



# Can't Pay, Won't Pay – Striking the Balance: Revenue's Approach to Tax Payment, Collection and Enforcement in the Current Economic Climate



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## Introduction

Issues surrounding the payment, collection and enforcement of collection of tax have become very topical and increasingly difficult in recent times. This can partially be attributed to the unprecedented global and domestic downturn that the State finds itself in. In this article I consider the dilemmas faced by the Revenue Commissioners (from a tax practitioner's perspective) in the current economic climate with respect to striking a balance between the

need to collect tax revenues and the duty of care that must be shown toward the taxpayer. I will consider the methods of enforcement that the Revenue Commissioners have traditionally used to collect taxes and also cover the "Case Decision Escalation Framework" (CDEF) guidelines that they have recently issued to their staff.

## Current Economic Climate

The Revenue Commissioners published their annual report for the year ended 31 December

2008 in April 2009. In their Board Review they reflect on the falling tax revenues that occurred in 2008 as compared to 2007. They note that "gross receipts in 2008 fell by 9.2% compared to 2007 and net receipts fell by 13.5%". They go on to state that "asset related taxes were hardest hit, with receipts from both capital gains tax and stamp duty down by half". In their analysis the Revenue Commissioners conclude that:

*“rising unemployment and curtailed consumer spending also exerted downward pressure on receipts. VAT, the single largest tax head, was down by just over €1 billion year on year. While a large proportion of this shortfall can be attributed to the collapse in the construction sector, VAT payments from the wholesale and retail trades and from the motor industry also slowed significantly as the year progressed.”*

The Exchequer statement for the first three months of 2009 shows a deficit of over €3.7 billion, largely caused by a decrease of over €2.5 billion in tax revenues from €11.1 billion in the first three months of 2008 to €8.6 billion for the same period in 2009.

Ireland's level of national debt is relatively low, at 43% of GDP, or €54 billion. However, the running deficits that have arisen due to the recent falls in tax revenues are expected to result in an increase in the national debt by as much as €20 billion in 2009, based on information provided by the National Treasury Management Agency (NTMA) and views expressed by various economic commentators.

Ireland is therefore becoming increasingly reliant on international credit, and, just like any other lender would (or at least should!) do, the international market is looking at issues such as Ireland's falling tax revenues and the commitment the Government has given to the banks through the Government Bank Guarantee Scheme when considering the risk inherent in lending to Ireland. The recent downgrading of Ireland's credit rating from an AAA rating to an AA+ rating by ratings agency Standard & Poor's is a stark reflection of the fact that Ireland is now seen as a more risky investment for the international investor than had been the case

in recent years. Consequently, the cost of the Irish Government's borrowing will now be more expensive, which will put even more pressure on the economy.

It is clear that the Government urgently needs to increase (or at least stop the dramatic decline in) its tax revenues in order to stem the increasing national debt, and indeed attempts have been made to do so through the early announcement of Budget 2009 on 14 October 2008 and the announcement of the recent emergency Budget in April 2009. The other options obviously include reductions in public spending budgets.

Many taxpayers are faced with acute economic difficulties. Businesses are finding it extremely difficult to obtain credit from the banks, and as a result they are struggling to maintain sufficient cash-flow to pay their creditors, which include Revenue.

### Striking the Balance

The Revenue Commissioners are therefore faced with the dilemma of collecting an ever-increasing amount of unpaid taxes from taxpayers who have an ever-dwindling supply of cash at their disposal. Many

of these taxpayers are involved in financially viable businesses that have contributed (and should, hopefully, continue to contribute) valuable tax revenues to the State. No purpose is served by taking a hardline approach to this type of taxpayer that results in them going out of business and depriving the State of the future tax revenues that they should generate.

Ms Josephine Feehily, chairman of the Revenue Commissioners, made the following comments on 24 April 2008 at the publication of the Revenue's Annual Report for 2007: “Our fundamental aim, in all that we do, is to make it

easy for people who want to do business with us and to make it difficult for those who don't”. This sums up very concisely the balance that the Revenue Commissioners seek to strike in the performance of their duty to collect taxes.

Even in the era of the Celtic Tiger, when most businesses were flourishing, there were inevitably taxpayers who did not want to “do business” with Revenue, even if they had the cash-flow to do so, i.e. the taxpayers who “won't” pay their taxes. Such taxpayers gain an unfair competitive advantage over the taxpayers who pay their taxes in a timely manner, as by withholding tax payments they can use those monies to improve their cash-flow. The current economic climate cannot, of course, be allowed to become an excuse for tax evaders not to pay their taxes. Conversely, the majority of taxpayers do, in fact, want to “do business” with the Revenue Commissioners. Therefore the Revenue Commissioners need to ensure that they recognise the difference between the taxpayer who “won't” pay their taxes and the taxpayer who genuinely “can't” and to tailor their approach accordingly.

On the recent publication of Revenue's Annual Report for 2008 the Board of the Revenue Commissioners acknowledged that “demanding trading conditions, falling cash flow and tightening credit availability made it more difficult for businesses to meet their tax and duty obligations in a timely manner, and this trend is set to continue throughout 2009”. However, the Revenue Commissioners also reiterated that “it is a priority goal of Revenue to ensure that compliance rates remain at the highest possible level, and collectible debt remains at the lowest possible level”.

### Revenue Powers

The Collector-General's Office has responsibility for collecting the taxes due and for pursuing taxpayers when they fail to comply with their tax obligations. Part 42 of the Taxes Consolidation Act 1997 details the tax collection

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and recovery methods available to the Revenue Commissioners. The main methods that may be used by them to encourage the timely payment of tax are summarised below (a detailed examination of each of these methods is outside the scope of this article)<sup>1</sup>.

### Charging interest

Interest at 0.0273% per day or part of a day (c. 10% per annum) may be charged on the late payment of income tax, corporation tax, capital gains tax, gift tax and inheritance tax. A rate of 0.0322% per day or part of a day (c. 12% per annum) applies to the late payment of indirect taxes such as excise duties, VAT, PAYE, RCT, PSWT, DIRT and similar withholding taxes and exit taxes collected by other parties on a fiduciary basis for the Revenue Commissioners.

### Issuing demands

The Revenue Commissioners may issue various types of demands for payment of outstanding tax liabilities:

- › an estimate/demand where a return and payment for a period (or periods) have not been received,
- › an underpayment letter where a return has been received but with insufficient or no payment,
- › a demand letter covering the outstanding liability(ies).

The first two types of demand are generally issued on an automatic basis by the Revenue Commissioners' systems, while the third type is usually manually issued by a caseworker.

### Other measures

Revenue may also encourage compliance by taking such measures as withdrawing a taxpayer's C2 certificate, withholding repayments of tax due to the taxpayer (or connected persons), making an offset of tax repayments due against tax liabilities due, not issuing a tax clearance certificate or prosecution for non-submission of returns.

### Enforcement

If a taxpayer fails to respond to an estimate/demand, the caseworker then has four options:

- › referral of the case to the local Sheriff,
- › use of the "power of attachment",
- › referral of the case to the local State solicitor,
- › taking bankruptcy or liquidation proceedings.

#### Referral of the case to the local Sheriff

Under this option the caseworker will refer the outstanding liabilities to the Sheriff for collection of the debts. The Sheriff may, if necessary, seize certain assets

from the tax defaulter on foot of a warrant.

There are 16 Revenue Sheriffs who carry out debt collection on a professional basis for the Revenue Commissioners. The debt collection activities of the Sheriff are governed by the Enforcement of Court Orders Act 1926. This method of enforcement is most effective from a Revenue point of view where the tax defaulter has realisable assets that are unencumbered. These assets may be seized by the Sheriff and sold to pay the tax debt. The Sheriff also has the right to negotiate an arrangement with the taxpayer such as a phased payment generally not exceeding two years. The Sheriffs are

entitled to collect their fees and expenses in relation to the collection of the payment and/or seizure of the assets from the taxpayer. This is the most popular method used by the Revenue Commissioners, with 45,986 cases referred to the Sheriff in 2008, yielding €257.7 million to the Exchequer.

### Power of attachment

The Revenue Commissioners' power of attachment is provided for in s1002 Taxes Consolidation Act 1997 (TCA 1997). This legislation authorises Revenue to issue a Notice of Attachment to a debtor owing a debt to a taxpayer who has defaulted in paying their taxes. This effectively means that the taxpayer's debtor must pay its debt to the Revenue Commissioners, as opposed to paying the debt to the taxpayer, until such time as the amount detailed in the Notice of Attachment is discharged. The debts that can be subjected to an attachment include monies placed on deposit with banks (with or without interest), monies with insurance companies, State agencies, court settlements, compulsory purchase orders etc. An amount owed by a third party to the taxpayer as emoluments, i.e. wages or salaries, cannot be subjected to the power of attachment.

This is a very cost-effective enforcement option as no legal fees will be incurred by the Revenue Commissioners or the taxpayer. However, it may be an unfavourable method from the taxpayer's point of view as the debtor whose debt is subjected to the power of attachment will obtain certain knowledge of the taxpayer's tax affairs and the fact that they are in arrears. The secrecy obligations imposed on the Revenue Commissioners are removed by s1002(15) TCA 1997. In 2008 2,398 cases were the subject of power of attachment, with a yield of €28.9 million to the Exchequer.

### Referral of the case to the local State solicitor

In general, referral to a solicitor is used where the Sheriff or power of attachment options are

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1. However, see the two-part article by F. Mitchell, D. Macaulay & L. McCann, "Methods of Enforcement of Revenue Debts", *Irish Tax Review*, 21/5-6 (2008).

not suitable or have proved ineffective. The Revenue Commissioners have entered into a contract with six external solicitors to provide legal services associated with debt collection and the enforcement process. All legal services associated with debt collection (apart from liquidation work, which is carried out by the Revenue Solicitor's Office) are performed by these six solicitors. A total of 6,866 cases were referred to solicitors for enforcement in 2008, with a yield of €67.2 million to the Exchequer.

A number of legal options are available to the Revenue Commissioners, the first of which is their entitlement to obtain a court judgment that an amount is due to them by the taxpayer. The taxpayer is held liable for any costs and fees that arise when a case has been referred to a solicitor once court proceedings have been initiated. If the judgment does not obtain the desired effect, the judgment may be registered and published so that it will be in the public domain.

The Collector-General has a Specialised Enforcement Unit, which may use exemplary measures to pursue cases of serious debt and non-compliance. The main measures that may be used are bankruptcy, forced sale, committal order/committal to prison, a Mareva Injunction (freezing of assets) and a Garnishee Order (similar to the power of attachment). This unit may take criminal prosecution cases and may impose civil penalties under s987 TCA 1997.

### Bankruptcy and liquidation

The Revenue Commissioners may apply for the grant of a bankruptcy summons under s8 of the Bankruptcy Act 1988 or present a petition for adjudication under s11 of that Act in respect of tax due by a taxpayer. The Revenue Commissioners may also petition the High Court to wind up a company as provided for in the Companies Act 1963. If the courts find that a company has been trading fraudulently or recklessly and has continued to trade and add to these debts, this can also have serious legal implications for the directors. Tax debts are ranked as preferential debts in bankruptcy and winding-up procedures.

The methods of collection and enforcement of tax liabilities outlined above relate only

to the measures to be taken by the Revenue Commissioners in relation to otherwise compliant taxpayers who merely experience difficulty in paying their tax liabilities. A discussion of the procedures and penalties that may be pursued in the course of a Revenue audit or a voluntary disclosure in the case of a tax default is outside the scope of this article.

It is clear that the enforcement options open to the Revenue Commissioners are wide-ranging and severe. One of the ultimate responsibilities of the Revenue Commissioners is to collect taxes, and therefore, instead of pursuing the options outlined above, they may in certain cases consider agreeing phased payment/instalment arrangements.

### Phased Payment/ Instalment Arrangements

The Revenue Commissioners may as a concession consider agreeing to a phased payment/instalment arrangement if justifiable in the circumstances of the individual taxpayer or business. Every instalment arrangement will include interest as it is considered that the Exchequer should be compensated for the late payment of tax and that a level playing field should be achieved for both those who pay their tax on time and those who do not.

In order to obtain an instalment arrangement the taxpayer must provide the following to the Revenue Commissioners:

- › an explanation of the reasons for non-payment,
- › a clear outline of the reasons why the debt due cannot be paid now and in full,
- › details of current creditors and debtors,
- › a clear and time-bound proposal for payment of the debt in full in the shortest possible

timeframe, bearing in mind that the proposal must have a realistic prospect of success,

- › the proposed level of down-payment at the commencement of the proposed phased payment arrangement and
- › agreement to pay the full costs of enforcement action that may have been undertaken to date by Revenue in regard to the debt concerned.

### Case Decision Escalation Framework Guide

The Revenue Commissioners have acknowledged the unique economic circumstances that

taxpayers can find themselves in (in the current environment) and have issued guidelines to their staff with respect to their proposed approach to the collection of tax debts in the current climate. These guidelines are contained in the "Case Decision Escalation Framework" (CDEF) and are published, in accordance with the Freedom of Information Act 1997, on the Revenue website.

The CDEF guidelines make it clear that:

*"Revenue is determined to maintain the current high levels of compliance notwithstanding the more difficult economic circumstances in which businesses and taxpayers are now operating".*

The guidelines go on to emphasise that "Revenue cannot and will not become a banker of last resort" and therefore make it clear that the Revenue powers outlined earlier in this article will continue to remain relevant and valid.

HMRC in the UK has recently set up a dedicated Business Payment Support Service, which seeks to agree flexible payment arrangements with taxpayers on a timescale that is reasonable in each individual case. This service has proved very successful in the UK, with over 60,000

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businesses making arrangements regarding more than £1 billion in tax. The service constitutes a support line for businesses to contact HMRC and is open seven days a week. It would appear that the CDEF aims to be the Irish equivalent to this service, albeit that it would seem that the Irish Revenue has taken a less formal approach than its UK counterpart.

The CDEF aims to allow a speedy and appropriate referral of cases for a higher-level decision where factors that are largely outside the control of a business negatively impact the business's capacity to meet its tax payment obligations in a timely fashion. This is a deviation from the routine decision-making process, and therefore these decisions will be made at Higher Executive Officer, Assistant Principal or Principal level within the Office of the Revenue Commissioners. A Debt Management Coordination Group of the Revenue Commissioners will be responsible for ensuring consistency of approach across debt management groups throughout the State.

The key determinant for Revenue in deciding to deviate from the routine decision-making process will be whether the business concerned is viable and can show a capacity and commitment to meet all future tax payment obligations when they fall due. The extent of the leeway that Revenue will be prepared to give to a taxpayer will be "significantly influenced by the level and timeliness of meaningful engagement by the business in the first instance", according to the guidelines. It is therefore critical that taxpayers engage with Revenue as early as possible if there is a risk that they may be unable to pay their taxes, as a failure to do so will be considered "a serious escalation of the risk" from Revenue's point of view and may result in the enforcement measures outlined earlier in this article coming into play.

The considerations that may arise for Revenue under the new CDEF are deemed not to be publishable under the Freedom of Information Act 1997, and therefore it is not clear exactly what approach Revenue will take under the guidelines. However, guidelines state that the considerations may include a phased payment arrangement. The information that the taxpayer will need to provide to justify consideration for

a phased payment arrangement is stated to include:

- › realistic cash-flow for the following six months,
- › an up-to-date debt profile,
- › up-to-date management accounts,
- › an outline of how the proposed repayment schedule will be serviced,
- › up-to-date bank statements that will allow Revenue to take a view on whether there are increasing excesses on the account and to take a view on the extent of the account swing and
- › aged debtor and creditor profile.

In practice (since the publication of the CDEF guidelines) the Revenue Commissioners have also been seen to request a general background on the taxpayer's business and details of the measures that the taxpayer has taken to cut costs (i.e. the operation of reduced working hours, redundancies, sourcing cheaper suppliers etc.). This is largely in line with the general requirements in relation to agreeing an instalment arrangement with Revenue that existed before the publication of the CDEF guidelines.

It would be hoped that, for taxpayers with viable businesses who experience trading and/or cash-flow difficulties, the payment terms that could be agreed under the CDEF will be linked to the taxpayers' projected cash-flows, as opposed to the more rigid time limits that Revenue would have imposed in the past. One would also expect deferred payment arrangements to be an option that would be considered in certain cases.

The rate of interest charged on late payment of tax in Ireland is very high. As mentioned earlier in this article, the stated aim of the imposition of interest on late payment of tax is to ensure a level playing field between taxpayers who pay

their tax on time and those who do not. However, the interest rates of 10% and 12% per annum are excessive, particularly when compared to current commercial lending rates of c. 5.5% or to the UK rate of interest on late payment of tax of 4.5%. The interest rates charged by the Revenue Commissioners obviously go far beyond the stated intention behind the imposition of interest, which is to create a level playing field between the compliant and the non-compliant taxpayer. This is an area that needs to be addressed, and one would hope that there will

also be scope for interest to be waived or possibly applied at a reduced rate under the CDEF guidelines.

### Conclusion

As details of the arrangements or considerations that may be made under the CDEF guidelines have been deemed not to be publishable under the Freedom of Information Act 1997, it remains to be seen what form these arrangements will take in practice.

Through the issue of the CDEF guidelines, Revenue has demonstrated its awareness that it needs to avoid falling into the trap of being "penny wise and pound foolish" when carrying out its tax collection and enforcement duties, particularly in the current economic climate.

The effectiveness of the CDEF guidelines will very much depend on the Revenue Commissioners' ability to identify and apply leniency to the taxpayer who "can't" pay his or her taxes while continuing to apply the normal tax payment, collection and enforcement rules to the taxpayer who simply "won't" pay. It is very important that this balance is achieved, as the economy needs its financially viable taxpayers to remain in business so that they can continue to contribute much-needed tax revenues into the future.

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