

PAC-R-945

Correspondence 3A.2
Meeting 85 – 23/05/2013



Ms. Niamh Maguire,
Committee Secretariat,
Committee of Public Accounts,
Leinster House,
Dublin 2.

22 May 2013

Dear Ms. Maguire,

Ms. Feehly, Accounting Officer has asked me to forward the attached material for the information of the Committee in response to your letter of 14 May 2013.

Please do not hesitate to contact me if you require any further details.

Yours sincerely,

Paddy O'Shaughnessy
Principal Officer

1. VIES returns

A note on the filing of VIES returns

1. Background

In January 1993, frontier controls on the movement of **goods** between EU Member States were abolished and Importers and Exporters in EU trade no longer were required to complete customs documentation.

Under Council Regulation (EEC) No. 218/92 of 27th January 1992, the EU Council established a system of administrative co-operation known as the VAT Information Exchange System (VIES) which was designed to prevent and deter abuse of the VAT zero-rating provisions for goods traded in the EU from 1st. January 1993.

An integral part of the VIES arrangements is a requirement that each Member State must store and process specific information which it collects from its traders about their trade with other Member States. Each Member State collects details of intra-Community supplies by its VAT registered traders to business customers in other EU Member States: details of intra-Community acquisitions by Irish traders come from the VIES returns made by traders in other EU Member States.

Since 1 January 1993 VAT registered traders supplying zero-rated goods to VAT registered traders in other EU Member States are obliged to provide periodic VIES returns to the Revenue Commissioners giving details of their intra-Community supplies.

From 1 January 2010 the requirement to make VIES returns was extended to include supplies of **services** by Irish traders where the place of supply (and taxation) is another EU Member State and the business recipient of the service has an obligation to self-account for the VAT on the service in that other Member State.

The VIES return will contain the aggregate value of the goods or services provided to each trader/business in each Member State for the period covered by the return.

VIES returns are made on either a monthly or quarterly basis, depending on the nature and value of transactions. The Council Directive 2008/117/EC provides that VAT registered traders involved in intra-community supplies of goods or services must file returns

monthly if the supplies exceed €50,000 in value in any of the previous four quarters. Those traders who fall below this value may make quarterly returns. In some circumstances traders, who have a relatively small total amount of intra-Community supplies and satisfying some specific criteria, may apply to make Annual returns.

2. VIES Traders

VAT registered traders providing goods and/or services to other Member States are required to supply periodic VIES statements to the Revenue Commissioners. There are two categories of VIES filers – standard traders and large filers. Currently there are 9,900 traders on the VIES Trader register of which only 6 are Large Filers.

Standard Traders

There are 9,900 standard traders who file their returns via the ROS system in the same manner that all other ROS returns are filed. Returns can be done online via ROS if they are under the limit of 30 line items or transactions. If there are between 30 and 6000 line items or transactions the return must be done using the ROS Offline application.

Large Filers

Large filers are customers who submit VIES returns with more than 6000 line items or transactions. Since the ROS systems cannot cater for returns with more than 6000 line items these large filers make returns by submitting electronic files in a format agreed with Revenue's ICT Division through the Revenue-developed Connect Direct facility. There were just 5 large Filers during the period of the C&AG report and an additional Large Filer commenced using the Connect Direct facility in 2013.

The Large Filers make up a significant portion of the overall value of the returns on the VIES system. In 2012 these 5 companies made up approximately €13 billion of €78 billion worth of VIES transactions, 16% of overall volume. Large Filers deal almost exclusively in Services and in this context make up an even large proportion of services returned via VIES.

3. Communication with Other Member States

Ireland exchanges information with the other Member States of the EU via an IT system called the VIES Gateway. The transfer of VIES data to the other Member States is done on a monthly basis. Similarly, Revenue receives information in return from all other Member States, including reports that show transactions where invalid VAT numbers have been quoted by traders.

4. VIES in the context of trade values

The following tables puts in context the value of goods/services recorded within the VIES system when compared to the value of goods and services exports reported by the Central Statistics Office. The CSO figures include exports to other EU countries and exports to countries outside the EU. VIES only reports exports to other EU countries.

| Category | 2012 | 2011 | 2010 |
|---------------|-----------|-----------|-----------|
| | € billion | € billion | € billion |
| Goods Exports | 92 | 91 | 90 |
| of which | | | |
| VIES | 57 | 50 | 53 |
| (%) | (62%) | (55%) | (59%) |
| Services | N/A | 81 | 74 |
| of which | | | |
| VIES | 21 | 27 | 21 |
| % | | (33%) | (28%) |
| of which | | | |
| Connect | | | |
| Direct | 13 | 10 | 7.6 |

5. VIES Trader Analysis

There are currently circa 9,900 Traders registered within the VIES System. Of this number 7,400 are reporting on Goods only, 1250 are reporting on Services only and the remaining 1250 are reporting on both Goods and Services. There are 6 Large Filers dealing almost exclusively in Services who submit returns via the secure Connect Direct facility.

In terms of value indicators the traders involved are divided into 4 categories referred to as Value Indicators. The following Table gives details of the number of traders and the value of VIES transactions in 2012.

| Value Indicator | Description | No. of Traders (% of Total) | 2012 Value of VIES Transaction (% of Total) |
|-----------------|---|-----------------------------|---|
| A | Annual Intra-community Supplies > €10M | 554 (5.6%) | €50 bn (63%) |
| B | Annual Intra-community Supplies > €1M < €10M | 1422 (14.4%) | €26 bn (32.8%) |
| C | Annual Intra-community Supplies > €635K < €1M | 588 (6.0%) | €1 bn (1.1%) |
| D | Annual Intra-community Supplies > €635K | 7336 (74.0%) | €2 bn (2.6%) |
| Totals | | 9,900 (100%) | €79 bn (100%) |

It can be seen from the table that the 554 traders (or 5.6% of all traders) in the Value Indicator A category accounted for almost two-thirds of the value of all VIES transactions in 2012. Conversely, the 80% of traders that make up the Value Indicator C and D categories account for just €3 billion (or 3.7%) of the €79 billion in VIES transactions in 2012.

6. Compliance and Prosecution

There are inevitably some traders who are non-compliant and contacting these traders and getting them to comply is one of the tasks undertaken by the VIES team. For the year to January 2013 the average return filing rates are shown in the following table.

| Value Indicator | Description | Timely Compliance Rates based on 2012 Data | | |
|-----------------|---|--|-----------------|---------------|
| | | Within 1 Month | Within 3 Months | Within 1 Year |
| A | Annual intra-EU supplies greater than €10 million | 87.4% | 88.0% | 97.2% |
| B | Annual intra-EU supplies between €1 and €10 million | 83.9% | 84.6% | 95.5% |
| C | Annual intra-EU supplies between €635,000 and €10 million | 81.6% | 80.0% | 97.2% |
| D | Annual intra-EU supplies less than €635,000 | 66.0% | 73.0% | 87.0% |

It can be seen that ultimate filing percentage for the Value Indicator A, B and C is in excess of 95%: these three categories represent 99% of the value of VIES transactions. The increase in filing from one month to a year is attributable to natural later filers and actions by those contacted by Revenue staff.

Despite the efforts of the VIES team there are unfortunately times where efforts to make traders compliant are unsuccessful. In these circumstances the cases are passed onto the

Prosecutions section. The Prosecutions section works in contacting the customers again, issuing warning letters, 21-day letters and liaising with the Revenue Solicitor's Office in relation to initiating formal prosecution proceedings.

Cases are considered for prosecution on an ongoing basis as the non-submission of returns is identified. Below are the current statistics for the cases considered for prosecutions in 2012/2013.

| Month in which case first considered | Number of Cases Considered | Returns Received following customer contact (as set out above) | Percentage of cases where returns received following customer contact |
|---|-----------------------------------|---|--|
| Mar-Dec 2012 | 168 | 165 | 98.3% |
| Jan 2013 | 15 | 14 | 93.4% |
| Feb 2013 | 36 | 34 | 94.5% |
| Mar 2013 | 76 | 44 | 57.9% |

Of the three out of 168 cases that still haven't submitted returns for the period March to December 2012:

- 2 are moving towards the courts;
- 1 case has ceased and is not suitable for prosecution.

2. Waterford Revenue District Project

A detailed note on the Waterford Revenue District VAT on Intra-community Acquisitions Project.

Introduction

The Waterford Project was focused on Intra-Community acquisitions (ICAs) by Irish businesses from suppliers in other EU Member States. The purpose of the project was to identify audit cases by selecting cases that might not have correctly accounted for VAT on their ICAs. Cases were considered for selection if discrepancies or omissions arose when the VIES data of ICAs was cross-referenced against information available from other sources, such as, VAT 3 returns, business description, sales and purchases figures on Income Tax/Corporations Tax returns, etc. Discrepancies or omissions could indicate underreporting or non-reporting of VAT liabilities on ICAs.

Initial selection

The 600 cases were selected using REAP rules that showed that the cases had made ICAs that were reported by a foreign supplier through the VIES Gateway. The REAP rule simply identified that the case had made ICAs but gave no details of the value of the ICAs. No record of their overall REAP risk rating was kept so it is not possible to say how many cases would have been considered for audit on a whole case risk assessment basis. However, on a general note a case that files on time and makes timely payments will generally not have a high REAP risk rating so the vast majority of the 600 cases would not have come up for consideration through REAP.

The 600 cases were initially worked by Revenue staff using a template developed by Revenue to identify cases with the highest risk of underdeclaration of VAT. The template was based on looking at the values of the ICAs obtained on a case by case basis and comparing them to figures on the VAT 3s. The purpose of this comparison was to eliminate cases that had correctly self-accounted for the ICAs. This process eliminated 500 cases mainly based on materiality.

Case working

Following the initial work 100 cases were identified that might have potential Irish VAT liabilities. The potential liabilities might arise from:

- traders making acquisitions from traders in other EU member states, at a zero rate of VAT, and not paying VAT when the goods or services are released to market
- unregistered traders making intra-community acquisitions.
-

The following Table sets out results that have been recorded in relation to the approximately 100 remaining cases in the format presented in Figure 11.5 of the C&AG Report. It can be seen that 50 of the 100 cases were closed by appraisal or aspect queries and the associated liabilities were small. A further 32 cases were closed following correspondence with the traders. The total yield in relation to the 100 cases was almost €2 million. Included in this total were 2 cases with a combined yield of €1.5 million.¹

| Category/Case | Number | Yield (€) |
|---|------------|-------------------|
| Closed following correspondence with trader | 32 | 63,217 |
| Closed Audits (see Note below) | 13 | 754,117 |
| Case with Assessments and Notice of Opinion pending (Yield shown is that on the assessments plus the Notice of Opinion) | 1 | 1,032,590 (e) |
| Open audit case with likely yield | 1 | 30,000 (e) |
| Work commenced on 2 cases | 2 | 35,000 (e) |
| Profile interview to take place | 1 | 20,000 (e) |
| Balance closed by appraisal/aspect query | 50 | Small liabilities |
| Total | 100 | 1,934,924 |
| | | |
| Average over 600 cases | | 3,225 |
| Average over 100 cases | | 19,349 |
| Average over 50 Yielding Cases | | 38,698 |
| | | |
| Note: | | |
| 1 of the 13 cases had a yield of €478,742 which distorts the average figures. | | |
| | | |

(e) means estimated

¹ The two cases are (1) the Case with the Assessments and the Notice of Opinion pending (€1,032,590) and (2) the case shown in the note to the table (€478,742).

The Table shows that the average audit settlement varies from €3,225 to €38,698 depending on which of the three case bases is taken.

Outcome

On the basis that 600 cases were worked to identify 50 yielding cases, which will not be practicable on an ongoing basis, the learning from this project has contributed to the development of the REAP rules and new VIES rules for Revenue's VAT Real Time Risk project.

In addition, a Manual titled *Maximising the use of VIES data to identify VAT Risk* has been developed to assist case workers in identifying cases that present VIES risks. A copy of this Manual is attached for information.



3. International Traders

A note on the monitoring of International traders importing/exporting goods into Ireland at the request of Revenue and the number being monitored by Revenue at the request of other EU countries.

Three EU VAT information exchange mechanisms operate under the aegis of EU Council Regulation 904/2010.

Firstly, there is the **EUROFISC** initiative. EUROFISC is a network of officials in EU Member States that focuses on the detection and combating of cross-border VAT fraud. The work of the EUROFISC network involves an early warning mechanism leading to the ongoing monitoring of the cross-border business transactions of certain suspect traders. For example, where an EU Member State identifies a series of suspect EU cross-border

VAT transactions that may indicate possible VAT fraud, with one trader being a common denominator, the details (such as value of goods and services, VAT registration number etc) of the transactions are notified to the EUROFISC central coordinating office. That office correlates the notifications received from each EU Member State into a database the details of which are sent twice monthly to all EU Member States.

The appearance of a new trader on the EUROFISC twice monthly database is an indicator for the Revenue authority of the relevant EU Member State in which that trader is based to carry out a VAT compliance check. Some checks reveal nothing untoward whilst other checks result in such traders being placed on an on-going monitoring programme. Monitoring in this context involves checking on a regular basis the monitored trader's intra-Community business transactions, that are captured on the EU VAT Information Exchange System (VIES). Monitoring may also include visits to the trader for the purposes of examining his or her trading records.

Each EU Member State has an obligation to monitor the transactions of those traders in their jurisdiction that appear on the EUROFISC twice monthly database.

At present Revenue, under the EUROFISC initiative, are monitoring the intra-Community transactions of 15 traders. These are Irish companies that are on the EUROFISC database by virtue of notifications to EUROFISC by Revenue. To date, we have exchanged with other member states about a thousand pieces of information on those traders. In addition, we have received over 600 pieces of information concerning specific traders.

Secondly, there is what is termed a '*Mutual Assistance Request*' where one EU Member State requests another Member State to provide specific information or clarification as regards a transaction involving a particular trader that has occurred in that other Member State. During 2012, Revenue issued 443 such requests and received 254.

Thirdly, there are what are termed '*Spontaneous Information Communications*'. These are communications, made without prior request, of information to another Member State where it is believed that the information may be relevant to that State in combating VAT fraud. During 2012, Revenue sent 294 such communications and received 89.

4. VAT liability on exported goods

A note on VAT liability in respect of goods exported outside the EU which subsequently come back to Ireland for repair.

An Irish supplier who sells goods is obliged to register and charge VAT if his or her turnover in a continuous period of 12 months exceeds, or is likely to exceed, the turnover threshold, currently €75,000.

1. A supplier selling goods to a business customer in another EU Member State

An Irish supplier who sells goods to a business customer in another EU Member State charges the zero rate of VAT once the goods are dispatched or transported to that other Member State. The business customer who buys the goods must self-account for the VAT on the goods in their own Member State at the appropriate rate of VAT rate. For example, if it is a UK business customer that customer would self-account for VAT in the UK at the rate of 20%.

2. A supplier selling goods to a business customer in the USA

An Irish supplier who sells goods to a business customer in the USA charges the zero rate of VAT once the goods are dispatched or transported to the USA. There are no further VAT implications since the business customer who acquired the goods is outside the European Union.

3. A previously- sold good comes back to Ireland for repair

A repair on goods is generally treated as a service for VAT purposes. The entry to Ireland and the exit from Ireland of the goods that are the subject of the repair have no VAT implications. The VAT place of supply rules means that the place of supply (and taxation) for business-to-business transactions is the place where the business customer is established. If the business customer is established in another EU Member State then that business customer must self-account for VAT on the repair in their own Member State. If

the business customer is established outside the EU then there are no VAT implications for the business customer.

5. Effective rate of Corporation Tax

A note on the effective rate of corporation tax in relation to the headline rate of 12.5%, including a breakdown of the effective rate of tax paid.

Companies operating in Ireland are chargeable to corporation tax at the 12½ per cent rate on the profits that are generated from their trading activities here. The 10 per cent corporation tax rate for profits from manufacturing expired at the end of 2010 and the 12½ per cent rate now applies to such profits. A higher 25 per cent rate applies in respect of investment, rental and other non-trading profits, as well as certain petroleum, mining and land-dealing activities, while chargeable capital gains are taxable at the capital gains tax rate of 33 per cent.

Companies are chargeable to corporation tax on their profits after taking account of allowable deductions and reliefs provided for in the Taxes Consolidation Act 1997. Expenses that are incurred wholly and exclusively for the purposes of the trade are deductible in computing trading profits, while allowances are available for capital expenditure on plant and machinery, industrial buildings and certain intangible assets used in the trade, with such allowances treated as a deductible trading expense. Companies are charged on their net profits after account is taken of any losses they have incurred.

The Taxes Consolidation Act contains certain tax reliefs for companies that are standard features of a corporate tax system, including group relief - which allows for trading losses of a group company to be offset against profits of another group company - and double taxation relief which provides relief for foreign taxation on income earned abroad. There are also specific tax reliefs for companies that are targeted at promoting investment in key areas of economic importance, including a 25 per cent tax credit for expenditure on research and development and relief for start-up companies creating employment.

There are different ways of measuring the effective rate of corporation tax and there is no single internationally agreed comparative measure for this. An effective corporation tax rate of 11.9 per cent was estimated for Ireland in a study carried out by Price Waterhouse

Coopers in 2011 for the World Bank, which includes estimates of effective tax rates for 183 countries based on the tax obligations of a standardised company operating in each country. Another study - the European Commission's *Taxation Trends in the EU 2013*² – indicates an effective tax rate for Ireland that is close to the 12½ per cent corporation tax rate. In the absence of an agreed methodology for determining the effective tax rate, differences will inevitably exist in comparative studies on effective tax rates, depending on how the rate is calculated and the assumptions used in the calculation.

An estimate of total corporation tax payable as a percentage of taxable profits can be made from the latest aggregate corporation tax statistics compiled by the Revenue Commissioners, based on the tax returns of companies for the year 2010. These statistics indicate that aggregate net taxable profits, after taking account of various deductions, allowances, charges and reliefs, amounted to €41.215 billion while the total amount of corporation tax payable on these profits was €4.246 billion. This means that total corporation tax payable as a percentage of taxable profits was approximately 10.3 per cent for the year.

While this percentage is lower than the 12½ per cent rate, this can be attributed to the availability of certain reliefs – such as double taxation relief (€619 million), manufacturing relief³ (€403 million) and R&D credit relief (€142 million).

A summary of the calculations is set out in the **Annex** attached, while a more detailed breakdown is provided in Table CTS 3 and Explanatory Note in the Annual Revenue Statistical Report available on the Revenue website at www.revenue.ie .

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http://ec.europa.eu/taxation_customs/resources/documents/taxation/gen_info/economic_analysis/tax_structures/2013/report.pdf (Table 91, page 262)

³ This relates to the 10% rate of tax for manufacturing companies that expired on 31 December 2010.

ANNEX

Aggregate Taxable Profits of Companies for Accounting Periods ending 2010

| | €m | €m |
|--|--------|----------------------|
| Gross Trade Profits | | 70,804 |
| <u>Less deductible amounts as follows:</u> | | |
| Capital Allowances | 12,296 | |
| Trading Losses Brought Forward | 3,870 | |
| Current Year Trading Losses | 131 | |
| Trade Charges | 11,695 | |
| Group Relief | 2,747 | |
| | | (30,739) |
| Net trading Profits | | 40,065 |
| Net Rental Income | | 547 |
| Non-trading Profits / Capital Gains | | 5,849 |
| <u>Less Other Deductions:</u> | | |
| Management Expenses | 415 | |
| Excess Capital Allowances | 15 | |
| Non-trade charges/ other deductions | 4,804 | |
| Excepted Trade Losses | 12 | |
| | | (5,246) |
| Net Taxable Profits | | <u>41,215</u> |

Note:

After taking account of surcharges and various reliefs and credits, such as double taxation relief (€619m), manufacturing relief (€403m) and R&D credit relief (€142m), the total amount of corporation tax payable in respect of the net taxable profits of €41.215 billion for 2010 was **€4.246 billion**.

6. Outstanding Debt

A breakdown of the €2 billion outstanding debt owed to Revenue by a) age of debt and b) taxhead.

Please see table below with analysis by age and taxhead of total debt outstanding at 31/03/13.

Analysis of Total Debt (€m)

| Year | IT | CT | CGT | CAT | PAYE | PRSI | VAT | RCT | ELEVY | ATT | DIRT | Total | % |
|--------------|-------------|-------------|-------------|------------|-------------|-------------|-------------|------------|------------|-----------|-----------|---------------|---------------|
| 2012 | €5 | €72 | €0 | €12 | €69 | €61 | €69 | €3 | €1 | €0 | €0 | €291 | 14.5% |
| 2011 | €96 | €18 | €6 | €4 | €31 | €27 | €73 | €2 | €2 | €0 | €0 | €260 | 13.0% |
| 2010 | €57 | €20 | €4 | €2 | €16 | €22 | €64 | €2 | €0 | €0 | €0 | €189 | 9.4% |
| 2009 | €52 | €13 | €5 | €3 | €18 | €18 | €62 | €3 | €0 | €0 | €0 | €173 | 8.6% |
| 2008 | €74 | €18 | €12 | €4 | €10 | €13 | €60 | €5 | €11 | €0 | €0 | €208 | 10.3% |
| 2007 | €107 | €45 | €38 | €1 | €5 | €6 | €32 | €4 | €8 | €0 | €0 | €247 | 12.3% |
| 2006 | €52 | €26 | €38 | €1 | €5 | €4 | €24 | €4 | €8 | €0 | €0 | €162 | 8.1% |
| 2005 | €39 | €14 | €28 | €0 | €6 | €2 | €15 | €3 | €10 | €0 | €0 | €116 | 5.8% |
| 2004 | €36 | €6 | €10 | €0 | €2 | €1 | €16 | €1 | €0 | €0 | €0 | €73 | 3.6% |
| 2003 | €21 | €0 | €12 | €0 | €2 | €1 | €18 | €0 | €0 | €0 | €0 | €55 | 2.7% |
| 2002 | €19 | €3 | €26 | €1 | €1 | €1 | €11 | -€1 | €0 | €0 | €0 | €61 | 3.1% |
| to 2001 | €89 | €5 | €81 | €0 | €2 | €2 | -€10 | €1 | €0 | €0 | €0 | €171 | 8.5% |
| Total | €647 | €241 | €261 | €30 | €166 | €159 | €434 | €27 | €41 | €1 | €0 | €2,006 | 100.0% |