Revenue audit

This article is based on Revenue Audit Code of Practice 2010, which is effective from 1 October 2010 and is relevant for candidates sitting Paper P6 (IRL) from June 2012 onwards. The Code of Practice 2002 and transitional measures dealing with cases where a default occurred prior to 24 December 2008 is not examinable for the June 2012 sitting onwards. The requirements of the Paper P6 (IRL) syllabus in respect of Revenue audit is set out below:

‘The procedures relating to Revenue audit/enquiries, appeals and disputes’

This article is intended to clarify the level of knowledge required by candidates for the purpose of the Paper P6 (IRL) syllabus. As set out in the recent examiner’s presentation, candidates should be able to identify tax issues from a given scenario, assess the likely implications of any tax defaults being identified under a Revenue audit, advise clients of the conduct of an audit and their options in terms of disclosure and settlement with Revenue. The areas of study should include:

- what is a Revenue audit and how taxpayers are selected for audit
- the types of tax defaults, taxpayer disclosure options and penalty exposures
- the types of audit, conduct of an audit and settlement
- the Revenue powers – routine powers, search and seizure powers, access to information (for example, financial institutions)
- position of adviser.

Note: Revenue investigations will not be examined.

Revenue audit

A Revenue audit is ‘an examination of a tax return; a declaration of liability or a repayment claim; a statement of liability to Stamp Duty, or the compliance of a business with tax and duty legislation’ (Revenue Audit Code of Practice 2010). The intention is to establish the correct level of tax liability. All chargeable persons, inclusive of self-assessed individuals and companies, may be selected for audit.

A chargeable person may be selected for audit randomly. Audit cases are also selected based on a particular economic sector – for example, solicitors, nightclubs, dentists, or from risks identified using risk analysis profiling methods. A Revenue audit may examine compliance under all tax heads. The Revenue audit will examine the books and records of the taxpayer to establish if there is any tax default and if so, to reach a settlement with the taxpayer and ensure future compliance to the tax code.
Types of tax defaults, taxpayer disclosure options and penalty exposures

Types of tax defaults
The Finance Act 2008 set out the new categories of tax default and these are incorporated into the Code of Practice 2010. The tax default categories are as follows:

- **Deliberate behaviour** – this term is not defined in the legislation. In general, deliberate behaviour involves a breach of a tax obligation where there is intent on the part of the taxpayer and so does not qualify as careless behaviour. Examples of deliberate behaviour include failure to maintain books and records, omission of transactions from the books and records, providing false or misleading information.

- **Careless behaviour with significant consequences** – ‘careless’ is defined in the act as a failure to take reasonable care. ‘Significant consequences’ applies where the tax underpaid is greater than 15% of the correct tax payable for the relevant period. Examples of careless behaviour include failure to take advice, neglecting to categorise expenditure into allowable and disallowable categories for tax purposes, insufficient standard of record keeping in the business.

- **Careless behavior without significant consequences** – this category relates to defaults of a minor nature that are discovered during a Revenue audit, for example, computational errors and inadequate adjustments for personal expenditure in the profit and loss account. This category arises where the tax underpaid is less than 15% of the tax liability ultimately due.

Taxpayer disclosure options
Where a taxpayer has identified an error in their returns, there are a number of options available to them to regularise this. They can **self-correct** without incurring a penalty within a specified timeframe:

- For VAT purposes, the self-correction must take place before the due date for filing the income tax return for the chargeable period within which the relevant VAT period ends.
- For income tax, the self-correction must take place within 12 months of the due date for filing the return.

The taxpayer must apply in writing to the Revenue setting out the adjustment to be made, attaching a corrected computation of the tax liability and enclosing payment of tax, plus statutory interest. This option is not available if the taxpayer has already been notified of a Revenue audit or investigation.
Alternatively, the taxpayer may declare an *innocent error*. Where an auditor is satisfied that the underpayment of tax arose through innocent error, no penalty will apply. In determining whether the innocent error treatment will apply, Revenue consider whether the tax underpaid is less than €6,000, whether the taxpayer has a good compliance record or whether they had frequent errors.

Similarly, a penalty will not apply to a technical adjustment, described as adjustments to a tax liability, arising from differences in the interpretation or the application of legislation. The auditor must be satisfied that the taxpayer had taken due care, and the treatment used was based on a reasonable interpretation of the law. Where a taxpayer has not paid a tax liability which in future would be refunded, the Revenue may decide not collect this tax, or interest on this tax, where the taxpayer can prove that there is *no loss of revenue*. This treatment is concessional and the Revenue is mandated to ensure the correct operation of the tax so as to maintain its integrity. In determining whether to allow this concession, Revenue considers the taxpayer’s compliance record and level of co-operation with the Revenue. Where the concession is denied, a penalty of up to 9%, subject to a monetary limit may apply.

Finally, the taxpayer may opt to make a *qualified disclosure* to the Revenue. A qualified disclosure may be prompted (made after notification has been received of a Revenue audit), or unprompted (voluntary). In either case, the disclosure must be in writing to the Revenue, signed by or on behalf of the taxpayer and contain a declaration that to the best of the person’s knowledge and belief it is correct and complete. It must be accompanied by payment of the underpaid tax and interest. The amount of interest is calculated based on the category of tax default under which the disclosure is made (see ‘Types of tax defaults’ above). The penalty need not be included; however, it is necessary to specify under which category of tax default the disclosure applies to so as to determine the scope of tax liabilities to be included:

- where a disclosure is made under the deliberate behaviour category, it must include the amount of all liabilities to tax and interest, in respect of all tax-heads and periods, where liabilities arise
- where the disclosure is made under the careless behaviour category and
  - is a prompted qualifying disclosure, it must include the amounts of all liabilities to tax and interest in respect of the relevant tax-heads and periods within the scope of the proposed audit
  - is unprompted, it must include the amounts of all liabilities to tax and interest in respect of the tax-head and periods that are the subject of the unprompted qualifying disclosure.

Where a qualifying disclosure is made, there will be no publication of the taxpayers name or the settlement reached, no prosecution and a mitigation of
penalties depending on the level of tax default and co-operation (see Table 1 below).

Penalty exposure
The level of penalty applied depends on the type of disclosure made, the category of tax default and the level of co-operation by the taxpayer with the Revenue. Co-operation is very important and includes the taxpayer having all books and records available for the auditor, appropriate personnel available at the time of the audit, responding promptly to all requests for information, explanations, and prompt payment of the audit settlement liability, if any.

The penalty is a tax-geared penalty, calculated as a percentage of the underpaid tax and is set out in the Code of Practice 2010. In relation to a default due to deliberate behaviour, the penalty is set at 100% of the underpaid tax. For defaults under careless behaviour with significant consequences, the penalty is 40% of the underpaid tax and for careless behaviour without significant consequences the penalty is 20% of the underpaid tax. Where a qualifying disclosure is in place, the penalties are mitigated as follows:

<table>
<thead>
<tr>
<th>Penalty Table</th>
<th>Category of Default</th>
<th>Qualifying Disclosure Finance (No. 2) Act 2008</th>
</tr>
</thead>
<tbody>
<tr>
<td>All defaults where there is a qualifying disclosure</td>
<td>Penalty table for defaults that occurred on or after 24/12/2008</td>
<td>Prompted qualifying disclosure and co-operation</td>
</tr>
<tr>
<td>All defaults where there is a qualifying disclosure in this category</td>
<td>Careless behaviour without significant consequences</td>
<td>10%</td>
</tr>
<tr>
<td>First qualifying disclosure in these categories</td>
<td>Careless behaviour with significant consequences</td>
<td>20%</td>
</tr>
</tbody>
</table>

Where agreement cannot be reached with the taxpayer on the amount of penalties, Revenue can instigate court proceedings to have the court decide on the penalties applicable.

Types of audit, conduct of an audit and settlement
In the event of a notification of a Revenue audit, but before the examination of the books and records have begun, the taxpayer may make a prompted disclosure. This notification must be made within 14 days of the notice being
issued. A postponement of the audit will then be allowed for 60 days in order for this disclosure to be made.

The audit may take the form of a desk audit or at the taxpayer’s business location. The auditor would normally seek to:

- ascertain the nature of the business, identify those responsible for maintenance of the records and list the records kept
- examine the books and records, in whatever format held, both for completeness and the treatment of transactions having regard to tax and accounting principles
- check that all relevant returns have been made and are complete in accordance with the records
- make whatever enquiries are necessary for the audit
- advise the taxpayer of any errors, omissions or irregularities in the tax returns submitted (including those in the taxpayer’s favour), determine liability if it arises, request settlement and specify any action that may be required to place the taxpayer on a compliant footing
- conduct a physical and documentary walkthrough of premises to verify on-going compliance with criteria or conditions laid down in authorisations for certain customs procedures.

The Customer Service Charter sets out how the taxpayer can expect to be treated by the Revenue and, similarly, Revenue expectations from the taxpayer. The taxpayer has the right to seek a review of the conduct of the audit. If the taxpayer still considers that the proposed settlement is unacceptable, they may formally appeal to the Appeals Commissioners, provided that an appeal has been lodged within the statutory timeframe.

**Revenue powers in an audit situation**

This section is focused on the Revenue powers in an audit situation and is not a comprehensive review of Revenue powers overall. The Finance Act 1997 sets out the legislative basis for Revenue powers during an audit as ‘the inspector’s right to make enquiries to satisfy himself as to the accuracy of the returns made’. The Revenue also has the right to require books, records and certain other documents to be made available for inspection where a specific enquiry is being made.

The Revenue can request:

- the taxpayer to provide a statement of affairs setting out all of their assets and liabilities on a specified date
- third parties, such as suppliers and customers, to deliver or to make available for inspection any books and records or information and explanations in relation to a taxpayer that may be relevant to the taxpayer’s liability to tax
• financial institutions to make available details of accounts and financial transactions, which may be material in determining the taxpayer’s liability.

During the course of an audit, the Revenue may suspect that serious tax offences have occurred and can reconstitute the audit as an investigation. In this case, the Revenue powers are enhanced and include access to a business premises without a search warrant to inspect documents, remove business records and seek further documentation. The Finance Act 2007 further extends Revenue powers to allow them obtain a search warrant to be used where criminal prosecution is intended.

Position of adviser
The Finance Act 1995 introduced ‘aiding and abetting’ provisions whereby if an adviser is knowingly involved in, or facilitates the fraudulent evasion of tax, this constitutes an offence and is liable to a fine and/or imprisonment. The Finance Act 1997 obliges advisers who become aware of a material non-compliance or tax evasion of a client to report this to the client to rectify and request that they report it to Revenue. If, after six months, this has not been rectified, the adviser must cease to act for the client and advise Revenue of their retirement.

Conclusion
Revenue audits have continued to increase in number in recent years and this trend is likely to continue. Consequently, it is important for candidates to be familiar with the procedure and options available to taxpayers in the event that they have an undeclared tax liability or indeed are selected for audit. The Revenue Audit Code of Practice 2010 is available on the Revenue website (Revenue.ie).

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