companies 13.75

**Carter Commission** 8.8  
 rules for taxation of fringe benefits 12.12  
 unit of taxation 15.9

**Central Bank of Ireland** 30.8 - 30.11,  
 30.13 - 30.18, 30.20, 30.27, 30.36

**Central Statistics Office**  
 indices of stock prices 26.46

**Child allowances** (see Personal taxation - allowances and reliefs)

**Close companies**  
 corporation tax treatment 25.15 - 25.20

**Commission on Income Taxation**  
 averaging, recommendations 19.5  
 dependent relative allowance recommendations 16.29  
 investment income surcharge 33.13

**Company taxation** (see also Corporation tax)  
 advance corporation tax 28.4 - 28.9  
 basis of charge 25.2  
 capital gains tax treatment 13.75  
 classical system 27.6  
 closely-held companies 28.18 - 28.23  
 computation of profits 25.3  
 desirable attributes of general system 27.8

double taxation 29.3 - 29.11  
 double taxation elimination 29.6 - 29.9  
 double taxation and Irish tax incentive schemes 29.15  
 equity 27.29  
 EEC obligations 29.18 - 29.22  
 historical development, Appendix 17  
 imputation system 27.7, 29.16 - 29.17  
 incentive reliefs, Appendix 17  
 Irish dividends under the partial imputation system 29.12 - 29.14  
 limited liability 24.10  
 neutrality 27.9 - 27.28  
 neutrality and the distribution of company profits 27.14 - 27.17  
 neutrality and the quality of investment 27.10 - 27.22  
 neutrality and the raising of new funds by companies 27.25 - 27.28  
 neutrality and the volume of private savings 27.23 - 27.24  
 personal taxation 31.3 - 31.4  
 recommended rate 28.2 - 28.3  
 relationship between company and shareholders 24.2 - 24.9  
 retained profits 24.11, 27.20 - 27.22  
 small companies 28.14 - 28.17  
 subsidiary company operation 29.10 - 29.11  
 timing of payments 28.10 - 28.13  
 two-rate system 27.7

**Compensation payments**  
 loss of office 10.42 - 10.44  
 physical or other injury 10.50 - 10.52

**Comprehensive income tax base** (see Tax base)

**Comprehensive tax base** (see Tax base)

**Consultative Committee of Accountancy Bodies - Ireland**  
 incorporated and unincorporated entities 31.3  
 neutrality between retained and distributed profits 27.31

**Corporation tax** (see also Company taxation)  
 basis of assessment 25.5  
 close companies 25.15 - 25.20  
 distributions 25.8 - 25.11  
 dividends (see distributions)  
 equity 4.8  
 group relief 25.13  
 number of assessments 27.4 - 27.5  
 payment 25.12  
 rates of tax 25.6 - 25.7  
 reforms 38.16 - 38.17  
 simplicity 4.9

**Cost of sales adjustment** (see Business income)

**Convenants**  
 between separated spouses 10.104 - 10.107  
 tax treatment 10.96 - 10.103

**Credits, tax** 16.48 - 16.51  
 amounts 16.58 - 16.60  
 purpose 16.58 - 16.60  
 under progressive tax system 16.52 - 16.57

**Current cost accounting** 26.15 - 26.19  
 compared with current purchasing power accounting 26.25 - 26.37

**Current purchasing power accounting** 26.20 - 26.21  
 compared with current cost accounting 26.25 - 26.37

**Deductions from income** (see Income, deductions from)

**Denison E. F.** 20.20

**Department of Finance**  
 capital allowances on second-hand buildings 26.80  
 current cost accounting 26.33  
 deposit interest exemption 11.32  
 direct expenditure tax, assessment and collection 18.51  
 direct expenditure tax, feasibility 18.25  
 identification of expenditure taxpayers 18.27  
 indexation 20.15  
 stock relief 26.42

**Department of Social Welfare**  
 social insurance 21.7 - 21.9, 21.11

**Deposit interest, exemption** 11.27 - 11.33

**Depreciation** 26.57 - 26.61  
 asset lives 26.84  
 basis of allowances 26.62 - 26.69  
 buildings 26.74  
 index for adjustment purposes 26.66  
 land 26.73  
 lessors and occupiers of industrial buildings 26.77 - 26.78  
 Lord Kaldor's view 26.58  
 losses 26.85  
 motor vehicles 26.82 - 26.83  
 present tax treatment, Appendix 20  
 qualifying expenditure 26.70 - 26.85  
 recommended basis of allowance 26.65  
 Royal Commission on the Taxation of Profits and Income 26.59

second-hand industrial buildings 26.79 - 26.81  
 S.S.A.P. 16., 26.62

**Devaluation**  
 as outcome of shifting incidence of taxation 5.14  
 effects 5.15

**Development gains**  
 definition of betterment 14.3 - 14.4  
 definition of disposal 14.18  
 identification of gain 14.19  
 Kenny Committee recommendations 14.5 - 14.8  
 present treatment 14.9 - 14.12  
 rate of tax 14.16 - 14.17  
 treatment in other countries, Appendix 11

**Dilke Committee**  
 investment income surcharge 33.12

**Direct expenditure tax**  
 advantages 8.18 - 8.20  
 antiques 18.48 - 18.50  
 assessment and collection 18.51 - 18.54  
 assets, treatment 18.31 - 18.50  
 averaging 18.47, 18.63  
 avoidance and evasion 18.58 - 18.60  
 consumer durables 18.45 - 18.47  
 definition 4.10 - 4.11, 8.17, 18.4 - 18.5  
 disadvantages 8.21  
 distinction from income tax 18.11 - 18.13  
 double taxation relief 18.55 - 18.57  
 efficiency 4.12, 18.14 - 18.16  
 emigration 18.64  
 equity 4.12, 18.10 - 18.13  
 expenditure tax payable, treatment 18.71  
 gifts and bequests 18.68  
 housing 18.34 - 18.41  
 identification of liable taxpayers 18.27 - 18.30  
 immigration 18.67  
 income tax payable, treatment 18.70  
 loans 18.42 - 18.44  
 Lord Kaldor's views 18.7  
 Murphy case 18.75  
 practical difficulties 18.25 - 18.26  
 savings 11.2  
 structure 18.72 - 18.78  
 transitional problems 38.26 - 38.45  
 unit of taxation 18.62

**Disincentive of taxation**  
 perceptions 2.11

**Distribution of income in Ireland**  
 income tax as instrument of redistribution 17.13  
 information 6.2, Appendix 5  
 taxation effects, Appendix 5

**Distribution of taxation**

objectives 6.9

**Distribution of wealth**capital transfer taxes 36.13 - 36.28  
information, Appendix 31  
sources of inequality 36.5 - 36.7  
wealth tax 36.10 - 36.12**Double taxation**

expenditure tax 18.55 - 18.57

**Earmarked taxes** (see Assigned revenues)**Educational expenses** 10.85 - 10.86,  
10.89**Efficiency**advantages of single rate 18.14 - 18.16  
capital gains taxes 13.16  
criterion for tax system 3.7 - 3.9  
neutrality of company taxation 27.9 -  
27.28  
wealth tax 35.12 - 35.14**Equity**capital gains 13.15  
company taxation 27.29  
criterion for tax system 3.2 - 3.6  
expenditure tax 18.13 - 18.15  
progressivity 18.1  
perceptions of tax 2.3 - 2.9  
tax base 8.1  
treatment of losses 13.40  
wealth tax 4.17, 35.5 - 35.11**Equivalence scales** 16.61 - 16.64**Evasion** (see Avoidance and evasion)**Exempt income** (see Income, exempt)**Exemption limits, personal** 16.45 -  
16.47**Expenditure on residences** 10.74 -  
10.75**Expenditure tax** (see Direct expenditure tax)**Expenses, educational** (see Educational  
expenses)**Expenses, Schedule E** (see Schedule E  
expenses)**Expenses, travelling to work** (see Travel-  
ling to work, expenses)**Export sales relief** 11.45

380

**Farming**agriculture in the Irish economy, Appendix  
26**Farming profits**averaging provisions 19.7 - 19.12  
breeding stock 32.9  
determination of income 32.4 - 32.9  
exemptions from income tax 32.11  
farm management survey 32.25 - 32.34  
historical background, Appendix 27  
incentives to increase national herd 32.16  
payment of tax 32.38  
production unit accounting 32.24 - 32.37  
rates on land 32.19  
resource tax 32.20 - 32.23  
stock valuation at present 32.6 - 32.7  
trading stock 32.8**Financial institutions**banks 30.6 - 30.34  
building societies 11.34 - 11.40, 25.7,  
30.35 - 30.36**First In First Out** 26.39**Fisher, Irving** 18.21**Foreign pensions** 10.53 - 10.54**France**

'quotient familial' 16.16

**Fringe benefits**definition 12.3  
existing treatment 12.5 - 12.11  
frequency 12.13 - 12.14  
market value 12.17  
rules for taxation 12.12  
scheme for taxation 12.16**Gambling losses** 10.62**Gambling winnings** 10.61 - 10.63**Gifts' and inheritances' taxes**agricultural land 34.24 - 34.30  
assets not readily realisable 34.23  
capital acquisition tax 34.6 - 34.9  
donor and donee based taxes 36.13 - 36.28  
equity 4.6  
estate duty 34.9  
exemption threshold 34.35 - 34.39  
fragmentation of holdings 34.31  
historical background 34.4 - 34.5,  
Appendix 28  
inflation 34.47 - 34.48  
justification 34.2 - 34.3  
payment of tax with government securi-  
ties 34.36rate of tax on gifts 34.32 - 34.34  
reform of capital acquisitions tax 38.18  
relief for productive assets 34.16 - 34.22  
reliefs for consanguinity 34.40 - 34.44  
small gifts 34.49  
unit of taxation 34.11 - 34.15**Goods and services**broadly-based taxes 4.15  
narrowly-based taxes 4.14**Government securities**

treatment for capital gains tax 13.54

**Grants, cash**alternative to personal deductions under the  
income tax code 4.4**Griffith Valuation** 32.14**Health contribution** (see Assigned rev-  
enues)**Health expenses** 10.5 - 10.7**Historical cost accounting** 26.6 - 26.14  
advantages 26.13  
disadvantages 26.12**Hobbes, Thomas** 18.6**Housing**differential tax treatment of owned and  
rented 10.4, 10.21  
direct expenditure tax treatment 18.34 -  
18.41  
exemption of owner-occupied from capital  
gains tax 13.57 - 13.58  
government policy 10.24 - 10.28, 11.40  
local authority 10.10, Appendix 7  
owner-occupied, taxation 10.9, 10.12 -  
10.17, 10.19, 10.21 - 10.28  
rented 10.11  
rented, relief for persons aged 65 and over  
10.29  
taxation 10.3 - 10.7**Human capital** 10.86 - 10.87**Incentive of taxation** (see also Disincentive  
of taxation:  
perceptions 2.12 - 2.14**Incidence of taxation**definition 5.1 - 5.3  
effects 5.14 - 5.17  
international experience, Appendix 4**Income**

averaging (see Averaging)

business (see Business income)

comprehensive definition 8.6 - 8.9

**deductions**educational expenses 10.85 - 10.89  
expenditure on residences 10.74 - 10.75  
expenses of travelling to work 10.80 -  
10.84health expenses 10.70 - 10.71  
medical insurance premiums 10.68 -  
10.69permanent health insurance schemes  
10.72 - 10.73Schedule E employee allowances 10.90 -  
10.92Schedule E expenses 10.77 - 10.78  
definition 8.4 - 8.5, 10.7

exempt 10.29 - 10.78

Aosdana payments 10.60

artists 10.55 - 10.59

compensation payments for loss of  
office 10.42 - 10.44compensation payments for physical or  
other injury 10.50 - 10.52

foreign pensions 10.53 - 10.54

gambling winnings 10.61 - 10.63

general exemption limits 16.45 - 16.47

lump-sum retirement benefits 10.45 -  
10.48

redundancy payments 10.29

short-term social welfare benefits 10.30 -  
10.41

sweepstakes and lotteries 10.64 - 10.65

imputed (see Housing, taxation, and Hous-  
ing, government policy)

imputed, taxation 10.3

in-kind 12.1 - 12.2

investment (see Investment income)

maintenance schemes (see also Negative  
income tax) 16.65**Income tax** (see Personal income tax and  
Rate structure, income tax)**Indexation**arguments for 20.13 - 20.15  
budgetary implications 20.34 - 20.35  
changes in terms of trade 20.29 - 20.31  
choice of index 20.17 - 20.24  
Department of Finance views 20.15  
indirect taxes and subsidies, effects 20.25 -  
20.28  
inflationary expectations 20.7  
interest receipts 11.10 - 11.15  
Revenue Commissioners' views 20.15  
suitability of Consumer Price Index 20.23 -  
20.24  
technical problems 20.16 - 20.32  
timing of adjustments 20.32 - 20.33**Individual retirement accounts** 11.60

381

**Industrial Development Authority**  
tax-related lending 30.28

**Inflation**  
adjustment of taxes 38.19  
benefits conferred by delays in payment of tax 7.5  
capital acquisitions tax 7.17  
capital gains tax 7.21  
capital gains treatment 13.26 - 13.29  
determination of business income 7.23  
effect 7.1 - 7.2, 7.4 - 7.24 - 7.25  
fiscal drag 7.6 - 7.8  
impact on definition of tax base 8.9 - 8.13  
investment income 7.22  
pay-related social insurance contributions 7.18  
personal income tax 7.9 - 7.14  
pensions 11.59 - 11.61  
savings 11.7 - 11.15  
specific taxes 7.15 - 7.16  
public finance 20.9 - 20.15  
stamp duties 7.17  
tax base 7.19

**Inheritances** (see Gifts' and inheritances' taxes)

**Institute of Taxation in Ireland**  
advance corporation tax 28.5 - 28.6

**Interest on PAYE tax** 10.93

**Interest receipts**  
indexation 11.10 - 11.15

**International agreements**  
implications for Irish tax system 3.17

**Investment income**  
basis of assessment 33.8  
classification by schedules 33.3 - 33.7  
definition 33.2  
payment of tax 33.9  
rental income 33.6  
surcharge 33.10 - 33.21

**Irish Banks Standing Committee**  
tax-related lending 30.26

**Kaldor, Lord** 18.7  
depreciation 26.58

**Kenny Committee** 14.5 - 14.8

**Life assurance**  
as medium of savings 11.67 - 11.72  
investment of funds 11.71

**Life assurance premiums**  
relief 11.61 - 11.72

**Loan interest**  
tax treatment 11.16 - 11.20  
taxation of gearing gain 11.23 - 11.24

**Losses**  
treatment 13.36 - 13.42

**Lump sum receipts** 38.9

**Lump sum retirement benefits** 10.45 - 10.48

**Mac Naughten, Lord** 8.4

**Meade Committee Report**  
assets, treatment for expenditure tax 18.31 - 18.32  
deferral of capital gains tax 13.59  
direct expenditure tax 18.8  
negative income tax 23.15  
treatment of losses for capital gains tax 13.37

**Medical insurance premiums** 10.68  
10.69

**Mill, John Stuart** 18.6  
investment income surcharge 33.16

**Mortgage**  
direct expenditure tax treatment 18.37  
interest 11.25 - 11.26

**Murphy case** 15.3  
direct expenditure tax structure 15.75  
government's response 15.4  
impact 10.76

**National Economic and Social Council**  
accessions tax 36.17  
negative income tax 23.11

**National savings' scheme**  
investment income from tax treatment 11.73

**Negative income tax**  
background 23.6 - 23.11  
definition 23.3, 23.5  
difficulties 23.16 - 23.17  
National Economic and Social Council report 23.11  
objectives 23.12  
refundable tax credit scheme 23.14  
reverse income tax 23.13  
social dividend 23.15

**Neutrality** (see Efficiency)

**Ó Dálaigh report** (see Commission on Income Taxation)

**Payroll taxes**  
efficiency 4.7  
equity 4.7

**Permanent health insurance schemes**  
10.72 - 10.73

**Personal income tax**  
choice of unit (see Personal taxation, unit of)  
company tax 31.3 - 31.4  
description 9.3 - 9.6  
development 9.9 - 9.17  
efficiency 4.3  
equity 4.2  
progressivity 4.2

**Personal tax allowances and reliefs**  
age allowance 16.25 - 16.27  
blind persons' allowance 16.34 - 16.36  
dependent relative allowance 16.28 - 16.33  
employed person taking care of an incapacitated individual 16.37 - 16.39  
head of household allowance 16.43 - 16.44  
list of personal allowances available 16.2  
living alone allowance 16.40 - 16.42  
married persons' allowance 16.5 - 16.8  
one-parent family allowance 16.23 - 16.24  
purpose of personal allowances 16.58 - 16.60  
widowed persons' allowance 16.9 - 16.12

**Personal taxation, unit of**  
Asprey Committee view 15.10  
Carter Committee view 15.9  
dependants other than children 15.17  
direct expenditure tax 18.62  
extra-legal families 15.18 - 15.19  
income of children 15.14 - 15.16  
present system 15.2 - 15.13

**Private residence** (see Housing)

**Progressivity of taxation**  
definition 18.1  
degree 6.1 - 6.10  
effect on child allowances 16.15  
effect on tax credits 16.52 - 16.57  
effectiveness 6.7  
reduced rate 17.3 - 17.11  
single rate of tax 18.2 - 18.3

**Property taxes**  
equity 4.18

**Rate structure, income tax**  
advantages of single rate 17.13, 18.2  
disadvantages of single rate 18.3

distortions of different rates on different forms of income 18.14 - 18.15  
marginal rates 17.8 - 17.11  
present system 17.2  
reduced rate 17.3 - 17.11, 38.11 - 38.13

**Rates**  
business property 31.43  
land 32.12 - 32.19  
perceived inequity 10.18  
relief on domestic property 10.18

**Reliefs, personal tax** (see Personal tax allowances and reliefs)

**Redundancy payments** 10.49

**Rent**  
control 10.11  
imputed (see Housing, owner-occupied, taxation)

**Report of the Royal Commission on Taxation (Canada)** (see Carter Commission)

**Resource tax** 32.20 - 32.23

**Retirement annuities**  
relief for contributions 11.54 - 11.59, 11.62

**Revenue Commissioners**  
assessments to income tax 17.13  
averaging difficulties 19.29  
capital allowances on second-hand industrial buildings 26.80  
composite rate for building societies 11.35  
current cost accounting 26.33  
development gains taxation 14.14  
direct expenditure tax, assessment and collection 18.51  
direct expenditure tax, feasibility 18.25  
identification of direct expenditure taxpayers 18.27  
indexation 20.15  
indices of stock prices 26.47  
number of taxpayers at marginal rates 17.9  
provision on allowability of losses for capital gains tax 13.40  
restriction of Schedule D expenses 31.21  
roll-over relief for change of residence 13.72  
stock relief 26.42  
submission of income tax returns 18.29

**Roll-over relief** 13.60 - 13.61  
change of residence 13.69 - 13.74

**Royal Commission on the Distribution of Income and Wealth** 36.5

**Royal Commission on Income Tax**  
investment income surcharge 32.12

**Royal Commission on Taxation of Profits and Income**

capital allowances for depreciation 26.59  
disabled persons' allowance 16.35

**Royal Institution of Chartered Surveyors** 14.15

**Savings**

data, Appendix 8  
differential tax treatment 11.4  
economic background, Appendix 8  
efficiency of tax reliefs 11.5-11.6  
inflation effects 11.1  
national schemes (see National savings' schemes)

**Schedule D** see Self-employed

**Schedule E, employee allowance**  
10.90-10.92

**Schedule E expenses** 10.77-10.79

**Self-employed**

amount of tax payable 31.35-31.37  
basis of assessment 31.5-31.11  
deduction of expenses 31.15-31.18  
payment of tax present 31.25-31.29  
period of grace 31.42  
provisional payments of tax 31.30-31.34  
rates on business property 31.43  
rates of interest 31.38-31.41  
restriction of expenses 31.24  
transitional provisions 31.12-31.14

**Shareholders**

discounts 12.15

**Shareholders in Irish companies**

relief 11.41-11.44

**Sheltered activities**

definition 5.11  
determination of prices of services 5.11-5.12

**Short-term social welfare benefits** 10.30-10.41

**Simons H.C.** 8.6, 8.9

**Simplicity**

advantages of direct expenditure tax 18.17  
criterion for tax system 3.10-3.13  
perceptions 2.10  
wealth tax 35.15  
social insurance contributions 21.30-21.31

**Social insurance contributions**

efficiency 21.28-21.29  
equity 21.22-21.27  
evaluation 21.32  
inadequacy of base 21.25-21.26  
incidence 21.16-21.21  
options for reform 21.34  
prospective developments 21.7-21.8  
reform 38.20  
regressivity 21.27  
simplicity 21.30-21.31  
structure 21.5-21.4  
submissions 21.2  
tax or insurance premiums 21.9-21.15  
tax relief 21.39-21.41  
varying rates 21.23-21.24

**Social insurance fund** 21.35

**Social security**

definition 21.3  
description, Appendix 16

**Social security tax** 21.37-21.38

basis of assessment 21.42  
benefits 21.44  
rate of tax 21.43  
reservation, page 310  
tax relief 21.39-21.41

**Society of St Vincent de Paul**

equivalence scales 16.61

**SSAP 16** 26.15, 26.62

depreciation adjustment 26.62  
full text, Appendix 18  
provision for price change in monetary assets and liabilities 26.53-26.56

**Statement of Standard Accounting Practice 16** (see SSAP 16)

**Stock relief** (see Business income)  
proposed system 26.43-26.52

**Stocks** (see Business income)

**Superannuation contributions**

comprehensive income tax 11.51-11.52  
relief 11.46-11.50  
transferability 11.53

**Swedish Commission on Taxation**

direct expenditure tax 18.8  
expenditure, uneven distributions 18.47  
treatment of consumer durables for expenditure tax 18.47

**Sweepstakes and lotteries** 10.64-10.65

**Taxation**

definition 1.4  
distribution (see Distribution of taxation)  
equity (see Equity)  
imputed income (see Income)  
incidence (see Incidence of taxation)  
progressivity (see Progressivity of taxation)  
simplicity (see Simplicity)

**Tax avoidance**

high marginal rates of tax 6.7

**Tax base**

defects 18.10  
definition 8.1  
effect of single rate 17.13  
equity 8.3  
impact of bunching 8.15

**Tax capitalisation**

definition and examples 5.16

**Tax evasion**

high marginal rates of tax 6.7

**Tax expenditures**

definition 3.18  
effects 3.9

**Tax expenditure budget**

introduction 3.21

**Tax revenue**

composition in Ireland 1.24  
international comparisons 1.26-1.28

**Tax shifting** (see Incidence of taxation)

**Tax system**

development 1.7-1.12  
economic background 1.13-1.23  
summary of criticisms contained in submissions 2.1-2.15

**Terms of reference**

interpretation 1.3-1.6

**Travelling to work**

expenses 10.80-10.84

**Trusts**

absolute trusts 37.7  
capital acquisitions tax treatment 37.19-37.24  
capital gains tax treatment 37.13-37.18  
contingent trusts 37.7  
deductions 37.9  
definition 37.2  
discretionary trusts 37.7, 37.22-37.24  
income tax treatment 37.5-37.12  
in favour of children 37.10  
liability to tax 34.11  
settlor 37.14-37.15  
surcharge of trust income 37.11  
taxation of beneficiaries 37.8  
taxation principles 37.3-37.4  
trustees 37.16-37.18

**United Kingdom**

child benefit system 16.17  
progressivity of income tax 18.11

**United States**

proposals for cash flow consumption-based tax 18.8  
self-assessment 31.33

**Unsheltered activities**

definition 5.8  
determination of prices of goods and services 5.9

**Wealth tax**

efficiency 4.17, 35.12-35.14  
equity 4.17, 35.5-35.11  
main provisions of 1975-1977 tax, Appendix 30  
redistributive effects 36.10-36.12  
simplicity 35.15

**Williams, Lady Rhys** 23.15

**Wilson Committee**

disadvantages of equity finance 27.19

**Wrenbury, Lord** 8.4

**Youth Employment Levy** (see Assigned revenues)

## Index to the Second Report of the Commission on Taxation — Direct Taxation — The Role of Incentives

### Absenteeism

incentives to combat 10.57 – 10.61

### Accelerated capital allowances (see also Free depreciation)

energy conservation 10.78 – 10.79  
evaluation 2.23, 5.10, 5.12, 5.15 – 5.17,  
7.9 – 7.22, 7.61, 11.20  
hotels 7.31  
industrial buildings 7.30, 11.18  
multi-storey car parks 11.11  
rented accommodation 11.11

### Accelerated depreciation (see Accelerated capital allowances)

### Added-value (see Value-added)

### Advance corporation tax

primary fund 11.42 – 11.46  
section 84 loans 9.4, 9.19 – 9.21

### Agriculture

capital taxation 10.14, 10.30 – 10.34  
incentives 10.5 – 10.38  
land leasing 10.14, 10.25 – 10.29  
land tax (see Resource tax)  
livestock 10.35 – 10.38, Appendix 8  
transfer of land 10.12 – 10.15, 10.25,  
10.30 – 10.34  
utilisation of land 10.6 – 10.13, 10.24

### Annual allowance

dredging 7.41 – 7.42  
multi-storey car parks 7.36

### Bridges (see Toll roads and bridges)

### Capital

incentives 2.6, 2.14, 2.24, 4.10, 5.15 –  
5.16, 8.3  
taxation 2.19 – 2.20

### Capital allowances

agriculture 10.38  
dredging 7.23, 7.41 – 7.42  
farm buildings 7.23, 7.32 – 7.33  
historical development, Appendix 2  
hotels 7.23, 7.31

lorries and motor vehicles 7.23, 7.27  
machinery and plant 7.23, 7.62 – 7.63,  
11.18  
multi-storey car parks 7.23, 7.36 – 7.37,  
Appendix 2  
patent rights and royalties 7.23, 7.47 –  
7.51  
quarries 7.23, 7.59 – 7.60  
rented accommodation 7.23, 7.52 – 7.58,  
Appendix 2  
research and development 7.23, 7.43 –  
7.46  
ships 7.23, 7.34 – 7.35  
tax-related lending 9.7, 9.9, 9.11, 9.14 –  
9.15  
toll roads and bridges 7.23, 7.38 – 7.40,  
Appendix 2

### Capital gains tax

buildings 7.28  
employee shareholdings 9.28  
present tax system 2.3, 2.8, 2.25  
quarries 7.59  
transfer of land 2.28, 10.30

### Competitiveness

costs 3.7  
economic growth 1.5, 1.14 – 1.18, 2.13  
employment 1.8  
factors affecting 11.9

### Consultative Committee of Accountancy Bodies — Ireland

primary fund 11.40

### Co-operative societies

taxation 6.1, 6.16 – 6.21, Appendix 6

### Córas Tráchtála

export salesmen 10.42

### Corporation tax

advance corporation tax 9.19  
employee shareholdings 9.30 – 9.31  
employment incentive, Appendix 2  
loans to certain farmers 9.22  
manufacturing profits tax 6.11, 11.31,  
Appendix 2  
primary fund 11.39 – 11.46

Shannon relief 6.9 – 6.10  
transitional arrangements for depreciation  
11.25  
woodlands 6.30

### Credits, tax

as incentives 5.10, 5.14, 5.17, 5.19, 5.22  
corporation tax 11.31, 11.39, 11.41, 11.44  
– 11.45  
indexation 2.20  
personal 11.13  
resource tax 10.18 – 10.19  
tax-related lending 9.16

### Department of Agriculture

land leasing 10.27

### Department of Finance

machinery and plant 7.25, 7.62  
tax-related lending 9.3 – 9.4, 9.11

### Depreciation

evaluation of allowances 7.7 – 7.22  
transitional arrangements 11.18, 11.20 –  
11.26

### Direct aids (see also Grants)

future rate 11.3 – 11.6  
incentives 5.20 – 5.31  
market development 11.17

### Dredging

capital allowances 7.23, 7.41 – 7.42

### Efficiency, tax

effects of proposals in first report 2.1,  
2.26, 2.32  
incentives 5.3 – 5.4  
resource tax 10.14 – 10.16

### Employment

abroad 10.46 – 10.51  
agriculture 10.5, 10.16  
disincentives 2.12  
economic development 1.1 – 1.3, 1.7 –  
1.10, 1.13 – 1.19  
effects of proposals in first report 2.32,  
7.6  
exemption of income from stallion fees  
6.24 – 6.25  
incentives 4.6 – 4.7, 4.15, 5.11, 8.1 – 8.12,  
Appendix 2  
leasing 9.10  
manufacturing profits' tax 6.14  
social insurance contributions 2.6, 2.13,  
2.16

### Energy

incentives for conservation 10.78 – 10.79,  
Appendix 3

### Equity

incentives 10.80  
resource tax 10.8, 10.16, 10.18  
salesmen 10.45  
wage/salary earners 10.55

### European Economic Community

competitors 3.6  
export sales' relief 6.3  
farm modernisation scheme, Appendix 3  
forestry 6.33  
incentives 5.9, 5.23, Appendix 4  
interest subsidy schemes, Appendix 3  
manufacturing profits' tax 11.32  
research and development 7.44  
tax-related lending 9.11

### Exchange rate

competitiveness 3.7, 3.12, 11.8  
incentives 3.11

### Export sales' relief

assessment 5.15, 5.23, 5.27, 6.1 – 6.7  
description, Appendix 5  
dividends 6.8, 11.32 – 11.33  
EEC, Appendix 4  
films 10.70  
future 11.27, 11.29  
historical development 5.11, 6.11,  
Appendix 2  
Shannon relief 6.10  
tax-related lending 9.17, 9.19

### Farm buildings

capital allowances 7.23, 7.32 – 7.33

### Film industry

incentives 10.69 – 10.75

### Foreign employment (see also Salesmen)

taxation 10.46 – 10.51

### Foreign workers

tax incentives 2.12, 11.12 – 11.14

### Free depreciation

analysis 7.11 – 7.22  
effect 2.6  
farmers, Appendix 2  
hotels 7.31, Appendix 2  
industrial buildings, Appendix 2  
leasing 9.14  
machinery and plant 7.24, 11.18, Appen-  
dix 2  
phased withdrawal 11.20 – 11.26

### Gifts' and inheritances' tax

agriculture 10.30, 10.33 – 10.34  
effects of proposals in first report 2.7, 2.28

**Grants**

- capital allowances 7.61 - 7.63, 11.18
- capital equipment 4.4
- effect 2.6
- employment schemes 8.11
- hotels 7.31
- incentives 5.20 - 5.31
- leasing 9.7 - 9.8, 9.11, 9.14
- livestock, Appendix 8
- multi-storey car parks 7.37
- outline of available grants, Appendix 3
- overseas sales' personnel 10.44

**Hotels**

- capital allowances 7.23, 7.31, 11.18

**Incidence, tax**

- incentives 4.1 - 4.15

**Income tax**

- absenteeism 10.57 - 10.61
- company 2.26, 2.27, 6.15
- co-operatives 6.21
- defects of present system 2.2 - 2.5, 2.8, 2.9
- dividends 11.31 - 11.38
- employee shareholdings 9.27 - 9.33
- farmers 6.18, 10.8, 10.11, 10.19
- indexation 2.21 - 2.22
- marginal tax rates 2.5, 2.11, 2.12, 2.22, 10.43 - 10.44, 10.56, 10.61
- patents 7.49 - 7.51
- proposals in first report 2.7, 2.9 - 2.12, 2.22, 2.31
- research and development 7.46
- resource tax 10.18
- stallion owners 6.22 - 6.23
- woodlands 6.30 - 6.35

**Industrial buildings**

- capital allowances 7.23, 7.28 - 7.30, 7.64, 11.18, Appendix 2
- energy conservation 10.78

**Industrial Development Authority**

- export sales' relief 6.2 - 6.3
- grant schemes, Appendix 3, Appendix 4
- leasing 9.8
- Shannon relief 6.9

**Initial allowance**

- capital allowances 7.61 - 7.65
- dredging 7.41
- industrial buildings 7.64 - 7.65
- machinery and plant 7.64 - 7.65, 11.18, Appendix 2
- multi-storey car parks 7.36
- ships 7.34, Appendix 2

**Institute of Taxation in Ireland**

- primary fund 11.41

**Interest**

- loans to farmers 9.22
- subsidies 5.20, 11.6, Appendix 3
- tax deduction 2.24, 2.27
- tax-related lending 9.18

**Inventors**

- incentives 10.67 - 10.68

**Investment** (see Venture capital)

- accelerated capital allowances 11.17
- depreciation 11.22, 11.29
- economic growth 1.4
- efficiency 2.26, 7.4
- export sales' relief 6.4, 6.7
- forestry 6.31 - 6.32, 6.34
- incentives 4.4 - 4.8, 5.10 - 5.11, 5.23 - 5.24, 11.2, 11.25
- Ireland 7.1 - 7.6
- manufacturing profits' tax 6.12
- risk 2.3 - 2.4
- tax neutrality 2.32

**Investment allowance**

- evaluation 5.12, 5.15, 5.17
- machinery and plant 10.78
- ships 7.34 - 7.35

**Irish Bloodstock Breeders' Association**

- stallions 6.24

**Labour**

- substitution 4.10, 8.3
- taxation 2.6, 2.14
- tax exemptions 5.15

**Land leasing** (see Agriculture)**Land tax** (see Resource tax)**Land transfer** (see Agriculture)**Livestock** (see Agriculture)**Loans to certain farmers** (see Tax-related lending)**Lorries and motor vehicles**

- capital allowances 7.23, 7.27

**Machinery and plant**

- capital allowances 7.11, 7.17 - 7.18, 7.23 - 7.26, 7.62 - 7.64, 8.3, 9.14, 10.78, 11.18, Appendix 2

**Manufacturing profits' tax**

- dividends 11.31 - 11.38
- employment incentive 8.7
- future 6.1, 6.11 - 6.15, 11.27 - 11.29
- history 5.11, Appendix 2, Appendix 5
- incidence 4.4

- primary fund 11.39, 11.41
- selectivity 5.23, 5.28
- tax-related lending 9.19
- tourism 10.76

**Market development** 11.17**Minister for Finance**

- accelerated depreciation 7.12 - 7.14

**Motor vehicles** (see Lorries and motor vehicles)**Multi-storey car parks**

- capital allowances 7.23, 7.36 - 7.37, 11.11

**National Board for Science and Technology**

- inventors 10.67
- research and development 7.45

**National Economic and Social Council**

- woodlands 6.33

**Neutrality, tax**

- efficiency 2.32, 5.3
- retained and distributed profits 2.26, 9.20, 11.34 - 11.35

**Normal depreciation**

- analysis 7.15 - 7.22
- hotels 7.31, 11.18
- industrial buildings 7.30, 11.18
- machinery and plant 7.24 - 7.26, 11.18
- tax-related lending 9.14
- transition 11.20 - 11.26

**Patent rights and royalties**

- capital allowances 7.23, 7.47 - 7.51, 11.18, Appendix 2

**Plant** (see Machinery and plant)**Primary fund** 6.15, 11.39 - 11.47**Productivity**

- competitiveness 3.7, 4.7, 11.9
- earnings 10.52 - 10.56
- economic development 1.1 - 1.2, 1.7 - 1.9
- leasing 9.10

**Profit**

- definition 6.21
- distributed 2.7, 2.26, 9.20, 11.31 - 11.36
- effect of depreciation allowances 7.16
- export sales' relief 6.2
- relief 4.2, 4.4, 4.10
- retained 2.7, 2.26, 9.20, 11.31, 11.33 - 11.36

**Profit-sharing schemes** 9.1, 9.27 - 9.32, 10.2, 11.11, Appendix 2**Quarries**

- capital allowances 7.23, 7.59 - 7.60

**Rate of return**

- agriculture 10.6
- incentives 3.10, 4.5, 4.9 - 4.10
- savings 4.13 - 4.14
- state investments 11.3

**Rented accommodation**

- capital allowances 7.23, 7.52 - 7.58, 11.11

**Research and development**

- capital allowances 7.23, 7.43 - 7.46, 7.66
- grants, Appendix 3
- special allowance 5.13

**Resource tax**

- agricultural 10.6, 10.8 - 10.11, 10.14, 10.16 - 10.24
- definition 10.4

**Revenue Commissioners**

- absenteeism 10.59
- capital allowances 7.24
- employees working abroad 10.46, 10.48
- direct expenditure tax 11.13
- film industry 10.70
- free depreciation 5.17, 7.19
- manufacturing profits' tax 11.32
- patent rights 7.50
- primary fund 11.42, 11.45
- stamp duty on agricultural land 10.32
- taxation of profits 11.34
- tax-related lending 9.3, 9.11

**Salesmen**

- earnings from work done abroad 10.39 - 10.45
- recruitment grants, Appendix 10

**Savings**

- economic growth 1.4
- incentives 4.13 - 4.14, Appendix 2
- taxation 2.4, 2.7, 2.17 - 2.19, 2.28, 2.32, 7.6

**Section 84 loans** (see tax-related lending)**Selectivity**

- incentives 5.3 - 5.6, 5.31

**Shannon relief**

- future 6.9 - 6.11, 11.29
- history, Appendix 5
- tax-related lending 9.19

**Sheltered sector**

definition 1.5  
 employment 1.7-1.8  
 incentives 4.3, 4.8, 4.11, 4.15, 7.58

**Ships**

capital allowances 7.23, 7.34 - 7.35,  
 Appendix 2

**Social insurance**

employers' contributions 6.15, 8.7, 11.30  
 employment 2.6, 2.14 - 2.16, 8.1, 8.5

**Social security tax** 2.7, 2.13, 7.6, 11.28

**Stallion fees**

exemption of income 4.4, 6.1, 6.22-6.29

**Stock relief** 2.23, Appendix 2

agriculture 10.36 - 10.37

**Subsidy**

capital investment 7.63  
 construction industry 7.58  
 employment 8.2  
 housing 9.25 - 9.26  
 interest 5.20, 9.15, 9.21, 11.6, Appendix 3  
 labour 5.20, 8.3  
 livestock, Appendix 8  
 wage 8.7

**Tax avoidance**

co-operative societies 6.18  
 export sales' relief 6.6  
 present tax system 2.2 - 2.3, 2.8  
 tax-related lending 9.3  
 venture capital 11.16

**Tax evasion**

high marginal tax rates 2.5, 2.9, 2.11, 2.22

**Tax exemptions**

co-operative societies 6.16 - 6.17, 6.20  
 evaluation 5.15, 5.18, 5.31  
 inventors 10.67 - 10.68  
 role 5.11  
 stallions 6.1, 6.22 - 6.29, Appendix 2  
 woodlands 6.1, 6.30, Appendix 2

**Tax-related lending**

evaluation 5.25, 9.1 - 9.26  
 history, Appendix 2  
 housing purchase loans 9.2, 9.25 - 9.26  
 incentive for capital 2.6, 4.4  
 incidence 4.11  
 leasing 9.2 - 9.3, 9.7 - 9.15, Appendix 2  
 loans to farmers 9.2, 9.22 - 9.24  
 preference share financing 9.2, 9.16 - 9.21, Appendix 2  
 section 84 loans 9.2 - 9.4, 9.17 - 9.21, 11.46, Appendix 2

**Toll roads and bridges**

capital allowances 7.23, 7.38 - 7.40

**Tourism**

incentives 10.76 - 10.77

**Unsheltered sector**

definition 1.5  
 incentives 1.6, 1.8, 4.3, 4.7, 4.15

**Value-added**

economic growth 1.1 - 1.3, 1.7 - 1.8, 11.4  
 incentives 5.11, 6.14, 8.4

**Venture capital**

investment incentive 10.62 - 10.66, 11.15 - 11.16  
 United Kingdom, Appendix 12  
 United States, Appendix 11

**Woodlands**

taxation of profits 4.4, 6.1, 6.30 - 6.35

**Index to the Third Report of the Commission on Taxation — Indirect Taxation****Agricultural Levies**

definition 2.12 - 2.15  
 EEC CAP 2.14 - 2.15  
 MCAs 2.14

**Alcohol**

abuse 8.3, 8.7 - 8.12  
 beer (see Beer)  
 cider (see Cider and perry)  
 costs of abuse 8.7 - 8.12, Appendix 13  
 cross-border smuggling 8.16 - 8.19  
 excise duties 8.1 - 8.46, Appendix 12  
 EEC harmonisation 6.31 - 6.34  
 efficiency 8.5 - 8.14  
 equity 8.4  
 justification 8.3 - 8.19  
 other countries 8.15 - 8.18  
 present system 8.2  
 rate differentiation 8.20 - 8.45  
 home-made alcohol (see Home-made alcohol)  
 road traffic accidents 8.10 - 8.11  
 small brewers 8.31  
 spirits (see Spirits)

**Alumina**

excise duty 12.18

**Animal food stuff**

VAT 5.48

**Animal medicine**

VAT 5.48

**Balance of payments**

consideration 6.14 - 6.17

**Banks**

stamp duty (levy) 13.40

**Beer**

excise duty 8.28 - 8.30, Appendix 12

**Betting and gambling**

excise duties 11.7 - 11.20  
 card games 11.10  
 evasion 11.11 - 11.16  
 football pools 11.10  
 games of chance 11.10

gaming premises and machines 11.19  
 justification 11.7 - 11.8  
 on/off course betting 11.17 - 11.18  
 present system 11.9 - 11.19  
 history of taxes and levies, Appendix 21  
 EEC Sixth Council Directive 11.8  
 reports 11.2 - 11.3  
 social costs 11.5 - 11.6  
 suppression 11.4

**Birth/marriage/death certificates** (see Miscellaneous fees)**Books**

EEC Sixth Council Directive 5.46  
 VAT 5.45 - 5.47

**Bord Fáilte**

foreign tourism revenue 5.86

**Broadcasting licence fees** (see Miscellaneous fees)**Broadly-based taxes**

multi-stage 2.5 - 2.6  
 single-stage 2.4

**Building and associated services**

VAT 5.57 - 5.67

**Business charges** (see Miscellaneous Fees)**Business expenses**

input tax 5.90 - 5.96

**Cascade taxes** (see Broadly-based taxes)**Censorship of Films Act**

stamp duty on fees 13.43

**Cheques and bills of exchange**

stamp duties 13.32 - 13.33

**Cider and perry**

excise duties, Appendix 12

**Cigarettes** (see also Tobacco)

EEC system of excise duty 6.31 - 6.33

- Clothes' dryers**  
case for excise duty 12.5
- Clothing and footwear**  
VAT 5.37 - 5.38, Appendix 5  
expenditure, Appendix 9
- Common Agricultural Policy (CAP)** 2.14  
- 2.15, Appendix 4
- Companies' capital duty**  
stamp duty 13.27 - 13.31
- Companies' registration fees**  
stamp duty 13.43
- Construction Industry Federation**  
stamp duty 13.7 - 13.14
- Consular service fees**  
stamp duty 13.43
- Conveyances**  
stamp duty 13.21 - 13.22
- Córas Iompair Éireann**  
VAT 5.77 - 5.80
- Court fees**  
stamp duty 13.43
- Credit cards and charge cards**  
stamp duty 13.34 - 13.36
- Customs' duties**  
definition 2.11  
origins, Appendix 1
- Deep freezers**  
case for excise duty 12.5
- Department of the Environment, the**  
motor vehicle duties 10.36
- Department of Finance, the**  
adjustment of excise duties for inflation 7.14
- Direct taxes**  
structural changes 1.14 - 1.15
- Dishwashers**  
case for excise duty 12.5
- Dog licences**  
excise duty 2.8, Appendix 3
- Domestic heating oil**  
excise duty 12.25 - 12.26
- Drinks' industry**  
economic importance 8.13-8.14, Appendix 14  
taxation of alcohol 8.16
- Drinks' Industry Group** 8.13  
cross-border smuggling of alcohol 8.16  
home-made alcohol 8.42
- Driving licences** (see Miscellaneous fees)
- EEC**  
Common Agricultural Policy (see Common Agricultural Policy)  
Council of Ministers 4.13  
General Agreement on Tariffs and Trade 4.15  
own resources (see VAT, own resources)  
Sixth Council Directive (see Sixth Council Directive)  
Treaty of Rome (see Treaty of Rome)  
Twelfth Council Directive 5.94 - 5.96  
value-added tax 4.12 - 4.17, 4.32 - 4.35
- EEC Commission**  
harmonisation of stamp duties 13.17  
harmonisation of tax systems 6.31  
transition to single rate of VAT 14.6
- Electrical Industries' Federation of Ireland**  
illegal importation of televisions 12.9
- Electricity**  
expenditure, Appendix 9  
VAT 5.42 - 5.44
- Electricity Supply Board**  
Bord na Móna 5.44  
EEC grants 5.44  
fuel oil 12.18, 12.12 - 12.23  
Irish National Petroleum Corporation 5.944  
National Prices' Commission 5.44  
taxation 5.43 - 5.44
- Excise duties**  
*ad valorem* rate 2.9, 6.3, 7.2 - 7.5  
adjustment for inflation 7.6 - 7.15  
definition 2.8 - 2.9  
efficiency 6.26 - 6.27  
equity 6.24 - 6.25  
importance, Appendix 11 - Annex 2  
imported goods, Appendix 11  
justification 6.10 - 6.22  
methods of collection, Appendix 11  
miscellaneous fees 2.17 - 2.18, Appendix 3  
periods of deferment, Appendix 11 - Annex 3  
rates as at February, 1984, Appendix 11 - Annex 1

- reduction of present level 14.2 - 14.14  
revenue aspects 6.7 - 6.9  
specific rate 2.9, 6.3, 7.2 - 7.5  
simplicity 6.28 - 6.30  
structural changes 1.17 - 1.18  
system 6.2 - 6.6, Appendix 11

- Farmers**  
VAT 5.48 - 5.56, Appendix 5

- Fee stamps** 13.43 - 13.44

- Fertilisers**  
VAT 5.48

- Film censorship** (see Miscellaneous fees)

- Fishermen**  
VAT, Appendix 5

- Fixtures and fittings**  
VAT 5.66

- Food**  
VAT 5.35 - 5.36, Appendix 5  
expenditure, Appendix 9

- Footwear** (see Clothing and footwear)

- Foreign tourism**  
revenue 5.86 - 5.89

- Foreign travel**  
taxation 12.15 - 12.17

- Forklift trucks**  
motor vehicle duties 10.28, Appendix 20

- Fuel oil**  
excise duty 12.18 - 12.24

- Gambling** (See Betting and gambling)

- Gaming licences**  
excise duty 2.8

- Goods vehicles**  
Motor vehicle duties 10.37 - 10.39, Appendix 20

- Gramophone records**  
excise duty 12.2 - 12.11

- Greyhounds**  
betting duty 11.18  
VAT exemption on supply 5.75

- Home-made alcohol**  
excise duty 8.37 - 8.43

- Horses**  
VAT exemption on supply 5.75

- Household expenditure**  
analysis of goods and services, Appendix 9

- Hydrocarbon oil**  
excise duty, Appendix 18  
excise duty on oils not used in road vehicles 12.18 - 12.26  
transport 10.8 - 10.19  
VAT, Appendix 5

- Indirect taxation**  
administrative costs 3.10  
compliance costs 3.10  
definition 1.2  
efficiency 3.3 - 3.9  
equity 3.2  
international constraints 3.11 - 3.13  
justification 1.3 - 1.11  
simplicity 3.10  
structural changes 1.12 - 1.19

- Industrial oil**  
excise duty 12.20 - 12.24

- Inspection fees** (See Miscellaneous fees)

- Insurance transactions**  
stamp duty 13.41 - 13.42

- International System of Tax Classification,** Appendix 2

- Irish Hospitals' Sweepstakes**  
stamp duty 13.18 - 13.39

- Irish National Bookmakers' Association,**  
evasion of betting duty 11.11

- Irish Tobacco Industry,** Appendix 17

- Irish Tobacco Manufacturers**  
Joint Committee of the Secondary Legislation of the European Communities 6.33

- Irish Tobacco Manufacturers' Advisory Committee**  
social costs of smoking 9.10

- Law Society of Ireland**  
stamp duty 13.8 - 13.9

- Life insurance**  
stamp duty on policies 13.37

- Liquefied petroleum gas (LPG)** 10.8 - 10.9, 10.16 - 10.17

- Luxury goods**  
case for higher VAT rates 5.27, 6.18 - 6.20

**Matches and mechanical lighters**

excise duty 12.12 - 12.14

**Mineral oils**

EEC harmonisation of excise duties 6.34

**Minister for Finance**

bloodstock and greyhound industries 5.75

farming inputs 5.50

foreign travel 12.15

hydrocarbon oil 12.19

video players 6.13

**Miscellaneous fees** 2.17 - 2.18**Monetary Compensatory Amounts (MCAs)**

definition 2.14

development, Appendix 4

effects, Appendix 4

**Money lending**

excise duty 2.8

**Motor cycles**

excise duty, Appendix 19

motor vehicle duties, 10.30-10.36, Appendix 20

**Motor vehicles**

excise duty, Appendix 19

**Motor vehicles duties, Appendix 20**

definition 2.10

origins, Appendix 1

**Multi-stage taxes** (see Broadly-based taxes)**Narrowly-based taxes**

types 2.7-2.18

**National Prices' Commission**

electricity 5.44

**Oral medicine**

expenditure, Appendix 9

VAT 5.39 - 5.41

**Passenger transport**

expenditure, Appendix 9

VAT exemption 5.77 - 5.83

**Passports**

stamp duty 13.43

**Plants and seeds**

VAT 5.48

**Pollution**

taxation 6.12

394

**'Prefrick', the** 13.25**Private cars**

excise duty 10.21 - 10.23, Appendix 19

motor vehicle duties 10.27-10.46, Appendix 20

**Promissory notes**

stamp duty 13.32 - 13.33

**Property taxes**

structural changes 1.15 - 1.19

**Public records' fees**

stamp duty 13.43

**Public Service vehicles**

motor vehicle duties 10.40

**Racing Board, the**

evasion of betting duty 11.12

**Radio Telefís Éireann**

broadcasting licence fees 2.17

**Rates**

origins, Appendix 1

**Refrigerators**

case for excise duty 12.5

**Rented accommodation**

Sixth Council Directive 5.68

VAT 5.68 - 5.70

**Revenue Commissioners, the**

alcohol 8.21 - 8.23

beer 8.29

betting duty 11.13

inflation 7.14

perfume 8.34

single rate of VAT 14.5

stamp duties 13.10

tobacco products 9.7

VAT 5.3, 5.9, 5.21, 5.40

**Sales tax, Appendix 8****Searches** (see Miscellaneous fees)**Seed and plants**

VAT 5.48

**Single stage taxes** (see Broadly-based taxes)**Sixth EEC Council Directive**

books (see Books)

cheques and bills of exchange 13.32 - 13.33

description 4.17

impact in Ireland 4.33 - 4.35

rented accommodation (see Rented accommodation)

restrictions and limitations for Ireland 5.71 - 5.84

transitional provisions, Appendix 6

**Small brewers**

rebate of excise duty 8.31

**Smuggling**

alcohol 8.16 - 8.19

fuel 10.11

televisions 12.6 - 12.9

**Spirits**

excise duty 8.32 - 8.36, Appendix 12

**Sporting events**

VAT exemption on admission 5.74

**Stamp duties**

abolition 14.15 - 14.21

administrative costs 13.10

background 13.2

case 13.3

compliance costs 13.11

definition 2.16

EEC 13.17

efficiency 13.14 - 13.16

equity 13.12 - 13.13

future 13.18

incidence 13.5 - 13.6

origins, Appendix 1

present system 13.19 - 13.20, Appendix 22

receipts, Appendix 23

**Stocks and shares**

stamp duty 13.23 - 13.26

**Table waters**

excise duty 8.44 - 8.45

**Taxis**

motor vehicle duties 10.28, Appendix 20

**Telecommunications' services**

household expenditure, Appendix 9

VAT exemption 5.76

**Telephones**

case for excise duty 12.5

**Televisions**

cross-border smuggling 12.6 - 12.9

excise duty 12.2 - 12.11

**Tobacco**

excise duty 9.1 - 9.25, Appendix 16

efficiency 9.6 - 9.10

equity 9.5

justification 9.3 - 9.13

other countries 9.11 - 9.12

present system 9.2, Appendix 16

rate differentiation 9.14 - 9.24

health consequences of smoking 9.4

growth of smoking, Appendix 15

social costs of smoking 9.6 - 9.7

**Tobacco Industry**

economic importance 9.8 - 9.10

**Tourism**

purchase of goods, Appendix 10

**Tractors**

motor vehicle duties 10.98

**Transport**

excise duty 10.1 - 10.51, Appendix 19

revenue collected 10.2

justification of special rate 10.3 - 10.7

first registration fees, Appendix 20

goods' vehicles 10.24

hydrocarbon oil (see Hydrocarbon oil)

lead in petrol 10.18

liquefied petroleum gas (see Liquefied Petroleum Gas)

motor vehicle duties (road tax) 10.27 - 10.46, Appendix 20

exempt vehicles 10.41 - 10.46

forklift trucks (see Forklift trucks)

goods' vehicles (see Goods' vehicles)

motor cycles (see Motor cycles)

private cars (see Private cars)

public service vehicles (see Public Service vehicles)

taxis (see Taxis)

parts and accessories 10.25 - 10.26

rebates for fuel used in passenger service 10.19

Road Fund 10.47 - 10.50

smuggling of fuel 10.11

vehicles used by invalids 10.42 - 10.46

**Travel agents**

journeys within the EEC 5.84

**Treaty of Rome**

Article 95, 6.35

**Tyres**

excise duty, Appendix 19

**United Nations' System of National Accounts** 2.18**Vacuum Cleaners**

case for excise duty 12.5

395

**Value-added tax**

administrative costs, Appendix 5  
 advantages 4.18 – 4.23  
 base-from-base method 4.7 – 4.8  
 books (see Books)  
 broadening of tax base 5.31 – 5.97  
 changes since introduction, Appendix 5 – Annex 1  
 clothing and footwear (see Clothing and footwear)  
 comparison with sales tax 4.25 – 4.31  
 compliance costs 5.5 – 5.9  
 definition 4.2  
 development, Appendix 5  
 EEC (see EEC)  
 efficiency 5.29 – 5.30  
 equity 5.13 – 5.28  
 consumption 5.14 – 5.17  
 higher rate 5.27 – 5.28  
 negative income tax 5.25  
 single rate 5.14  
 zero rate 5.22 – 5.26  
 evasion 4.21 – 4.23  
 evolution, Appendix 5  
 exemption 5.29 – 5.34  
 expenditure at present rates 14.3  
 farmers (see Farmers)  
 fisherman (see Fishermen)  
 food (see Food)

future 4.32  
 incidence 5.18 – 5.21  
 inequities and anomalies 5.9 – 5.12  
 inflation 4.24  
 methods 4.3 – 4.6  
 operation 4.7 – 4.11  
 oral medicine (see Oral medicine)  
 own resources, Appendix 7, Appendix 7 – Annex 1  
 present system, Appendix 5  
 rate structure 5.4 – 5.12  
 tax-from-tax method 4.9 – 4.10  
 transition to single rate 14.5 – 14.11  
 zero-rating 5.32 – 5.34

**Veterinary surgeons**

VAT 5.48

**Video players**

excise duty 6.13, 12.2 – 12.11

**Visas**

stamp duty 13.43

**Washing machines**

case for excise duty 12.5

**Wine**

excise duty, Appendix 12

**Index to the Fourth Report of the Commission on Taxation — Special Taxation****Administrative costs**

environmental taxes 7.23 – 7.28  
 local income tax 3.15

**Agricultural land**

farm tax 5.27 – 5.28  
 local property tax 5.26 – 5.31  
 rates 5.26

**Charges for specific services**

imposition of 1.1, 1.20 – 1.24

**Charitable donations**

taxation 9.23 – 9.30

**Charities**

capital acquisitions tax 9.7, 9.24, 9.28  
 capital gains tax 9.8  
 covenants 9.10 – 9.12  
 definition 9.3 – 9.4, 9.20 – 9.22  
 income tax 9.5 – 9.6, 9.24 – 9.28  
 indirect taxes 9.9, 9.17, 9.36 – 9.38  
 investment income 9.35  
 size of charity sector 9.2  
 taxation of charitable donations 9.23 – 9.30  
 tax credit on dividends 9.18  
 trading income 9.31 – 9.34

**Compliance costs**

local income tax 3.15  
 local motor vehicle duties 4.9

**Covenants**

charitable purposes 9.10 – 9.12, 9.16

**Department of the Environment, the**

equalisation of local taxes 1.18  
 level of local taxation 1.9  
 local motor vehicle duties 4.8  
 pollution charges 7.22  
 unit of local taxation 1.13

**Derelict sites**

taxation 7.27 – 7.28

**Efficiency**

local taxation 1.12  
 property taxes 5.24

**Environment**

taxation 7.1 – 7.29

**Equity**

local taxation 1.11  
 property taxes 5.5 – 5.8, 5.28

**Expenditure tax**

charitable donations 9.29 – 9.30

**Externalities**

taxation 7.2 – 7.8, 7.13

**Farm tax**

5.27 – 5.28

**Gas**

royalties 8.9  
 taxation 8.7, 8.12

**Grants**

central government 1.1, 1.16 – 1.19, 1.24  
 level 2.2 – 2.3

**Industrial and commercial property**

local property tax 5.22 – 5.25  
 rates 2.3, 5.22

**Local authorities**

accountability 1.15  
 central government grants 1.16 – 1.17  
 charges 1.21  
 income 2.3  
 local motor vehicle duties 4.7  
 local sales tax 4.2 – 4.3, 4.5  
 services 1.5 – 1.7  
 valuations 5.15

**Local government**

reasons for 1.2  
 revenue 1.9, 2.10, 5.43

**Local income tax**

administration 3.2 – 3.5  
 company profits 3.19  
 investment income 3.17 – 3.18  
 PAYE 3.20 – 3.21  
 residence 3.11 – 3.16  
 types 3.6 – 3.9

**Local indirect tax**

motor vehicle duties 4.7-4.9  
sales tax 4.1-4.6

**Local property tax**

historical background 5.2-5.6  
industrial and commercial property 5.22  
- 5.25  
justification 5.7-5.9  
land 5.26-5.31  
liability 5.33  
mortgage interest 5.17-5.19  
national property tax 6.1, 6.15  
payment 5.34-5.36  
real property 5.32  
relief for low incomes 5.37-5.42  
rented residential property, 5.20-5.21  
valuations 5.11-5.16

**Local taxation**

case for 1.1, 1.3-1.8, 1.24  
criteria 1.10-1.15  
level 2.4-2.10  
share of gross domestic product 5.44

**Mineral development**

off-shore operations 8.7-8.38  
on-shore operations 8.39-8.41

**Mortgage interest**

local property tax 5.17-5.19  
residential property tax 6.4-6.5

**Natural resources**

development 8.1-8.2, 8.5-8.6  
taxation 8.3-8.4

**Oil**

1985 policy statement 8.11  
royalties 8.8-8.9  
taxation 8.7, 8.12

**Pollution**

control 7.12-7.13  
taxation 7.14-7.23

**Rates**

agricultural land 2.3, 5.26  
criticisms 5.3-5.4, 5.34  
historical background 5.2  
industrial and commercial property 2.3,  
5.22  
local authority tenants 5.21  
mortgage interest 5.17

**Rented residential property**

local property tax 5.20-5.21

**Residential property tax**

criticisms 6.4-6.13  
introduction 5.2  
mortgage interest 5.17  
valuations 5.14

**Ring fence**

off-shore mineral development 8.13 -  
8.23, 8.43

**Royalties**

basis 8.28-8.36  
corporation tax 8.38  
natural resources 8.1-8.4, 8.26-8.27,  
8.47  
1985 policy statement 8.11  
1975 policy statement 8.8-8.10  
rate structure 8.37

**Waiver schemes**

local property tax 5.37-5.42

**Index to the Fifth Report of the Commission on Taxation — Tax Administration****Administrative Costs**

informing taxpayers 1.4  
staff training 1.4

**Appeals**

against assessment 4.3-4.16, 7.2  
Appeal Commissioners 4.15, 7.3-7.4, 7.14  
backlog 4.8-4.11  
to court 7.5-7.12  
*in camera* 7.11-7.12  
legislation 4.12, 4.16  
numbers 4.7  
rights of taxpayers 7.13-7.14

**Appeals procedure**

inadequacies 1.15

**Assessment procedures**

appeals (see Appeals)  
existing system 4.3-4.6  
self-assessment (see Self-assessment)

**Capital gains and capital acquisitions**

collection procedures, Appendix 5  
self-assessment 4.63-4.67, 6.30  
withholding tax 5.26-5.32

**Central Bank of Ireland**

information powers of the Revenue Com-  
missioners 12.47, 12.51

**Compliance costs**

collection agents 1.4, 1.10, 1.13  
compensation 8.7  
effects of Commission's proposals 8.3-  
8.6  
financial costs 8.8-8.11  
information returns 12.59  
VAT 8.9  
United Kingdom (see United Kingdom)

**Construction Industry Federation**

tax deduction scheme 5.33-5.42, Appen-  
dix 1

**Corporation tax**

collection procedures, Appendix 6  
maintenance and preservation of records,  
Appendix 4

**County registrars/sheriffs**

Department of Justice (see Department of Jus-  
tice)  
duties and description 15.28, Appendix 7  
enforcement of estimated certificates  
15.31-15.33  
level of tax collection 15.29-15.33  
Minister for Finance (see Minister for Finance-  
Revenue Commissioners (see Revenue Com-  
missioners))  
summary distraint 15.24, 15.51

**Customs and excise duties**

appeal procedures 19.11-19.19  
customs clearance procedures 19.20-  
19.28  
enforcement and penalties 19.29-19.47,  
Appendix 12  
legislation 19.6-19.10, Appendix 11  
organisation and procedures, Appendix 10  
periods of deferment, Appendix 10-Annex 1  
United Kingdom (see United Kingdom)

**Department of Finance, the**

communication with the Revenue Com-  
missioners 1.16  
direct expenditure tax 17.11  
legislation 2.6-2.7  
mobility of staff with the Revenue Com-  
missioners (see Staff mobility)  
technical advisory committee on legis-  
lation 2.17

**Department of Justice, the**

enforcement proceedings 15.36

**Department of the Public Service, the**

Board of the Revenue Commissioners  
3.30  
central enquiry office 8.16  
staff mobility 2.23

**Direct expenditure tax**

(See Tax, direct expenditure)

**Director of Public Prosecutions, the**

criminal offences relating to taxation  
14.36

**Finance bills**

establishment of technical finance bills 2.12

**Income distribution effects of Commission's proposals**

equity 21.21 - 21.27  
incidence 21.19 - 21.20

**Information powers of the Revenue Commissioners**

banks, building societies 12.44 - 12.55  
compliance costs 12.59  
construction industry sub-contractors' scheme 12.13  
corporation tax 12.5 - 12.12  
income tax 12.5 - 12.12  
insurance companies 12.56  
international exchange of information 12.60 - 12.62

Minister for Finance (see Minister for Finance)  
obligation to keep records 12.63 - 12.68  
PAYE 12.13

power of entry inspection of records 12.16 - 12.26

power to obtain information about named taxpayers 12.36 - 12.40

power to obtain information about tax avoidance 12.41 - 12.43

power to search persons 12.32 - 12.35  
power to search premises 12.10, 12.27 - 12.31

principles 12.2 - 12.3

scope 12.4

**Institute of Freight Forwarders of Ireland**

VAT on imports 18.37

**Institute of Taxation**

Revenue preference in tax debts 16.19  
self-assessment 4.36

**Irish Buildings Societies' Association**

information powers of the Revenue Commissioners 12.52

**Irish Congress of Trade Unions**

tax avoidance 11.22

**Irish Institute of Credit Management**

Revenue preference in tax debts 16.9, 16.18

**Irish Tax Officials' Union**

central enquiry office 8.16  
self-assessment 4.38

**Joint Oireachtas Committee on Fiscal Affairs**

2.15, 3.20

**Judiciary**

Revenue practice on members' expenses 3.21 - 3.26

**Legislation**

clarity 1.13  
dissatisfaction 2.4 - 2.10  
improving 2.11 - 2.27  
advance publication of draft legislation 2.14  
appointment of Joint Oireachtas Committee on Fiscal Affairs 2.15  
consolidation of existing legislation 2.25 - 2.27  
permanent review body 2.21 - 2.22  
staff mobility 2.23 - 2.24  
technical advisory committee 2.16 - 2.20  
technical finance bill 2.12 - 2.13  
initial appearance 2.2 - 2.3

**Minister for Finance**

county registrars/sheriffs 15.37  
powers to search premises 12.10  
tax avoidance 11.5 - 11.7  
tax evasion 10.4 - 10.12

**Motor vehicle duties**

collection by An Post 20.13 - 20.16  
costs of present administration 20.4  
evasion 20.17 - 20.26  
linkage with insurance premiums 20.5 - 20.12  
number of rates 20.3

**Office of the Collector General**

15.17 - 15.20

**Oireachtas**

Joint Committee on Fiscal Affairs (see Joint Committee on Fiscal Affairs)  
Revenue practice on members' expenses 3.21 - 3.26

**Ombudsman**

customs and excise appeals 19.36  
maladministration 8.28

**Parliamentary questions** (see Taxpayer assistance)**PAYE**

collection procedures, Appendix 5  
effects of Commission's proposals 6.11 - 6.13  
maintenance and preservation of records, Appendix 4  
non-cumulation 6.15 - 6.23  
present system 6.2 - 6.10, Appendix 2  
self-assessment 6.24 - 6.30

**'Phoenix syndrome'**

16.36 - 16.46

United Kingdom (see United Kingdom)

**Present system of tax administration**

broad impressions 1.5 - 1.9  
criticisms 1.10 - 1.16  
simplification 1.17 - 1.19

**Public Accounts Committee**

Revenue discretion 3.14 - 3.15

**Revenue Commissioners, the**

assessment appeals 4.7, 4.14, 3.14  
back-duty settlements 13.14  
Board 3.27 - 3.31  
'care and management' 3.16  
collection of interest on overdue tax 16.14  
communication with the Department of Finance 1.16  
county registrars/sheriffs 15.35  
criminal proceedings for tax offences 14.32  
customs and excise legislation 19.9  
customs and excise seizures 19.40  
direct expenditure tax 17.11  
enforcement of payment 15.46  
information powers (see Information powers of the Revenue Commissioners)  
legislation 2.6  
mobility of staff with the Department of Finance (see Staff mobility)  
parliamentary questions 8.27  
PAYE 6.8, 6.10  
penalties 13.8  
preferential status as creditor 16.16 - 16.35  
residential property tax 4.28  
Revenue discretion 3.14 - 3.18  
tax avoidance 11.23  
tax collection 15.17, 15.19  
tax evasion 10.3, 10.26, 13.22  
technical advisory committee on legislation 2.18  
technical finance bills 2.12  
VAT 18.5  
VAT on imports 18.38  
VAT registration 18.49  
withholding taxes 5.44

**Revenue effects of our proposals,**

Appendix 13  
basis of estimates 21.15 - 21.20  
income distribution effects (see Income distribution effects):  
timing 21.9

**Revenue practice**

advance rulings 3.9 - 3.11  
criticisms 3.5 - 3.8  
expenses incurred by Judiciary (see Judiciary)

expenses incurred by TDs and Senators (see Oireachtas)

present position 3.2 - 3.4  
Revenue Commissioners' discretion 3.12 - 3.20

**Self-assessment**

advantages and disadvantages 4.33 - 4.39  
basis 4.40 - 4.41  
capital gains and capital acquisitions (see Capital gains and capital acquisitions)  
compliance 4.49 - 4.52, 4.58 - 4.60  
criticisms 1.11 - 1.13  
experience in Ireland 4.24 - 4.32  
main features 4.22 - 4.23  
PAYE (see PAYE)  
payment arrangements 4.53 - 4.54  
residential property tax 4.27 - 4.29  
return forms 4.42 - 4.48, 4.55  
revenue effects 4.61 - 4.62  
systems in other countries 4.19 - 4.21  
United Kingdom (see United Kingdom)  
United States of America (see United States of America)

**Solicitor enforcement of debt collection,**

Appendix 7

**Staff mobility**

2.23 - 2.24

**Tax avoidance**

anti-avoidance, transfer of assets abroad, Appendix 3  
incidence 11.3 - 11.4  
Irish Congress of Trade Unions (see Irish Congress of Trade Unions)  
judicial attitudes 11.8 - 11.11  
legislative attitudes 11.12 - 11.26  
Minister for Finance (see Minister for Finance)  
official attitudes 11.5 - 11.7  
Revenue Commissioners (see Revenue Commissioners)  
United Kingdom (see United Kingdom)

**Tax collection and enforcement of payment**

collection system 15.6 - 15.22  
compliance 15.10 - 15.16  
county registrars/sheriffs (see County registrars/sheriffs)  
court recovery action 15.25 - 15.26  
deferred payment of arrears 16.6  
deterioration 1.14  
enforcement proceedings 15.23 - 15.37  
instalment arrangements for payment of arrears 16.3 - 16.5, 16.7 - 16.10  
involvement of local tax offices 15.22  
Irish Institute of Credit Management (see Irish Institute of Credit Management)  
Minister for Finance (see Minister for Finance)  
problems and deficiencies of present system 15.2 - 15.5, 15.38 - 15.39

proposed enforcement structure 15.40 – 15.68  
Revenue Commissioners (see Revenue Commissioners)  
United Kingdom (see United Kingdom)  
United States of America (see United States of America)  
write-off of unpaid tax and interest 16.11 – 16.15

#### **Tax, direct expenditure**

assessment 17.5 – 17.10  
collection 17.11 – 17.15  
savings relief 17.25 – 17.39  
treatment of assets 17.16 – 17.24  
United Kingdom (see United Kingdom)

#### **Tax evasion**

administrative data 10.17 – 10.27  
anti-evasion campaign 10.5 – 10.12  
enforcement activities 10.18 – 10.27  
Minister for Finance (see Minister for Finance)  
preventative measures 10.28 – 10.32  
public perceptions 9.2 – 9.6  
Revenue Commissioners (see Revenue Commissioners)  
United Kingdom (see United Kingdom)  
United States of America (see United States of America)

#### **Tax offences and penalties**

appeals 14.26 – 14.27  
back-duty settlements 13.13 – 13.20  
criminal offences 14.29 – 14.36  
default 14.7 – 14.18  
Director of Public Prosecutions (see Director of Public Prosecutions)  
failure to notify chargeability 14.23 – 14.25  
failure to submit returns 14.19 – 14.22  
imposition of penalties 13.7 – 13.12  
inconsistency of present system 13.25 – 13.29  
mitigation of penalties 14.28  
objectives of revised system 14.5 – 14.6  
present range 13.2 – 13.6  
publication of names of defaulters 13.21 – 13.24  
Revenue Commissioners (see Revenue Commissioners)  
United Kingdom (see United Kingdom)

**Taxpayer assistance** 8.12 – 8.28  
central enquiry office 8.16 – 8.19  
parliamentary questions 8.26 – 8.28  
simplification of forms and publications 8.20 – 8.25

#### **United Kingdom**

back-duty settlements 13.18  
collection enforcement 15.41, 15.64  
costs and benefits of VAT 8.9, 18.11 – 18.12  
customs and excise legislation 19.7  
expenditure tax 17.3 – 17.5, 17.16 – 17.17  
motor vehicle duty 20.18, 20.20  
'phoenix syndrome' 16.42  
Revenue preference 16.25, 16.27 – 16.28  
search of persons 12.33  
search of premises 12.30  
self-assessment 4.44  
tax avoidance 11.10, 12.41  
tax evasion 10.13  
tax offences and penalties 14.6  
taxpayers compliance 15.14

#### **United States of America**

collection enforcement 15.41, 15.60  
retention of documents for tax purposes 12.65, 12.67  
self-assessment 4.20 – 4.21, 4.58, 6.26  
tax evasion 10.14 – 10.16

#### **University College, Dublin**

tax evasion 9.5

#### **Value-added Tax**

accounting 18.2  
collection procedures, Appendix 6, Appendix 6 – Annex 1  
EEC Sixth Council Directive 18.9  
imports 18.20 – 18.39, Appendix 9  
maintenance and preservation of records, Appendix 4  
registration 18.40 – 18.52  
returns 1.13  
second-hand goods 18.53 – 18.57  
United Kingdom (see United Kingdom)

#### **Withholding taxes**

Construction Industry tax deduction scheme (see Construction Industry tax deduction scheme)  
extension to other areas 5.43 – 5.45  
income subject to withholding 5.8

#### **Working Party on Simplified Accounts**

VAT 18.13