



An Analysis on Revenue Collection

December 2017



Ministry for Finance
An Analysis on Revenue
Collection

Financial Year 2016

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List of Abbreviations

BO	Budget Office
CDU	Customs Debt Unit
CES	Customs Electronic System
CR	Commissioner for Revenue
CTD	Capital Transfer Duty
DOC	Department of Customs
EU	European Union
FSS	Final Settlement System
IRD	Inland Revenue Department
IT	Information Technology
ITU	International Tax Unit
MFIN	Ministry for Finance
MITA	Malta Information Technology Agency
NAO	National Audit Office
SSC	Social Security Contributions
TCU	Tax Compliance Unit
TOR	Traditional Own Resources
UCA	Urban Conservation Area
UCC	Union Customs Code
VAT	Value Added Tax
WCO	World Customs Organisation
YA	Year of Assessment

Executive Summary

Scope

- To collate and assess the procedures in place and the revenue collected by the Inland Revenue Department (including the Capital Transfer Duty), VAT Department and the Department of Customs during 2016.
- To report on the level of enforcement procedures in place in relation to the collection of revenue.
- To enquire about the status of the integration between the three main revenue-generating Departments, necessary to strengthen and consolidate the Maltese fiscal structure, and increase sustainability.

Methodology

The NAO conducted detailed research in relation to the composition and collection of these types of revenue. Questionnaires were then compiled and sent to each of the respective Departments, as well to the Commissioner for Revenue dealing separately with the merger aspect.

A meeting was held with Senior Management of the three Departments, during which this Office discussed in detail the questionnaires, as well as the scope of this analysis.

As far as possible, the figures and information provided were analysed by the NAO. Information from the Financial Estimates, as well as from various Ministry for Finance Annual Reports, was also used.

Revenue Analysis

The mode of collection and analysis of income generated by the three main revenue-generating Departments during 2016 included a five-year trend analysis of income. Most noticeably, a €329.5 million increase in absolute terms resulted in Income Tax over these five years, with the highest spikes in Capital Gains Tax for 2014 (25%), Provisional Tax in 2015 (21%) and Duty on Documents and Transfers in 2015 (29%). A steady upward trend in VAT income was also noted since 2012, with a total increase of €191 million.

With regards to the Department of Customs, a €124.1 million increase in income was reported, which was mostly due to significant increases in Import and Excise Duties in 2014 and 2016 over the previous years.

Enforcement Action

The most commonly enforcement tool used by the Inland Revenue Department was Remission of interest agreements in relation to arrears of company tax and tax due by individuals, which totalled 744 during 2016 and contributed to the collection of circa €4 million by 31 May 2017.

Similarly, the VAT Department entered into 92 Remission Agreements, generating €3 million. This, in addition to the issue of 760 Demand Notices, 59 Judicial Letters, as well as 137 Civil Court sittings.

Legal action taken by the Department of Customs included 118 and 32 Criminal and Civil Court cases respectively. The Department also settled 111 cases out of Court, issued 18 Letters to Prosecute and 265 Seizure Notes.

Staff Complement

Due attention needs to be given to the various staffing requirements across these Departments.

Integration of Revenue Departments

Various measures are being implemented to support the adoption of the merger, including a consolidated Commissioner for Revenue website, a One Stop Shop, a Joint Enforcement Unit, Consolidated Debt Collection and a Call Centre. A Permanent Secretary (Merger and Administration) within the Ministry for Finance was appointed, but to date, although crucial, the critical post of Director General Support Services is as yet vacant.

A contractor has also been identified to analyse all the processes involved. The implementation date for the merger is set for December 2018.

Chapter 1

Introduction

1.1. Background

Estimated revenue for 2016 with respect to the three main revenue-generating Departments within the Ministry for Finance (MFIN), namely the Inland Revenue Department (IRD)¹, the Value Added Tax (VAT) Department and the Department of Customs (DOC), amounted to €1,301,035,000, €736,481,000 and €288,875,000, respectively.

In brief, the main responsibilities of the three Departments are as follows:

- Inland Revenue Department

The IRD is in charge of the administration of the Income Tax and Capital Transfer Duty (CTD) Acts and the enforcement of the collection of Social Security Contributions (SSC).

- VAT Department

The VAT Department is responsible for the collection and management of the VAT in line with the VAT Act (Cap. 406) and other pertinent Legal Notices.

- Department of Customs

The DOC is entrusted with the control of imports and exports of goods, as well as for the collection of the respective taxes and duties, as mandated in the relevant Acts.

The Commissioner for Revenue Act (Cap. 517), enacted on 20 January 2012, established that the role of the Commissioner for Revenue (CR) is to oversee the integration and management of the revenue Departments, above mentioned. The aim of merging these Departments into one entity is to strengthen the revenue streams and consolidate the Maltese fiscal structure, thereby increasing sustainability, which is essential in the rapidly changing economic scenario.

¹ Including the Tax Compliance Unit (TCU) and CTD.

1.2. Scope

The scope of the analysis was to collate and assess revenue collected by the IRD², the VAT and the DOC during 2016. The level of enforcement procedures in place in relation to the collection of revenue was also reported upon. Moreover, this Office enquired about the status of the integration between the main three revenue-generating Departments.

1.3. Methodology

The National Audit Office (NAO) conducted detailed research in relation to the composition and collection of revenue. Amongst others, performance audit reports conducted by foreign Supreme Audit Institutions were referred to, particularly with regard to the efficiency and effectiveness of debt collection. These reports also put forward areas for further consideration, including the use of External Debt Collection Agencies, as well as the adoption of management information systems.

On the basis of the research carried out, this Office sent a total of four questionnaires, one to each of the respective Departments and another to the CR relating to the merger³. A meeting was held with the Senior Management of these three Departments, during which this Office explained thoroughly the scope of this analysis and the questions included in each questionnaire. Following a review of the submitted information, the NAO eventually asked for further clarifications from each of the Departments.

An analysis of the figures quoted in the replies to the questionnaires was conducted by the NAO. Information from Financial Estimates and MFIN Annual Reports pertaining to various years was also used in this exercise, the results of which are portrayed throughout this Report. Unless otherwise stated, all the figures quoted in the tables throughout this Report were provided by the respective Departments.

This Office is also in receipt of statements of Arrears of Revenue for each of the three Departments, an analysis of which is presented in the Report by the Auditor General – Public Accounts 2016.

Financial Estimates 2016

Communication by the NAO with the Budget Office (BO) showed that revenue projections required as part of the 2016 budget preparatory process were initially prepared by the respective Departments as per MFIN Circular No. 1/2015 - '2016 – 2018 Business and Financial Plans'. Each Department provided its three-year revenue projections, in response to said Circular. However, during the meeting held with Senior Management, information collected by the NAO suggested that a top-down approach was being adopted with regard to revenue projections and that ultimately, the revenue targets for the year 2016 were those set by MFIN.

It was also confirmed that while departmental projections were submitted to MFIN in the first quarter of 2015, the official budgetary estimates for 2016 were finalised late in the year, whereby the BO had a

² Excluding income from the International Tax Unit (ITU).

³ Referred to in this Report as Merger Questionnaire.

better picture of the relevant revenue trends, including any planned budget measures and their impact on projected revenue.

Upon request by the NAO, the BO provided the revenue projections submitted by each of the three Departments. Subsequently, these figures were compared to the amounts included in the Financial Estimates for the year 2016. It was noted that the published estimated revenue figures provided by MFIN exceeded the ones submitted by each of the Departments. Differences noted are detailed in Table 1.

Table 1: Analysis of Projections by Departments against Financial Estimates for 2016

Department	Projected by	As per Financial	Variance	
	Department	Estimates	€	%
	€	€		
IRD	1,160,328,000	1,301,035,000	140,707,000	12
VAT	715,011,000	736,481,000	21,470,000 ⁴	3
DOC	262,755,000	288,875,000	26,120,000	10

(Source: Financial Estimates 2016, pages 187-188)

Whilst each Department submits its projections in the first quarter of the year, the final 2016 Financial Estimates were presented in Parliament in October 2015.

It was confirmed that throughout the year ongoing discussions were held between the BO and the respective Departments, through which the relative projections were updated to reflect any monthly performance fluctuations. Since current year performance serves as a baseline for the forthcoming year's estimate, estimated amounts reflect improvement, or otherwise. In addition, the Financial Estimates may be revised further due to various initiatives deemed necessary at any given point in time, including increased enforcement measures.

Subsequently, the Economic Planning Division within MFIN performs independent forecasts through econometric modelling, where the macroeconomic performance and outlook are assessed for each revenue item. Ongoing revisions are made during the analysis, with material variances analysed to establish the underlying assumptions, as well as to compare results. Towards the end of the process, the final estimates are the ones most compatible with the macroeconomic scenario for the year to which they refer.

Such estimates are provided net of any new initiatives, since such measures only become known as the annual National Budget approaches. Consequently, targeted revenue to be derived from such initiatives would have to be reflected at a later stage accordingly. In addition, the Financial Estimates may be further revised due to various initiatives deemed necessary at any given point in time, including increased enforcement measures and higher collection of revenue arrears.

⁴ Part of this variance related to a financial estimate made in respect of a new item, being Environmental Contribution which was not projected by the Department at that time, and which amounted to €6,250,000.

Chapter 2

Inland Revenue Department

2.1. Revenue Generation

The Financial Estimates for the year 2016 for the IRD presented figures as per Table 2 below.

Table 2: 2016 Estimates in relation to the IRD

Revenue Category		Estimate 2016 €
Licences, Taxes and Fines		
0232	Duty on Documents	94,000,000
0243	Death and Donation Duty	1,000
Income Tax		
0171	Income Tax	1,206,700,000
Fees of Office		
0304	Legal Costs and Fees	10,000
0309	Fees for permits for the acquisition of immovable property by Non-Residents	60,000
0345	Participation fees in Department's Tenders	1,000
0349	Miscellaneous fees	12,000
Interest on Loans made by Government		
0679	Others	1,000
Miscellaneous Receipts		
0999	Miscellaneous Receipts	250,000
Total		1,301,035,000

(Source: Financial Estimates 2016, page 187)

The above figures show that the main revenue-generating items relate to the collection of Income Tax and the collection of Licences, Taxes and Fines, particularly Duty on Documents.

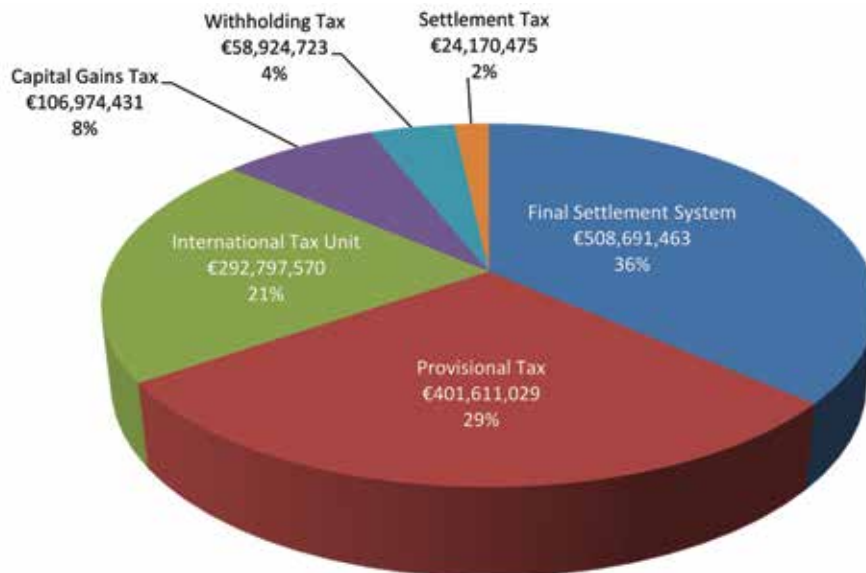
Figures presented by the IRD showed that during 2016, the gross revenue actually collected by the Department in relation to Income Tax amounted to €1,393,169,691, thus substantially higher than the budgeted figure. Of the collected amount, transfers to refunds amounted to €64,900,000 leaving a net revenue balance of €1,328,269,691. Furthermore, income from the SSC, including the State Contribution, totalled €804,388,726 bringing the total net collection up to €2,132,658,417.

The Department confirmed that it prepares its own monthly forecasts of expected revenues. In so doing, a number of considerations are taken into account, including past results and trends, changes in legislation, Financial Estimates and the knowledge of business, including timeframes for payments, as well as time lags for measures to take effect. The actual results of a particular month are subsequently matched with the departmental projections and any resulting variances are subsequently analysed within the Department itself. A number of factors are considered when assessing such variances including their magnitude (absolute or percentage), observed trends and the extent to which they can be attributed to fiscal or economic factors. Year-to-date data and business related factors are also considered.

The estimates originally submitted by IRD in relation to the Income Tax category amounted to €1,134,500,000⁵ whilst the amount eventually shown in the financial estimates presented by the BO was increased to €1,206,700,000, as mentioned above.

A breakdown of the 2016 gross Income Tax collected of €1,393,169,691 into the IRD’s main revenue-generating categories is portrayed in Chart 1.

Chart 1: Gross Income Tax 2016 Categories



The largest portion of revenue was generated from the Final Settlement System (FSS), which is a tax deduction methodology designed to produce accurate deductions from employees’ emoluments. At €508,691,463, it accounted for 36% of the gross revenue generated by the IRD during 2016.

The IRD’s top revenue-generating categories included Provisional Tax, which represented 29% of gross revenue. Maltese legislation includes provisions and rules on tax payments during the year in which the taxable income is generated. Accordingly, companies and self-employed individuals must make provisional tax payments in April, August and December of every year, based on the prior year’s earnings. In addition, the Provisional Tax category also includes payments for Self Assessment, Part-time Self Employment, Tax at Source, Payments in Terms of Article 73 and Agriculture Produce Scheme in relation to individuals. Same category also includes Company Tax, Tax at Source, payment in terms of Article 73, profits taxed at 32.5% topping-up as well as tax on dividend from untaxed account in relation to Companies.

⁵ This amount excludes budgeted refunds of €75,000,000.

The Department confirmed that figures for the ITU, which accounted for 21% of gross income, represent transfers of monies from Central Bank of Malta bank accounts, managed by the Unit itself, to the Public Account. These amounts are recognised as revenue on the day such transfers take place. The aim of this Unit is to support the development of Malta as an international financial and business centre.

Other categories of income include Capital Gains Tax, Withholding Tax and Settlement Tax, which collectively represented 14% of gross revenue.

2.2. Variance Analysis

The actual amounts collected by the IRD during 2016 were in excess of the targeted revenues as analysed in Table 3.

Table 3: Variance Analysis of Estimated against Actual Revenue 2016 – Income Tax and SSC

Revenue Category	Estimated Revenue €	Actual Revenue Collected €	Variance	
			€	%
Income Tax Revenue net of Refunds	1,206,700,000	1,328,269,691	121,569,691	10
SSC ⁶ including State Contribution	785,700,000 ⁷	804,388,726	18,688,726	2
Totals	1,992,400,000	2,132,658,417	140,258,417	

(Source: Financial Estimates 2016, pages 187, 248)

In both instances, the collected amounts exceeded the targeted revenue, with the result that the aggregate amount collected was of €140,258,417 more than that estimated.

Further analysis into the Income Tax revenue variance was carried out by the NAO. However, since the estimated income figure as per the Financial Estimates was given as one lump sum, the breakdown used for analysis purposes had to be the unofficial projected figure prepared by the IRD, gross of refunds, which amounted to €1,209,500,000. For comparison purposes, the figures for actual revenue collected were also taken gross of refunds. Table 4 refers.

Table 4: Variance Analysis of Estimated Gross Revenue against Actual 2016 – Income Tax

Revenue Category	Estimated Gross Revenue €	Actual Gross Revenue €	Variance	
			€	%
FSS	465,000,000	508,691,463	43,691,463	9
Provisional Tax	405,000,000	401,611,029	(3,388,971)	(1)
Settlement Tax	27,500,000	24,170,475	(3,329,525)	(12)
Capital Gains Tax	97,000,000	106,974,431	9,974,431	10
Withholding Tax	64,000,000	58,924,723	(5,075,277)	(8)
Totals⁸	1,058,500,000	1,100,372,121	41,872,121	4

⁶ The SSC Class 1 and Class 2 are included in this figure.

⁷ Targets of income from the SSC are reported in the Financial Estimates under the Ministry for the Family and Social Solidarity.

⁸ Totals exclude figures in relation to the ITU.

When queried about the reported discrepancies, the IRD stated that in a complex fiscal environment characterised by many variables, it is difficult to attribute such variances to any one particular event or factor.

Nevertheless, it was explained that the highest positive variance of €43,691,463, registered under the FSS, is partly explained by the increase in the number of gainfully occupied persons and the resulting decrease in unemployment. These factors have yielded positive results, which exceeded the Department's expectations. Additionally, the 10% increase in Capital Gains Tax was linked to the number of preliminary agreements and deeds involving property transfers, which during 2016, were also higher than expected.

The IRD officials also stated that during 2015 there was a one-off concession for taxpayers to regularise their position with regard to rental income. As detailed by the IRD, this concession was most probably not given much consideration when the projections for 2016 were being calculated, hence resulting in a negative 8% variance in the withholding tax income category, as explained in Table 4.

A 12% negative variance was also noted in relation to Settlement Tax, which in monetary terms exceeded €3 million. According to the IRD, this discrepancy was partly attributable to the erroneous allocation between tax and additional tax with respect to the FSS agreements. It was further explained that due to the unavailability of specific software to cater for such agreements and the waiving, of related penalties, the allocation between the two categories of tax was not being computed correctly at the receipting stage. Hence the 2016 trends were skewed upwards and consequently led to this negative variance.

Similar issues were also noted in the discrepancies relating to the Additional SSC (Penalties), which resulted in a 64% negative variance. In this regard, the IRD further stated that due to the software limitations as explained above, the trends over the period 2013 to 2015 indicated that the actual additional SSC for 2016 should have been closer to the projected amount. Table 5 further refers.

Table 5: Variance Analysis of Estimated against Actual Revenue 2016 – SSC

Revenue Category	Projected Revenue	Actual Revenue	Variance	
	€	€	€	%
SSC - Class 1	473,800,000	493,181,250	19,381,250	4
SSC - Class 2	41,800,000	42,435,152	635,152	2
Additional SSC (Penalty)	6,000,000	2,180,561	(3,819,439)	(64)
State Contribution	257,800,000	266,591,763	8,791,763	3
Totals	779,400,000⁹	804,388,726	24,988,726	3

⁹ This figure differs from the Budgeted Revenue as per Table 3 because the €779,400,000 is the unofficial projected figure calculated by the IRD, whilst the figure in Table 3 equates to the Financial Estimates provided by the BO.

Tax Rate Adjustment

The Department was also queried about the effects of the budget measure to gradually reduce Income Tax rates over the past years, from 35% to 25%, on individual income that does not exceed €60,000 per annum. The NAO was informed that studies have in fact been effected both before and after the introduction of this measure. The analysis provided is reproduced in Table 6.

Table 6: Assessment of Income following Tax Rate Adjustment

Year of Assessment (YA)	Difference in Tax €
2014 (compared with YA 2013 from 35% to 32%)	15,497,846
2015 (compared with YA 2014 from 32% to 29%)	19,493,001
2016 (compared with YA 2015 from 29% to 25%)	27,077,769

The IRD explained that the figures presented relate to the difference in tax on the declared chargeable income in any particular year when applying the reduced rates, as compared to the applicable rate of the year before.

2.3. Trend Analysis

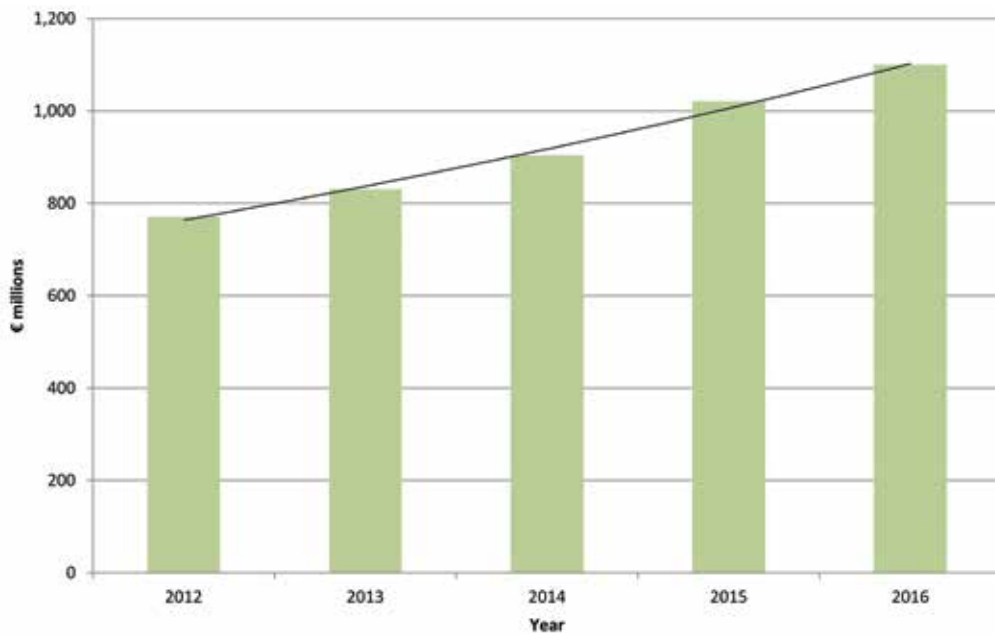
An analysis of the 2016 gross income broken down by category, was also carried out by comparing it to the income generated under the various revenue categories for the years 2012 to 2015, as shown in Table 7.

Table 7: Analysis of Gross Income Tax (2012 – 2016)

Revenue Category	2012 €	2013 €	2014 €	2015 €	2016 €
FSS	354,736,774	381,378,393	420,555,016	445,346,274	508,691,463
Provisional Tax	277,666,534	304,044,299	319,739,171	386,263,612	401,611,029
Settlement Tax	22,220,693	26,634,838	24,762,821	27,689,108	24,170,475
Capital Gains Tax	65,985,089	67,146,645	83,661,541	100,030,629	106,974,431
Withholding Tax	50,283,922	51,401,029	55,109,378	61,364,626	58,924,723
Totals	770,893,012	830,605,204	903,827,927	1,020,694,249	1,100,372,121

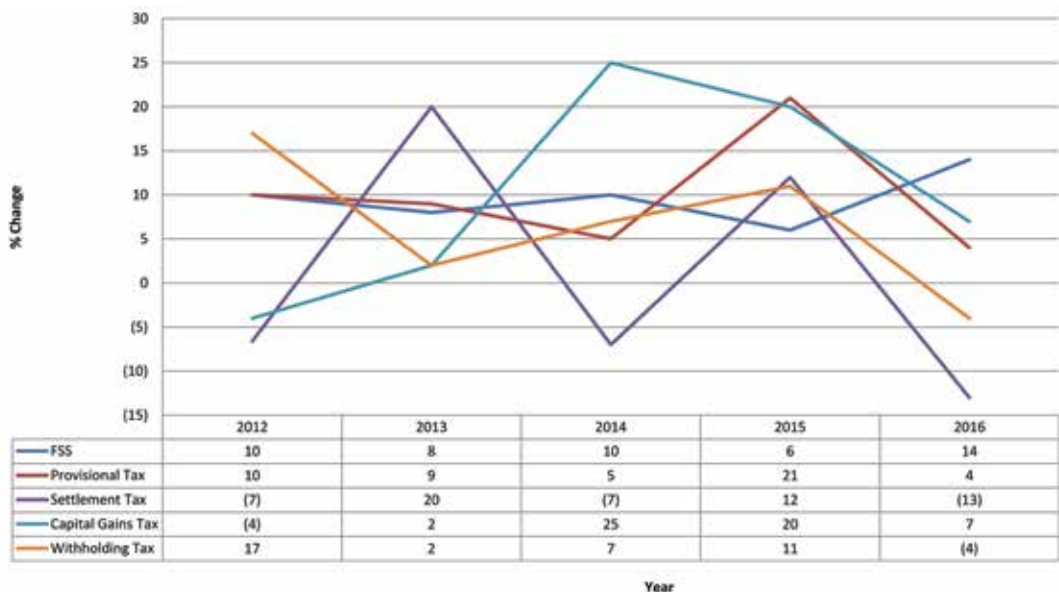
The above figures were charted and a trend line was extracted from the ensuing analysis. Chart 2 further refers.

Chart 2: Trend Analysis of Gross Income Tax (2012 – 2016)



The above shows that an upward trend was registered as regards to Income Tax collected over the period 2012 to 2016, where the increase in absolute terms amounted to €329.5 million. Notwithstanding the evident trend, further analysis has shown that income generated under the various Income Tax headings fluctuated substantially over the same period as shown in Chart 3.

Chart 3: Analysis of Gross Income Tax (2012 – 2016)

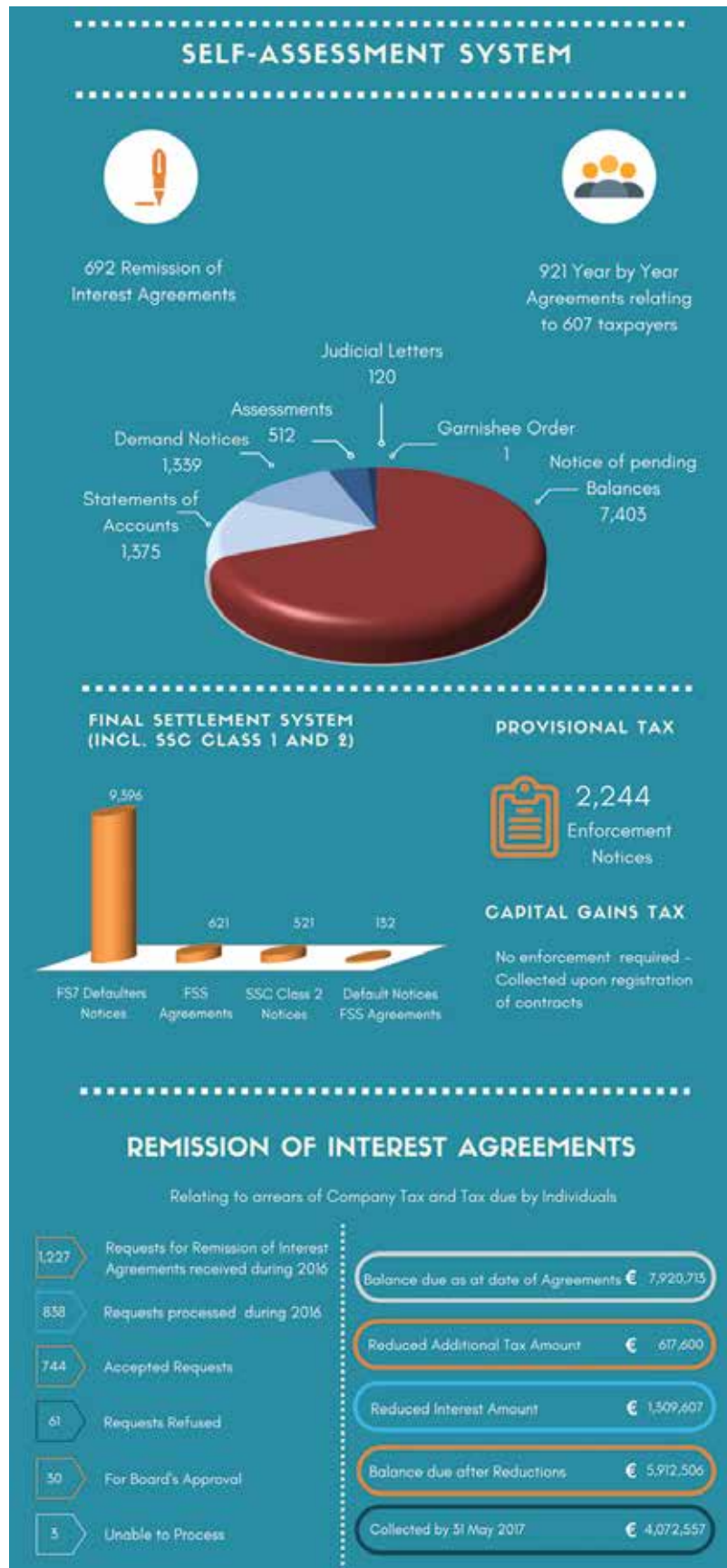


The Department was asked to comment about the major movements over the assessed period, especially in relation to unusual increases and decreases in the Provisional Tax, Settlement Tax and Capital Gains Tax categories. No detailed replies were forthcoming, except for stating that the explanations put forward regarding the variances between the actual revenue collected and the estimate would also generally apply to these recorded actual figures.

Furthermore, it is pertinent to note that no data was forthcoming in relation to arrears collection due to limitations in the system, as remarked by the Department.

2.4. Collection Procedures

A number of enforcement actions were taken by the Department during 2016 in order to pursue the collection of the amounts due under the various income categories.



The Department also confirmed that no enforcement action was taken in relation to Pre '99 balances and that the amount of circa €97,000 collected in this regard related to balances included in remission of interest agreements. During 2016, there were 70 such agreements that included Pre '99 balances. Similarly, because of its nature, no action was necessary in relation to the collection of Withholding Tax, since this is collected at source.

Furthermore, the IRD confirmed that there were a number of cases in Court during 2016, as is further portrayed below.



Following the NAO enquiry, it was also confirmed that no further analysis is made by the Department to assess the effect of the reduction of interest and penalties vis-à-vis tax settled from the five-year agreements in relation to the FSS and the SSC.

Nevertheless, as a means of further enforcement, the IRD stated that the Computer Liaison section draws up, on a monthly basis, FSS/SSC Status Reports as well as TCU and Audit Reports. The latter show the balances due by taxpayers that were investigated by the TCU and the Audit section within IRD, and are forwarded to the Collection section for necessary action to collect the amounts due. Other reports are also available on an ad hoc basis.

2.5. Capital Transfer Duty

As portrayed in Table 2, €94 million were estimated with respect to income from Duty on Documents for the year 2016. From figures presented by the Department, it transpired that the total actually collected during 2016 amounted to €135,325,826, i.e. a 44% increase over the estimated revenue amount. Of the total sum collected, €134,566,696 related to fees from 2016, whilst the remaining balance of €759,130 was settled against past arrears.

Further enquiry regarding the positive variance registered revealed that this increase can be partially attributed to the First Time Buyers Scheme, enacted back in 2013, which has seen a steady increase in the number of immovable property related contracts registered every year. Through this Scheme, property transfers made between 5 November 2013 and 1 January 2018, are subject to an exemption on the amount of Duty on Documents due on the first €150,000 of the property's value, given that said immovable property is the first to be acquired inter vivos by the transferee. The Department further confirmed that the number of contracts for first time buyers registered during 2016 was 2,578.

Even though this Scheme can be considered as a main contributor to the positive variance, other stamp duty relief schemes such as the Urban Conservation Area (UCA) Scheme, together with other positive economic factors can also be attributed to the increase in contracts, and thus to the increase in revenue. In fact, under the UCA Scheme, a transfer inter vivos of immovable property situated within a UCA during 2016 was subject to a reduced rate of Duty on Documents of 2.5%.

Trend Analysis

An analysis of income collected over the past five years (2012 to 2016) in relation to Duty on Documents and Transfers was also conducted by this Office. Charts 4 and 5 further refer.

Chart 4: Trend Analysis of Duty on Documents and Transfers (2012 – 2016)

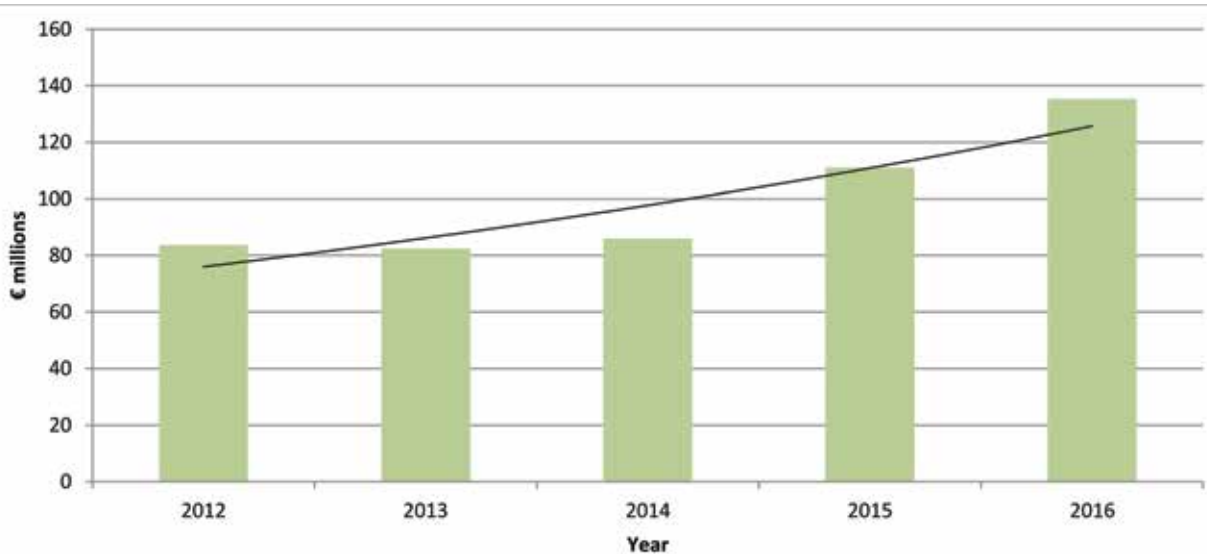
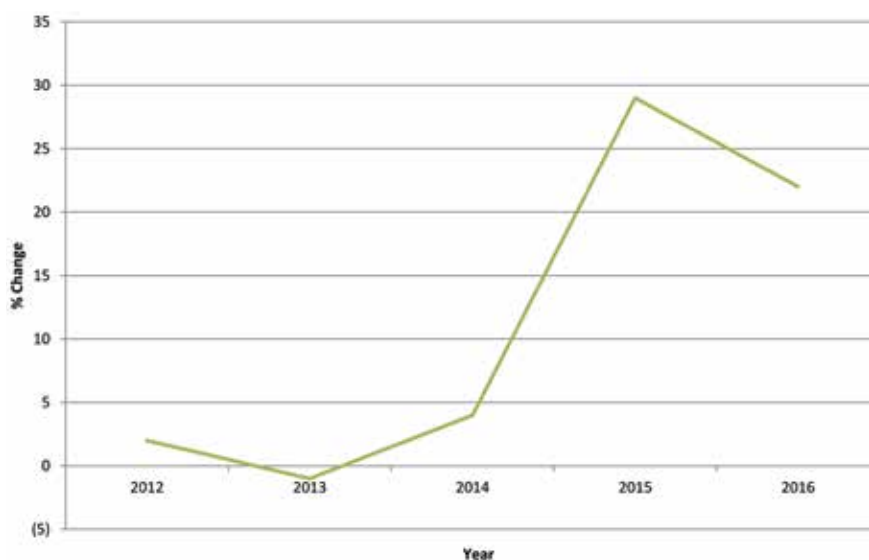


Chart 5: Analysis of Revenue from Duty on Documents and Transfers (2012 – 2016)

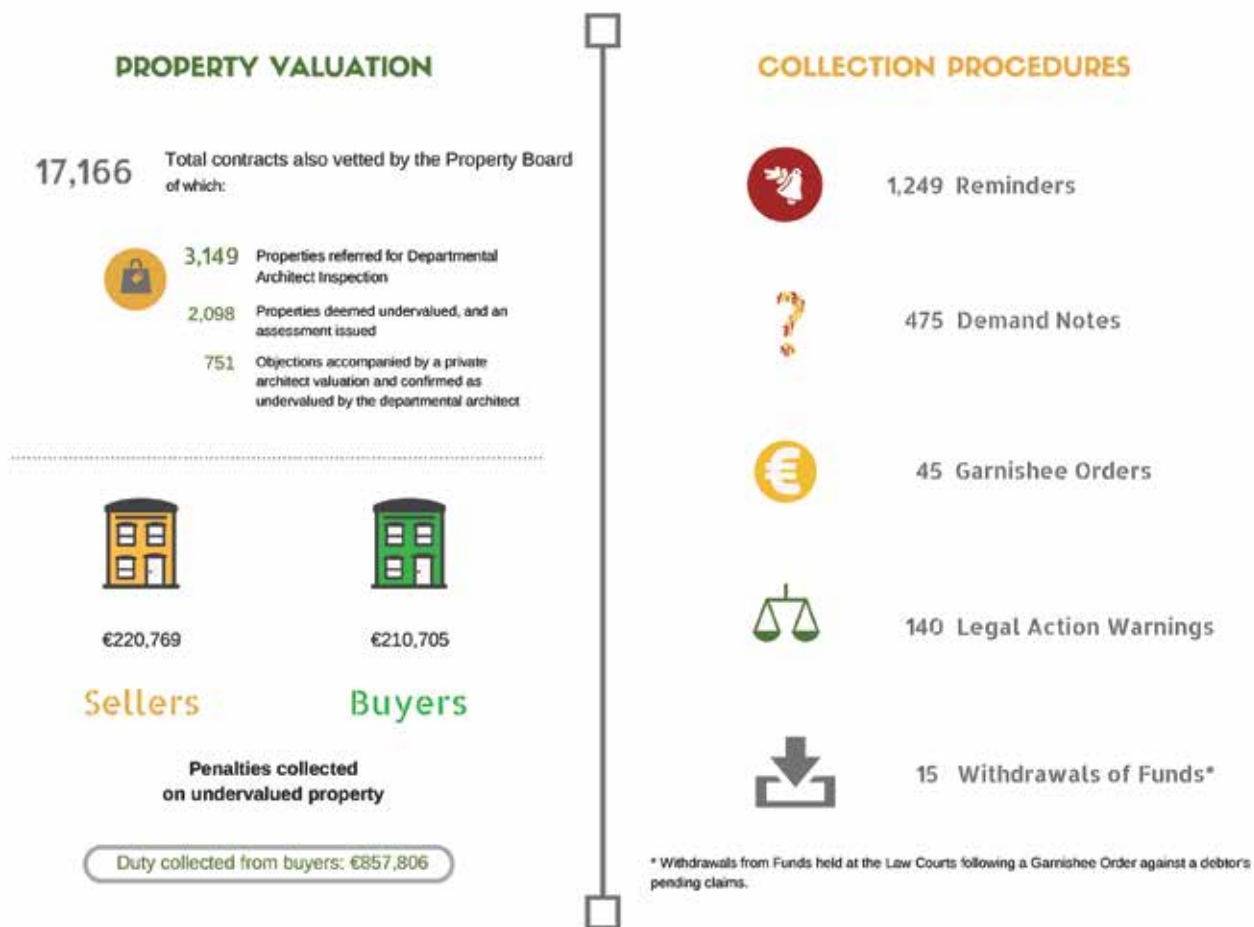


An upward trend was noticed since 2013 (Chart 4), however a noticeable spike was present between the income of 2014 and that registered in 2015 (Chart 5). When queried about it, the Department confirmed that this increase can also be attributed to the various stamp duty relief schemes availed of during these years.

Collection Procedures

Collection procedures in relation to the CTD are mainly Information Technology (IT) based, controlled and targeted to ensure that the necessary action is taken in a timely manner and that no legal procedures are overlooked.

Capital Transfer Duty Enforcement Action



Dues from Notaries

The IRD also confirmed that with regard to arrears, the residual amounts due by notaries only represent interest on late filing of deeds since notaries always remit the full amount upon submission of contracts. The IRD then sends to each notary a breakdown of the amount due at the end of each month. The total balance due always stands in the region of €25,000.

Wrong Architect Valuations

The IRD also stated that the collection of extra capital gains tax is not provided for in the Duty on Documents and Transfers Act (Cap. 364), which is administered by the CTD. Both buyers and sellers are fined a penalty of 20% of the Duty on Documents due for understatement of property value as per Article 52(4) of the said Act. In fact, during 2016, additional revenue of €1,289,280 was collected from buyers and sellers from the CTD’s claims for duty and penalties on additional value of property.

2.6. Tax Compliance Unit

As part of the analysis, the NAO was informed that the Unit generated a total revenue of €48.65 million during 2016, arising from compliance and investigations exercises, but without a further split between revenue emanating from work carried out by the TCU and tax audits.

Moreover, even though the NAO queried on the number of investigations carried out by the TCU during 2016, as well as on the number of concluded cases during same year, such details were not made available.

It was confirmed that the Compliance and Investigations Directorate has the role to perform full blown investigations, limited-scope audits and aspect audits. It was also explained that apart from these customary audits, a new concept of voluntary compliance was put into action. Demand for this service is expected to increase drastically in the coming years.

During 2016, the Unit was also engaged in the ongoing process of amalgamating the various work processes related to compliance, inspections and investigations. This project is nearing completion and, according to the Department, it will be finalised during 2017.

Another achievement at the end of 2016 was the setting up of a Joint Enforcement Task Force, whose scope is to combat the black economy and ensure a level playing field for businesses. This Task Force functions through the Inspectorate Unit in collaboration with the Anti-Fraud Unit.

2.7. Maternity Benefit Fund

Since July 2015, the IRD has been collecting maternity benefit contributions from employers. These contributions are subject to the necessary reconciliations and verifications, and the collected amounts are periodically transferred to the Board of Trustees, which is independent from Government and responsible for the administration of the Fund. A total of €8,838,699 was collected during the period July 2015 to May 2017, i.e. since the inception of the Fund.

It was also confirmed that by way of enforcement, the FSS section is rejecting end-of-year documents which do not include details of the Maternity Fund due. Furthermore, Malta Enterprise is requesting Compliance Certificates at the application stage of a number of its support measures to amongst others, ensure that the applicant is not defaulting Income Tax and Social Security Payments (which also include this Fund).

Chapter 3

VAT Department

3.1. Variance Analysis

The total revenue collected by the VAT Department during the financial year 2016 amounted to €726,280,519. This was predominantly made up of VAT collected, which totalled €724,798,345.

Table 8: Variance Analysis of Estimated against Actual Revenue 2016 – VAT

Revenue Category	Estimated Revenue	Actual Revenue			Variance	
		Arrears	Arising from 2016	Total	€	%
	€	€	€	€		
VAT	729,000,000	7,854,736	716,943,609	724,798,345	(4,201,655)	(1)
Eco-Contribution	1,220,000	119,114	1,342,380	1,461,494	241,494	20
Other Revenue	10,000	-	20,680	20,680	10,680	107
Totals	730,230,000	7,973,850	718,306,669	726,280,519	(3,949,481)	

(Source: Financial Estimates 2016, page 187)

A comparison of the actual amounts collected against the respective estimated figures revealed an adverse variance with respect to VAT of €4,201,655 as shown in Table 8.

Table 9: Variance Analysis of Projections against Financial Estimates 2016 – VAT

Revenue Category	Projected by Department	As per Financial Estimates	Variance
	€	€	€
VAT	709,000,000	729,000,000	20,000,000
Eco-Contribution	6,000,000	1,220,000	(4,780,000)
Other Revenue	10,000	10,000	-
Totals	715,010,000¹⁰	730,230,000	15,220,000¹¹

(Source: Financial Estimates 2016, page 187)

Further comparisons were made between the Department's projections and the amounts estimated as per Financial Estimates, where it was noted that MFIN expected an amount of €20 million more than proposed by the VAT Department, up to €729 million. On the other hand, the Eco-Contribution budget

¹⁰ This amount does not reconcile with the corresponding amount in Table 1 since €1,000 in Tender Fees was deemed to be out of scope of this analysis and therefore omitted from Table 9.

¹¹ Vide footnote 4.

was decreased by €4,780,000. This deduction was mainly due to measures announced in the 2016 Budget Speech, which stated that certain products were no longer to be subject to Eco-Contribution and were instead replaced by an excise duty rate. These included alcoholic beverages, chewing gum, plastic bags and bottles/cans of non-alcoholic beverages. Table 17 refers.

3.2. Trend Analysis

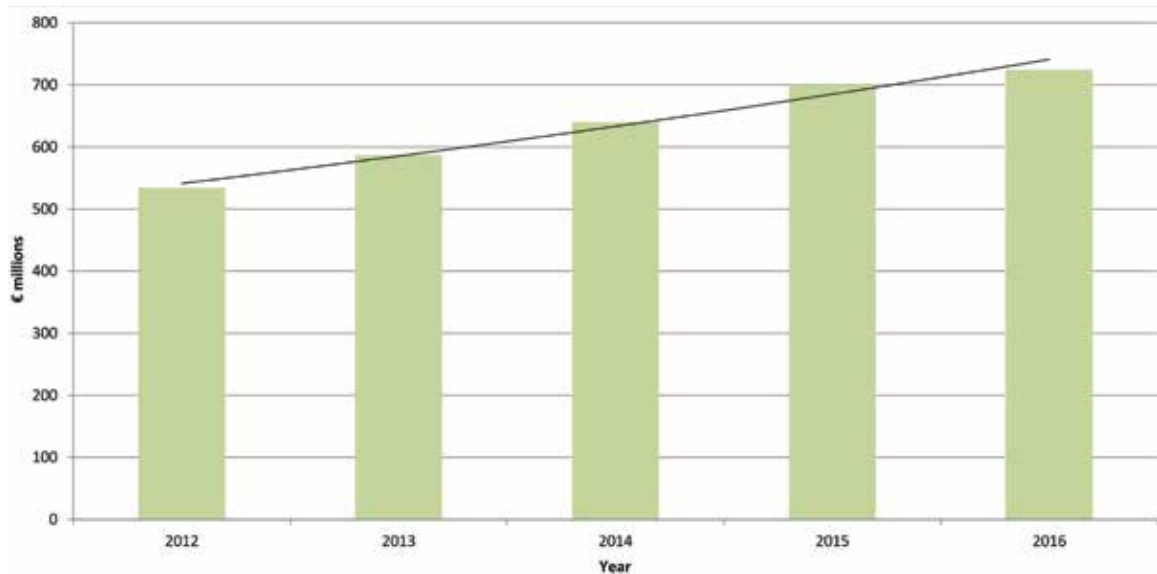
Revenue figures in relation to the VAT Department were analysed against the income generated in the prior four years, as shown in Table 10 and Chart 6.

Table 10: Trend Analysis of VAT Revenue Categories (2012 – 2016)

Revenue Category	2012	2013	2014	2015	2016
	€	€	€	€	€
VAT ¹²	534,196,579	587,170,640	639,675,627	699,998,113	724,798,345
Eco-Contribution	6,908,470	7,966,364	9,293,789	8,116,304	1,461,494
Other Revenue	9,983	2,506	10,647	6,244	20,680
Totals	541,115,032	595,139,510	648,980,063	708,120,661	726,280,519

(Source: MFIN Financial Estimates 2014, page 268; 2015, page 211; 2016, page 187; 2017, page 180)

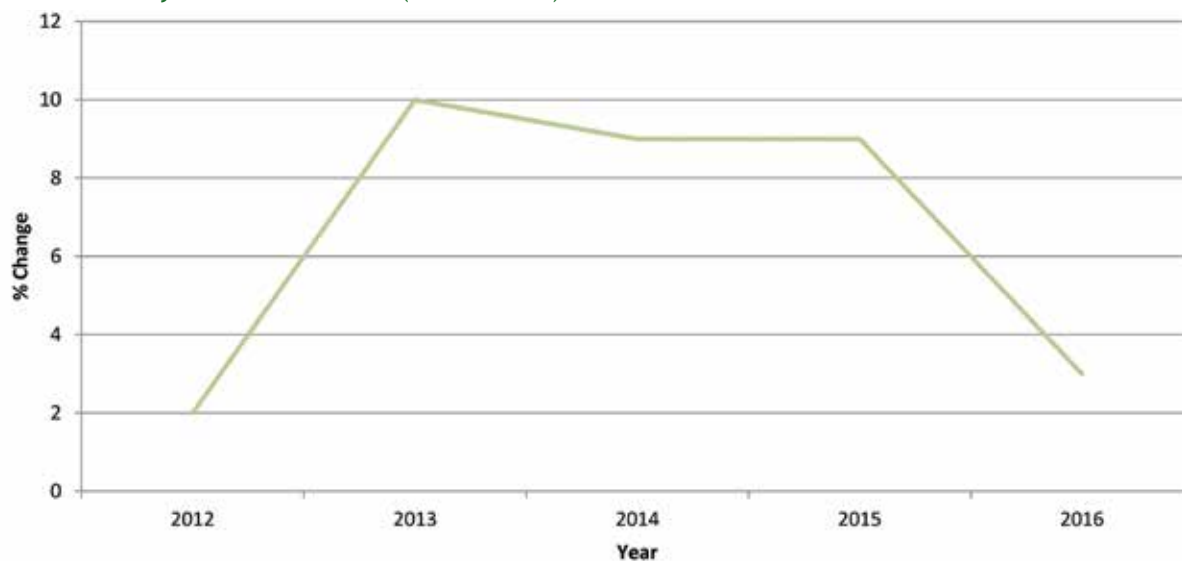
Chart 6: Trend Analysis of VAT Revenue (2012 – 2016)



(Source: MFIN Financial Estimates 2014, page 268; 2015, page 211; 2016, page 187; 2017, page 180)

¹² Total amounts listed include the VAT collected by the DOC on behalf of the VAT Department.

Chart 7: Analysis of VAT Revenue (2012 – 2016)



(Source: MFIN Financial Estimates 2013, page 259; 2014, page 268; 2015, page 211; 2016, page 187; 2017, page 180)

As shown in Chart 7, aggregate net revenue¹³ collected by the VAT Department rose at a steady rate between 2012 and 2015, i.e. at a rate between 9% and 10%. On the other hand, during 2016, total net revenue, experienced a slower rate of increase of 3% over the previous year.

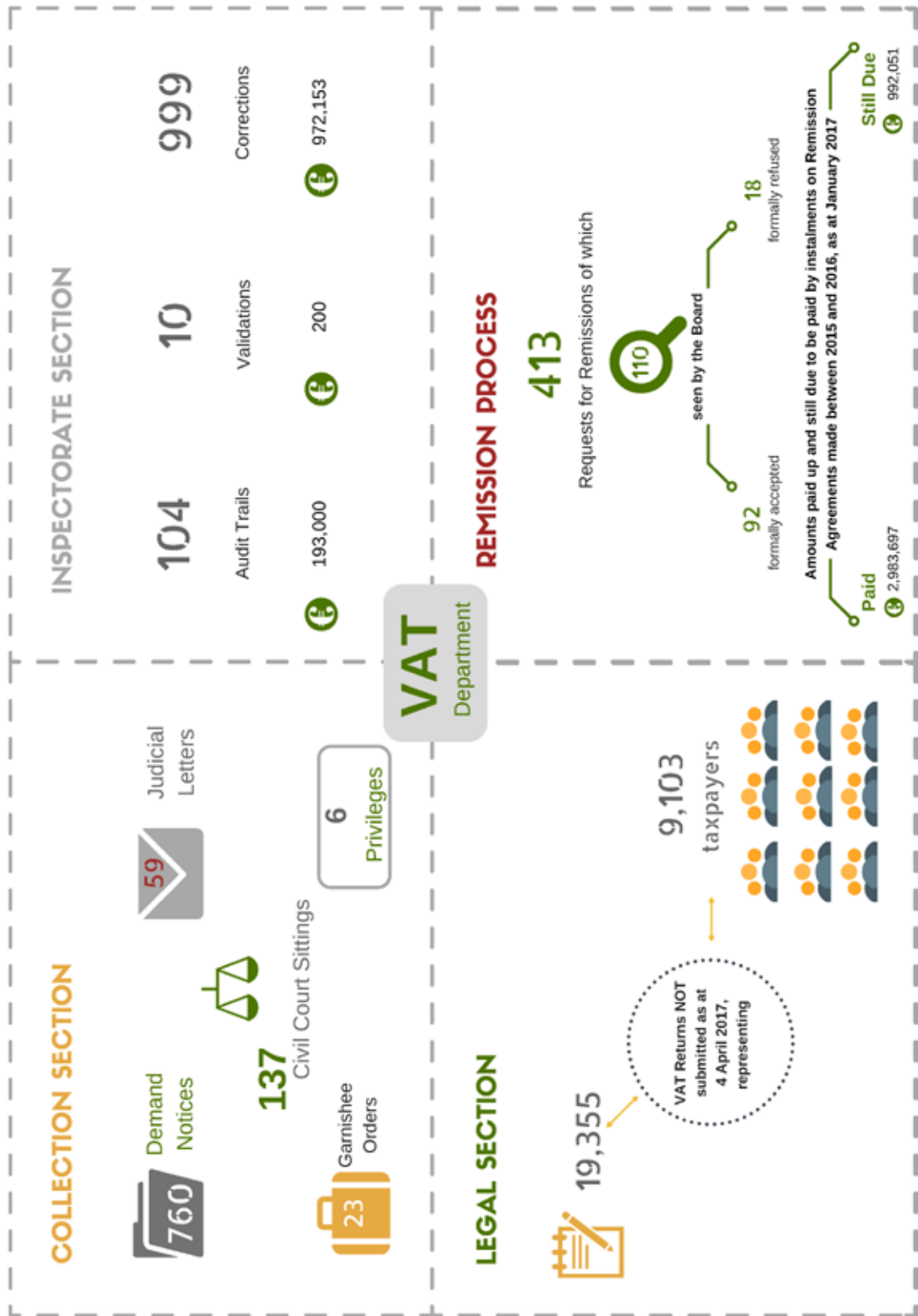
Upon enquiry as to the reasons behind the smaller increase in revenue during 2016, this Office was informed that the Department does not have the means and resources to make such a detailed analysis. Nevertheless, the Department highlighted the fact that the economic growth in 2015 increased at a higher rate than in 2016 and this was reflected in the actual figures of the VAT collected. Moreover, refunds are increasing annually at a higher rate than revenue (which can be due to various factors), thus absorbing a substantial amount of the increase in gross revenue. Table 11 refers.

Table 11: Refunds issued during 2014 – 2016 by the VAT Department

Year	Refunds €	Increase over previous year %
2016	172,278,134	22
2015	140,704,901	21
2014	116,374,668	No information provided

¹³ This figure is net of refunds.

3.3. Enforcement during 2016 at a glance



Court Sittings

- There were 157 Civil Court sittings during 2016. Taxpayers file these cases after the Department initiates enforcement action. Such Court cases require a substantial number of hours of discussion with the Department's lawyers, including the filing of respective replies and submissions.
- The Collections team meets taxpayers to discuss repayment programmes and remission requests.
- The team also processes compliance certificates that are required by the Department of Contracts when a tender is awarded. The Department pointed out that such requests are increasing drastically. In fact, during 2016, it was confirmed that a total of 470 certificates were issued.
- The Legal Section sends 200 requests per week to Police to charge respective taxpayers for non-submission of Returns. By April 2017, action was being taken on non-submitted Returns relating to June 2015 reporting period.



Enforcement Action

- One Assistant Director, one Revenue Manager and three part-time Inspectors, handled all enforcement duties during 2016.
- All efforts of enforcement are mainly focused on the VAT collection.
- Importance is given to short-term arrears, i.e. arrears of the same year. Such arrears are given the utmost importance, as the longer a debt is due, the more difficult it is to collect. Since most VAT returns are due every quarter, most VAT registered persons must submit four returns in a year. Thus, for example, a return which was due in February 2016 was considered as arrears if it was paid up in August of the same year, since it was already overdue and in fact incurred interest.



Results obtained from Enforcement Action made during 2016



- It was pointed out that it is not possible to show the results obtained directly from the enforcement action taken, as such work could take years to yield the actual results, since there is no direct correlation.
- When a taxpayer is addressed, all dues up to that date are discussed and repayment agreements are drawn up accordingly.
- Moreover, it is often the case that the demand notices include estimated tax, which in most instances is diminished drastically once the actual returns are submitted.

Outcome derived from Remissions



- Following queries by the NAO on whether the Department conducted any examination of the actual effects on revenue resulting from the remissions of additional tax, interest and/or penalties given to defaulters during 2016, VAT officials confirmed that no analysis has been made due to various factors, the primary one being the lack of human resources.
- The remission process requires detailed preparatory work that is done by the Collection team. This includes keeping the database updated with new applications, checking that they are filled in correctly, contacting the taxpayer and discussing the options of repayment, as well as obtaining the first payment. Moreover, some cases are not finalised since the taxpayer does not reply with his decision on what option to take up. No deadline is established for submission of reply.
- Moreover, software to calculate the remission options for certain cases is not yet finalised by the Malta Information Technology Agency (MITA). As a result, such cases could not be given the options of payment, as well as other application forms had missing data and the taxpayers had not provided feedback.

Chapter 4

Department of Customs

4.1. Variance Analysis

As explained earlier in 'Methodology', the Department submitted the estimates for the forecast year in the first quarter of the basis year, i.e. March 2015 for financial year ending December 2016. Thus, the projections were submitted well in advance, without knowledge of any new budgetary measures, historic trend results of the basis year and the elasticity effect on consumption. In the case of the DOC, such a scenario led to an aggregate variation of €26,120,000 (10%) between the Departmental projections and those published in the Financial Estimates for 2016, with the most material difference registered in Import and Excise Duties, as shown in Table 12.

Table 12: Variance Analysis of Projections against Financial Estimates 2016 – DOC

Revenue Category	Projected by Department €	As per Financial Estimates €	Variance	
			€	%
Import and Excise Duties	258,950,000	283,980,000	25,030,000	10
Licences, Taxes and Fines	1,649,000	1,950,000	301,000	18
Fees of Office	1,642,000	2,237,000	595,000	36
Reimbursements	114,000	173,000	59,000	52
Other Revenue	400,000	535,000	135,000	34
Totals¹⁴	262,755,000	288,875,000	26,120,000	10

(Source: Financial Estimates 2016, page 188)

When considering the Budget measures introduced in 2016, the DOC stated that together with the normal tax rate increase on harmonised goods, an excise duty on certain other goods replaced the previous Eco-Contribution charges. As a result, the new taxation regime was not reflected in the initial Departmental projections. In addition, one has to take into consideration the fact that the performance of certain revenue items is dependent on other categories. For instance, the sale of banderoles is influenced by the trend of receipts under excise duty for seals or bands, which are tagged to harmonised goods.

¹⁴ Tax collected on behalf of the VAT Department is not included under the DOC, but reported under the VAT Vote. These figures are net of refunds.

Table 13: Variance Analysis of Estimated against Actual Revenue 2016 – DOC

Revenue Category	Estimated Revenue 2016 €	Actual Revenue			Variance	
		Arrears of Revenue €	Arising from 2016 €	Total €	€	%
Import and Excise Duties	283,980,000	2,953,794	274,552,614	277,506,408	(6,473,592)	(2)
Licences, Taxes and Fines	1,950,000	6,155	1,885,116	1,891,271	(58,729)	(3)
Fees of Office	2,237,000	-	1,427,620	1,427,620	(809,380)	(36)
Reimbursements	173,000	-	131,206	131,206	(41,794)	(24)
Other Revenue	535,000	-	124,454	124,454	(410,546)	(77)
Totals	288,875,000	2,959,949	278,121,010	281,080,959	(7,794,041)	(3)

(Source: Financial Estimates 2016, page 188)

Further analysis was conducted by this Office to assess the variances arising when comparing the actual and budgeted figures with respect to 2016, as shown in Table 13. Negative variations resulted in all revenue items, which led to an overall shortfall of 3% from that originally targeted. Import and Excise duties experienced the most material variation of almost €6.5 million. In particular, excise duties on five different items were the main contributors leading to this variation. This negative trend in the categories of excise duties influenced the fall of 36% between what was intended to be generated from the sale of banderoles and the actual figure. Table 14 further refers.

During 2016, the DOC had two forms of Other Revenue, being income from the European Union (EU) Customs Programme and other miscellaneous receipts. As the Department explained, miscellaneous receipts are one-off sources of revenue. The 77% decrease in this form of income mainly arose from such receipts. The negative variation of 99% between the budgeted and actual revenue figure of miscellaneous receipts for 2016, reported in Table 14, is due to the fact that forecasts were based on the 2014 end-of-year results.

Table 14: Main Contributors to the Variances between Estimated and Actual Revenue 2016 – DOC

Revenue Category	Estimated Revenue	Actual Revenue ¹⁵	Variance	
	€	€	€	%
Excise Duties				
Ammunition Cartridges	150,000	19,000	(131,000)	(87)
Tobacco	9,930,000	3,552,000	(6,378,000)	(64)
Chewing Gum	750,000	497,000	(253,000)	(34)
Non-alcoholic beverages	1,200,000	844,000	(356,000)	(30)
Spirits	15,570,000	12,195,000	(3,375,000)	(22)
Fees of Office				
Sale of Banderoles	2,200,000	1,414,000	(786,000)	(36)
Other Revenue				
Miscellaneous Receipts	400,000	6,000	(394,000)	(99)

(Source: MFIN Financial Estimates 2016 page 188)

¹⁵ Figures are rounded to the nearest thousand.

4.2. Trend Analysis

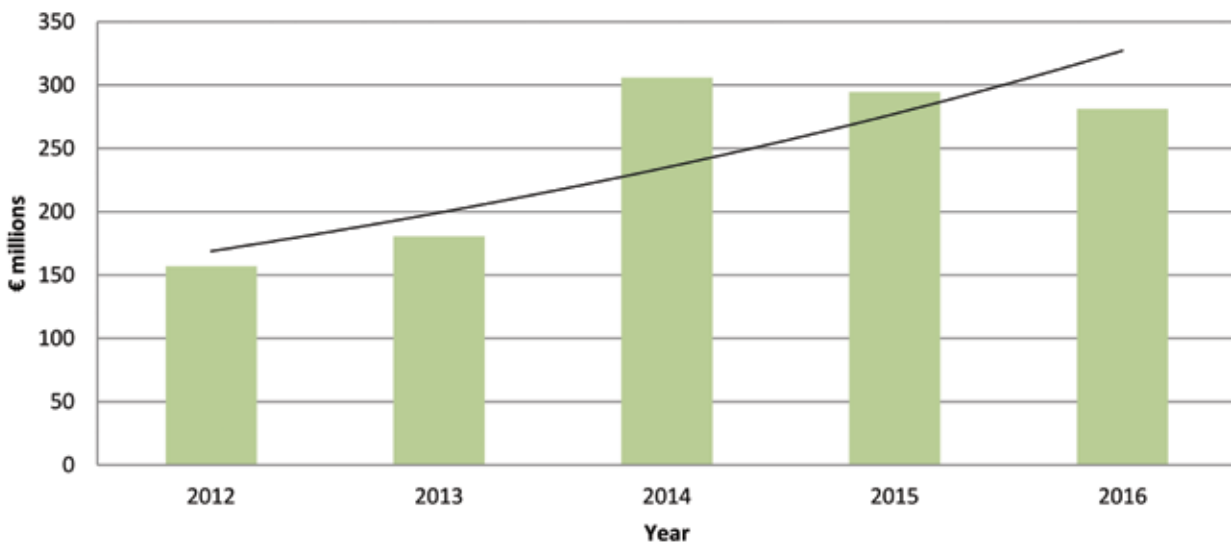
The total revenue collected by the DOC during financial year 2016 amounted to €399,907,040. However, if the aggregate of tax collected on behalf of the VAT Department amounting to €118,826,081 is excluded, the actual revenue goes down to €281,080,959 (Table 13). This figure could be analysed further against the income generated in the prior four years, as shown in Table 15 and Chart 8.

Table 15: Trend Analysis of the DOC Revenue (2012 – 2016)

Revenue Category	2012	2013	2014	2015	2016
	€	€	€	€	€
Import and Excise Duties	155,790,297	178,400,995	302,607,413	290,404,790	277,506,408
Licences, Taxes and Fines	993,016	1,391,302	1,685,006	2,270,333	1,891,271
Fees of Office	48,288	232,499	941,222	1,548,675	1,427,620
Reimbursements	110,798	99,883	318,029	89,529	131,206
Other Revenue	41,438	509,978	358,701	96,247	124,454
Totals	156,983,837	180,634,657	305,910,371	294,409,574	281,080,959

(Source: MFIN Financial Estimates 2014 pages 268-269, 2015 page 212, 2016 page 188, 2017 page 181)

Chart 8: Trend Analysis of the DOC Revenue (2012 – 2016)



(Source: MFIN Financial Estimates 2014 pages 268-269, 2015 page 212, 2016 page 188, 2017 page 181)

The growth registered in 2014 over the prior year, depicted in Chart 8, mainly resulted from the fact that in 2014, Enemalta p.l.c. settled past arrears of excise duties on petroleum products owed to the DOC. Nevertheless, if petroleum is excluded from this analysis, the total amount of excise duties generated from other excise goods still recorded an increase of €21,199,068 over 2013.

4.3. Effects of Budget Measures on Revenue

Increase in Excise Duty Rates

The increase in various excise duty rates announced in the Budget Speech for financial year 2016, led to higher revenue generated in a number of income categories. As portrayed in Table 16, the increase in excise duty of €5 per 1,000 kilograms of cement, resulted in a 10% increase in revenue. Meanwhile, the rise in excise duty for machine-made cigarettes led to a 4% growth in revenue under this category. Both increases were introduced in view of health and environmental protection considerations.

However, as previously explained under 'Trend Analysis', despite the various increases in excise duty rates for petroleum products listed in Table 16, the income arising from this category declined by 14% during 2016. This was mainly due to the settlement of one-off arrears in November 2015, which inflated the 2015 revenue by €30 million. Similarly, in spite of the increase in the rates of tobacco shown in the same table, an overall decrease of 4% in this form of revenue was registered.

Table 16: Budget 2016 Measures – Increases in Excise Duty Rates

Category	Product	2015 Rate	2016 Rate	Change in Rate	Change in Revenue following Implementation of Measure	
					€	%
Machine-Made Cigarettes	Cigarettes	25% of retail price plus €92.5 per 1000 cigarettes but not less than €150 per 1000 cigarettes	25% of retail price plus €100 per 1000 cigarettes but not less than €160 per 1000 cigarettes	Increase in lower and upper thresholds of €7.5 and €10 per 1000 cigarettes, respectively	2,861,000	4
	Cigars and Cigarillos	€22.95 per 1000 units	€24.33 per 1000 units	+€1.38 per 1000 units		
Tobacco	Hand-rolling and other smoking Tobacco	€108.07 per kg	€115.64 per kg	+€7.57 per kg	(161,000)	(4)
	Pipe Tobacco	€32.54 per kg	€34.49 per kg	+€1.95 per kg		
	Chewing Tobacco and Snuff	€32.82 per kg	€35.20 per kg	+€2.38 per kg		
Petroleum	Leaded and Unleaded Petrol, Gas Oil, Biodiesel	Various rates	Various rates	+€30 per 1000 litres in all categories	(21,046,000)	(14)
	Heavy Fuel Oil	€36 per 1000 kgs	€39 per 1000 kgs	+€3 per 1000 kgs		
	Kerosene	€442.4 per 1000 litres	€472.4 per 1000 litres	+€30 per 1000 litres		
	Petroleum Oils	€0.23 per litre	€0.25 per litre	+€0.02 per litre		
Cement	Cement	€35 per 1000 kg	€40 per 1000 kg	+€5 per 1000 kgs	1,096,000	10
Total					(17,250,000)	

(Source: Budget Speech 2016 pages 88-95)

Change in Excise Duty Rates following the removal of Eco-Contribution Charges

Additionally, the 2016 Budget Speech announced that the Eco-Contribution rate for certain products was to be replaced with an excise duty rate. The implemented changes in the tax regime are summarised in Table 17. Hence, the revenue that was previously collected by the VAT Department up till 2015, was reclassified under the excise duty revenue collected by the DOC in 2016. This led to significant increases in all categories of excise duties affected by this changeover, being beer, wines, chewing gum, water and non-alcoholic beverages as well as plastic bags. Hence, it is pertinent to note that part of the increase over the previous year was partially influenced by this reclassification, as well as by the fact that this budget measure was not yet known in 2015. Further details are discussed in 'Section C' under the sub-heading 'Variance Analysis'.

As shown in Table 17, an upsurge in revenue was noted in the non-alcoholic beverages and plastic bags categories. Other material revenue growth was registered in excise duty collected in respect of chewing gum, beer and wines, as further explained in the same Table.

Table 17: Excise Duty Rates following the removal of Eco-Contribution in Budget 2016

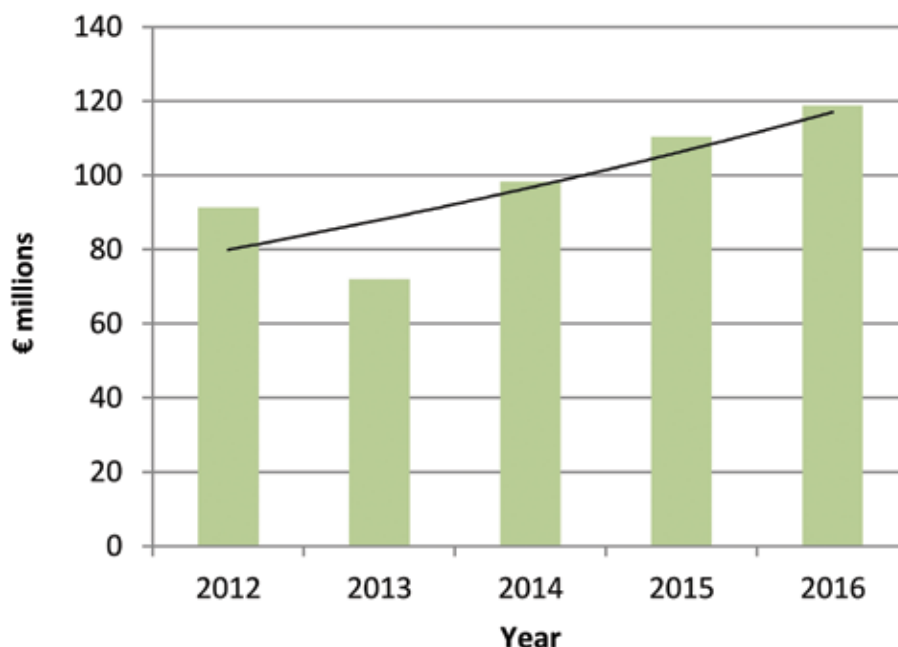
Category	Product	Previous Eco-Contribution Rate	Change in Excise Duty Rate in Budget 2016	Increases in Revenue following Implementation of Budget Measure	
				€	%
Beer	Beer	€0.02 per bottle or can	+€0.20 per hectolitre per degree Plato	497,000	18
Wines, Intermediate Products and Spirit Flavoured Beverages	Wine of fresh grapes	€0.12 per bottle or container	+€5 per 1000 litres	965,000	67
	Fermented beverages	€0.02 per bottle or container	+€20 per 1000 litres		
	Intermediate products	€0.12 per bottle	+€2 per hectolitre		
	Spirit flavoured beverages	€0.12 per bottle	+€0.01 per % volume per litre		
Chewing Gum	Chewing gum	€0.01 per 2g net	+€9 per kg	392,000	373
Waters and Non-Alcoholic Beverages	Waters and non-alcoholic beverages	€0.02 per bottle/container	+€5 per 1000 litres of beverages within CN Heading 2201 +€20 per 1000 litres of beverages within CN Heading 2202	1,480,000	955
Plastic Bags	Plastic bags	€0.14 per piece	+€140 per 1000 pieces		
	Degradable plastic bags	€0.02 per piece	+€20 per 1000 pieces		
	Bags without any handles, loops or slots	€0 per piece	+€1 per 1000 pieces	459,000	254
	Bags of HS Codes 3923 21 and 3923 29	€0.15 per bag	+€150 per 1000 bags		
Total				3,793,000	

(Source: Budget Speech 2016 pages 88-89, 93-95)

4.4. VAT collected by Department of Customs on behalf of the VAT Department

During 2016, the Department collected an aggregate of €118,826,081 in tax on behalf of the VAT Department. A trend analysis of the VAT collected between 2012 and 2016 is portrayed in Chart 9.

Chart 9: VAT collected by the DOC (2012 – 2016)



Goods imported locally from outside the EU and excise goods received from the EU, are to be declared by the trader or agent for clearance by the DOC. The majority of the declarations are made by means of the Direct Trader Input system. This entails the submission of an electronic Single Administrative Document through an Import System. The information entered on this document, for instance the commodity code of the product, the origin code and Customs value, allow the Import system, in conjunction with the Tariff Module¹⁶ and Taric Module¹⁷, to identify all taxes payable. All commodity codes have the respective VAT rate correlated with them in the Tariff Module. Thus, the Import System automatically calculates the amount of Import VAT payable to the DOC.

Upon enquiry, the DOC stated that several declarations relating to the financial year 2016 were selected for control purposes, whilst a number from the remaining declarations were randomly scrutinised by the Verifications and Audit Section within the Enforcement Directorate. From an aggregate of 101,945 declarations registered during 2016, circa 20% (20,230 declarations) were selected for control purposes whilst another 11,652 declarations (circa 11%) were scrutinised by the above-mentioned Section.

4.5. Traditional Own Resources

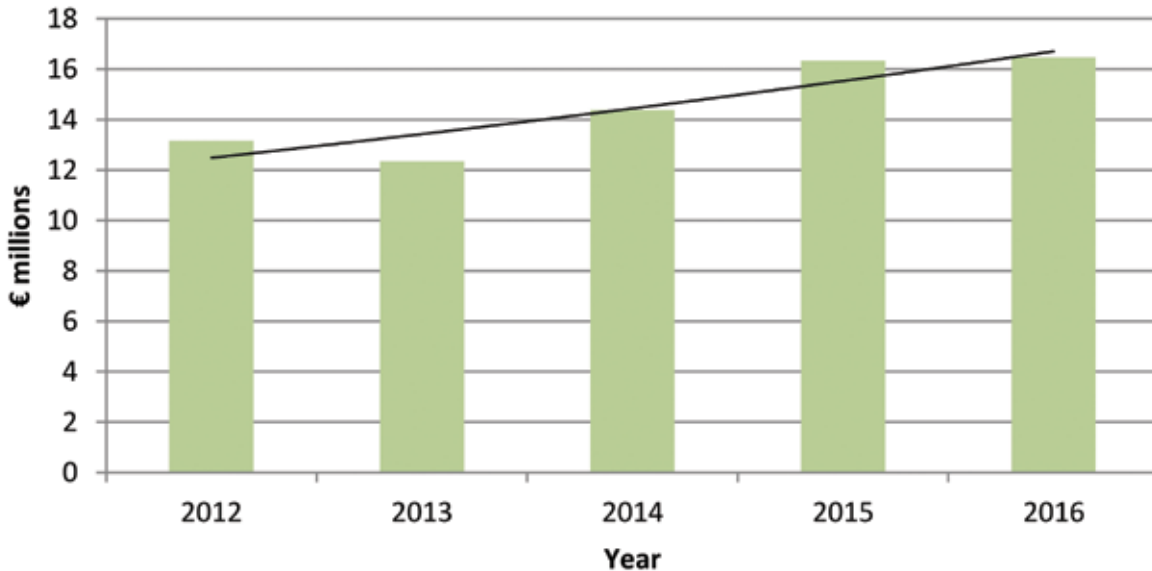
As part of Malta’s obligations as a European Union Member State, revenue collected in the form of customs duties is to be paid on non-EU importations, and levies are to be paid on agricultural products

¹⁶ The Tariff Module, based on the World Custom Organisation’s (WCO) harmonised commodity and coding system, provides the necessary tariff information.

¹⁷ The Taric Module is an information database developed by the EU, providing integrated information on the latest tariffs applicable on a product-by-product basis, according to country of origin.

that enter Malta from outside the Union. This revenue is referred to as Traditional Own Resources (TOR). Chart 10 shows the TOR collected since 2012, reaching €16,467,538 during 2016.

Chart 10: Traditional Own Resources collected (2012 – 2016)



In principle, all customs duties on non-EU imports must be paid to the Union. However, each member country is entitled to retain a portion of the money by way of a collection fee for administrative work involved in collecting these duties. To this effect, the European Council altered the legislative framework in relation to the EU's own resources system for the period between 2014 and 2020. Through the implementation of Council Decision No. 2014/335, the percentage of customs duties of non-EU imports to be retained by each member state was decreased from 25% to 20%. The new own resources rules became applicable following the entry into force of this decision on 1 October 2016, retroactively as of 1 January 2014. As a result, as confirmed by the DOC, Malta is reimbursing the EU the difference in the change of rate pertaining to years 2014 (€719,105), 2015 (€816,881) and part of 2016 (€420,005). The EU duly forwarded an information note to each Member State regarding how retroactive amounts are to be treated. The DOC informed the NAO that no penalties or interests were applicable with respect to these re-imbursements due to the new regulations.

In line with Article 2 of the EU Council Regulation No. 608/2014, the TOR generated by member states shall be inspected in adherence with same Regulation. Nevertheless, as confirmed by the DOC, no verification was done by the European Commission on the TOR collected during 2016.

4.6. Controls on Collection of Revenue

(Source: Standard Operating Procedures at Customs Debt Unit – Customs Department, MFIN)

The DOC established a set of Standard Operating Procedures, to ensure the accuracy and completeness of revenue as well as a uniform adoption of the EU and national legislation by the Department's Units. In addition, these procedures provide the Department's officers with the information required to perform their duties properly in a consistent manner and ascertain continuity in case of staff changes.

The Customs Debt Unit (CDU) pursues outstanding amounts due to the Department and effects refunds due to traders. Besides other tasks, it monitors the deferred payment facilities granted to certain importing companies and manages bank guarantees.

The measures adopted by the CDU include the following:

- a. Monitoring settled and unsettled balances in the Customs Electronic System.
- b. Liaising with Cashiers and Heads of Sections on any queries arising in the Customs Electronic System.
- c. Suspense Account Monitoring.
- d. Monthly Reconciliation and Account Analysis of different duties used during the month.
- e. Compiling the B Account which includes customs debt incurred that is not guaranteed.
- f. Issuing Refunds following proper Authorisation.
- g. Managing the Deferred Payment Facility.
- h. Submission of Own Resources reports to the Commission with a description of the cases of fraud and irregularities in customs duties exceeding €10,000.
- i. Maintaining a register of original guarantees received by the different DOC's sections.

4.7. Debt Collection Agreements

As part of the Department's efforts to recoup outstanding amounts, during the year under review the Tobacco Product Unit and the Alcohol Product Unit within the DOC drew up debt collection agreements with four importers to eventually collect an aggregate of €8,808,384. The debtors in relation to two of these agreements settled their debts in full, while the other two partly settled the amounts due during 2016, being 70% and 46% of the totals, with the balance of €1,053,542 remaining as arrears as at year-end.

In case of importations of energy products, manufactured tobacco and alcoholic beverages, the excise duties have to be paid as laid down in Article 10 of the Sixth Schedule within the Excise Duties Act (Cap. 382). This Article specifies that excise duty on goods taken out stations or bonded warehouses shall be paid before such goods are released. Otherwise, for goods withheld, excise duty shall be paid before such goods are released or else periodically, as may be allowed by the DOC.

On the other hand, on other commodities classified as non-harmonised goods¹⁸ the Department adopts a 90-day credit period from the time when the goods are released for consumption. As per aforementioned Article in the Excise Duties Act, the period allowed for debt settlement is at the discretion of the Commissioner.

¹⁸ Non-harmonised sectors are not subject to common EU rules and may come regulated under the national rules.

4.8. Enforcement Measures

Inspections in joint effort with the VAT Department

- Acquisitions from Member States are inspected through a risk analysis of gathered information.
- Goods are checked both with respect to Customs requirements and also from a fiscal perspective in line with the VAT legislation.
- Periodical meetings are held between the two departments to discuss new emerging trends.



Inspections on Intellectual Property Rights

- Risk analysis of different risk criteria on the Bills of Lading, airway bills, postal and couriers declarations.
- Scanning of goods.
- Inspections are subsequently performed.



Customs Operations organised by the European Council and the World Customs Organisation

- Customs operations are performed, following a threat assessment both by the Council and the WCO.
- A business case is then formulated and presented to the Customs Cooperation Working Party for adoption.
- An operational plan is designed considering any possible threats, scope, strategic and tactical objectives, timeline, risk indicators, participating countries, implementation, organisation, communication and evaluation.
- The operational plan is presented to the participating member state for discussion in a brief meeting.



Enforcement Measures during 2016

Type of Measure	Cases identified during 2016	Amount due to Department of Customs	Amount collected relating to 2016 €
Inspections performed in joint effort with the VAT Department	29	No amount receivable in relation to this measure.	Not Applicable
Inspections on Intellectual Property Rights	103	Customs store rents are calculated once goods are destroyed, in view of the respective Civil Court Judgement.	32,467 ¹⁹
Customs operations organised by the European Council and the WCO	European Council – 3 WCO – 4 EU Agency for Law Enforcement Cooperation (Europol) – 2 Maritime Information (Marinfo) – 1	No amount receivable in relation to this measure.	Not Applicable

X-Ray Scanning performed by the Container Monitoring Unit

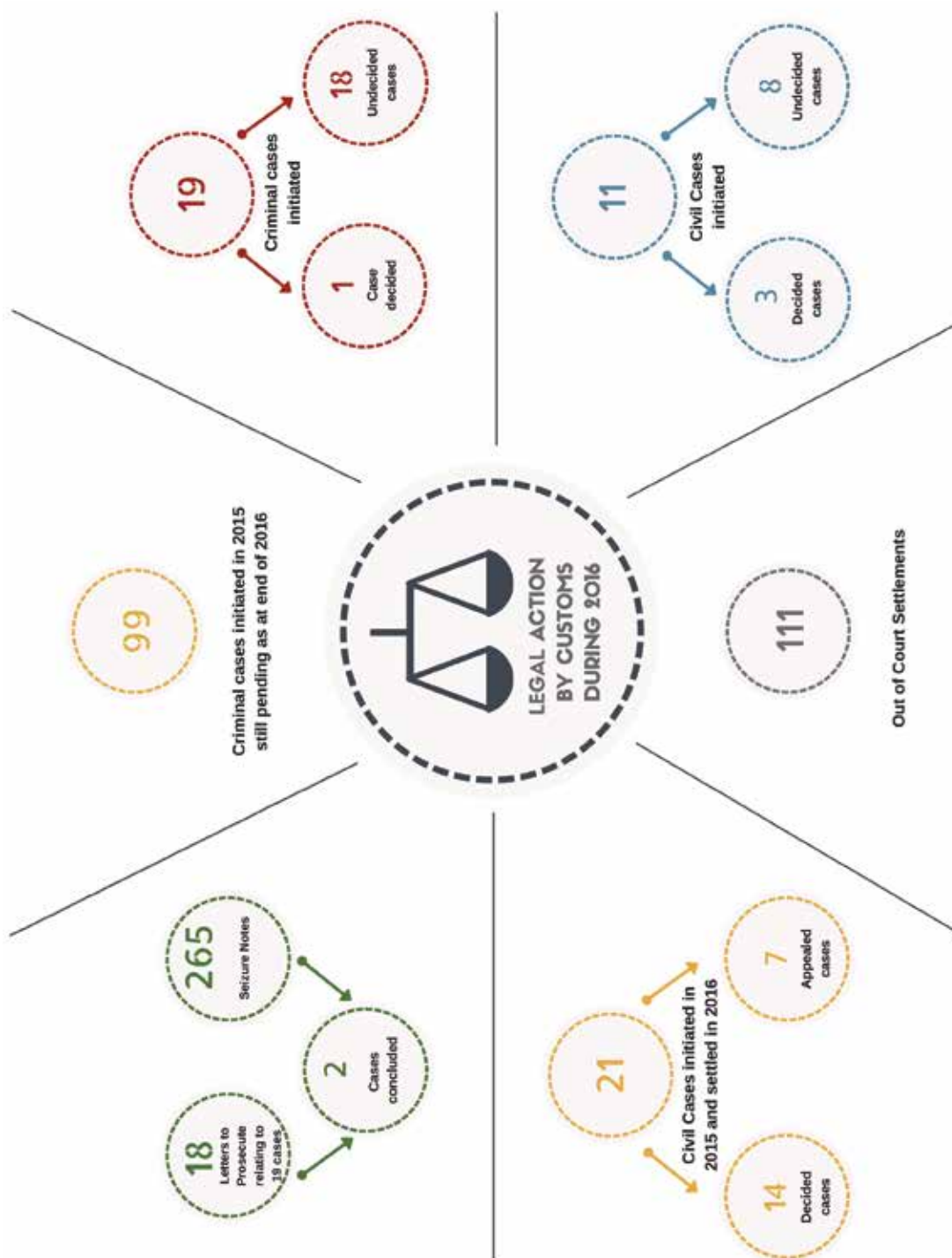
Around 12 to 48 hours prior to a vessel's docking at the Malta Freeport, the cargo manifest and a discharge list related to all transshipment cargo are received from the carrier or its local representative, as well as from the Freeport's Container Control Section. Following a comparison of these documents, the actual risk analysis is performed by scrutinising the manifest details against several risk criteria.

According to the size of the manifest, the targeting officer performs several phases of short listing, until the final list of containers selected for scanning is compiled. Under normal circumstances, the selected sample sums up to around 1.8% of units listed to be discharged. The list is subsequently forwarded to the Freeport authorities prior to the actual berthing of the vessel. Hence, the port planners can separate the selected units on discharge, avoiding double handling and re-stows. The units are conveyed for scanning when it best fits the operational schedule of the Freeport. Once selected, every container is not transhipped, until released by the DOC.

During 2016, the DOC made use of the VACIS and NUCTECH X-ray systems in order to scan the containers, with the latter being stopped in May 2016. Moreover, in the same year, the Department acquired new scanning equipment. Although this scanner, which is incorporated in a van, is intended to be used at the Freeport, the van can also be used in different locations. In addition, after the DOC concluded the procurement procedures for a new container X-ray scanner in February 2017, the NAO is informed that the Department is expected to have this equipment by the end of 2017.

¹⁹ The total amount receivable with respect to this measure was actually collected.

Legal Action during 2016



Chapter 5

Staff Complement

The NAO feels it is pertinent to reproduce a number of comments which were forwarded in relation to the Departments' respective staffing requirements.

5.1. Inland Revenue Department

The Department mentioned that it has a lack of analysts, statisticians and economists within its staff complement. However, despite this notable shortcoming, and the fact that it does not have a financial controller to take care of its financial reporting, the Department is still striving to make its own forecasts and projections for the line items under its remit.

Furthermore, when commenting about the Maternity Benefit Fund, the IRD stated that even though the amount may be insignificant when compared to the tax revenue and the SSC, the processes involved in its collection require a significant amount of human resources. Nevertheless, *"... no new influx of resources was provided to cater for the additional input required, with the consequence of further stretching the existing resources of the Department."*

When further queried by the NAO in relation to this shortfall in staff, the Department stated that since action to collect the amounts due is an ongoing process, should its human resources increase, this would have a positive impact on planning and execution of the work plan²⁰.

At this stage, reference is made to a Report commissioned by the Treasury and compiled by the Chartered Institute of Public Finance and Accountancy entitled 'Assistance in the Implementation of Accrual Accounting (Accounting for Taxation)'. This Report, dated March 2016 highlighted the fact that, amongst others, the IRD needs to employ statisticians/data analysts in order to be able to determine how reliable the provisional tax and social security contribution amounts are in terms of properly due amounts.

The IRD also pointed out that debt collection will still be a problem until its IT support, as well as that provided by MITA increase. The Department gave an indication of the staff complement it currently requires as outlined in Table 18.

²⁰ The International Monetary Fund Report of 2015 indicated that 15% – 20% of the revenue administration's resources are typically devoted to tax debt enforcement. As stated by the IRD, one of the IMF's reports' statement is to urgently increase the number of staff in tax collection.

Table 18: IRD Staff Complement

Section	Staff Complement during 2016	Required Staff Complement (Full-time equivalent)
Collection	<ul style="list-style-type: none"> • 1 Assistant Director • 1 Manager • 3 Principals • 1 Assistant Principal • 3 Senior Clerks • 3 Clerks (on contract working a 20-hour week) 	<ul style="list-style-type: none"> • 1 Director – To plan, monitor and control • 1 Assistant Director – To assist the Director and collaborate with the VAT Department in the merger process • 1 Revenue Manager – To manage Court cases and enforcement action • 2 Senior Principals – To present the Court cases in Court and deal with all issues that relate to them • 5 Assistant Principals – To discuss remission options with taxpayers • 10 Senior Clerks – 2 clerks to assist with Court cases paperwork and vetting of remission applications and 8 clerks to issue demand notices • 1 IT official – Full-time with the Collection team • 1 officer from the MITA team – Full-time with the Collection team

5.2. VAT Department

The VAT Department monitors closely the incoming revenue and the refunds being issued to ensure that all possible efforts are made to reach the set targets. However, the VAT Department’s officials explained that there is a serious lack of human resources in the Collection Section, which must be urgently addressed to ensure that enforcement action is taken in a timely manner.

In fact, following a query by this Office on the number of staff required by the VAT Department to effectively and efficiently conduct the necessary enforcement action, the Department’s officials indicated that it needs the following personnel complement:

Table 19: VAT Staff Complement

Section	Staff Complement during 2016	Required Staff Complement
Collection (including Remissions)	<ul style="list-style-type: none"> • 1 Assistant Director • 1 Revenue Manager • 3 Part-time Inspectors 	<ul style="list-style-type: none"> • 1 Director – To plan, monitor and control • 1 Assistant Director – To assist the Director and collaborate with the IRD in the merger process • 1 Revenue Manager – To manage Court cases and enforcement action • 3 Assistant Principals – To assist the Manager on Court cases and to discuss remission options with taxpayers • 5 Clerks – 1 to assist with Court cases paperwork and vetting of remission applications, and 4 others to issue demand notices • 1 IT official – Full-time with Collection team • 1 officer from MITA team – Full-time with Collection team
Inspectorate	<ul style="list-style-type: none"> • 1 VAT Inspector (retired during the year) • 1 VAT Inspector on reduced hours (30 hours per week), partly performed through telework²¹ 	<ul style="list-style-type: none"> • 2 Full-time officers until electronic processing is made possible
Legal	<ul style="list-style-type: none"> • 1 Principal • 1 Assistant Principal • 2 Full-time Clerks • 1 Part-time Clerk 	<ul style="list-style-type: none"> • 1 Prosecution Manager • 1 Junior Legal Officer • 5 clerical grades

Only the substantive grades were included in the list of staff complement required by the Collection Section, given that although a position for debt collectors was created, the result of the selection process was contested and the case is still pending in Court. The total number of Debt Collectors, approved by MFIN, for the VAT Department was four.

²¹ Duties during telework not related to corrections.

Similar to the situation of the IRD, the VAT Department insisted on adequate IT support to calculate the remission options as earlier explained in Section C of this analysis, as well as “... to finalise the work back enhancements and to set up a structured system of issuance of demand notices”.

5.3. Department of Customs

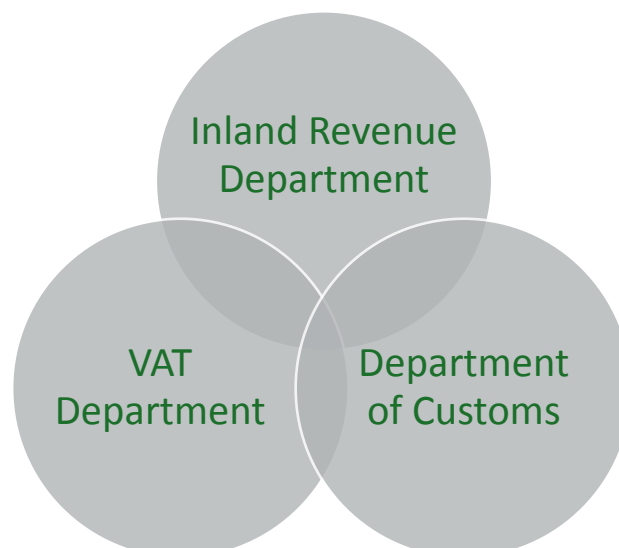
As highlighted in the ‘Malta Customs Business Strategy 2017-2019’, the Department is facing a challenge in its human resources allocation. Whilst experiencing a limited and ageing workforce, the DOC has an imbalanced organisational structure. Thus, the situation is leading to an inefficient use of resources. An aggregate of 30 officers are responsible for the enforcement of revenue collection.

Hence, the DOC is planning to reform its organisational structure by recruiting new officers in line with the Department’s capacity-building plan for the period between 2017 and 2019. Moreover, as part of the restructuring process, certain functions shall be allocated to other units according to the organisational plan and exigencies of the Department. Succession planning is also to be introduced to ensure the business continuity according to the mission statement.

Given the above statements, the NAO feels that such requests should be given urgent consideration in view of the implications involved in so far as revenue collection is involved.

Chapter 6

Integration of Revenue-Generating Departments



6.1. Background

(Source: MFIN Inter-Departmental Working Group for the Integration of Revenue Earning Departments – Strategic Appraisal and Recommendations – January 2007; Merger of the Revenue Departments into One Entity – The Accountant – Winter 2014 Edition)

An Inter-Departmental Working Group was set up in mid-2006 with the primary objectives to examine the three main revenue-generating Departments and recommend the best framework of establishing a closer working relationship, as well as creating increasing synergies between these Departments. In January 2007, the Working Group presented a Report on its work entitled 'Strategic Appraisal and Recommendations', to the then Hon. Minister of Finance.

The options for change have been assessed against six objectives, which were consistent with the approach taken by academics, the Organisation for Economic Co-operation and Development, the International Monetary Fund, as well as the World Bank.

The objectives were the following:

- a. Fairness to promote social justice.
- b. Customer service improvements.
- c. Significant compliance costs which fall disproportionately on small businesses, many of which are customers of all the Departments and which have most to gain from a more coherent approach.
- d. Effectiveness, involving maximising the collection of taxes required by law.
- e. Efficiency and further economies of scale.
- f. Confidentiality for taxpayers and other customers, which is central to maintaining confidence in the system.

6.2. Benefits of Integration

The operational benefits envisaged from the study included:

- a. more efficient application of resources by eliminating duplication of functions and additional specialisation;
- b. information sharing leading to more effective risk analysis by reducing data fragmentation;
- c. reduction of opportunities for tax evasion;
- d. more focus on a taxpayer-centred approach, resulting in the improvement of quality standards to provide equal treatment of taxpayers, concentrating further on service principles;
- e. common and better functionality for administration of all taxes;
- f. improved cash control management;
- g. centralisation of routine processes, which can be more easily automated;
- h. improving compliance activities;
- i. increase in co-operation of staff and better career opportunities for employees;
- j. uniformity of forms and correspondence across taxes, new statements of accounts and direct electronic refunds; and
- k. making maximum use of electronic transactions.

6.3. Merger State of Play as at March 2017

(Source: Merger Questionnaire, Meeting held with Senior Management of the three revenue-generating Departments)

Officials responsible for the merger explained that this project is an ongoing process. The MITA Project Team, in consultation with the CR and MFIN's Permanent Secretary, prioritised the main tasks such that critical services could be implemented in order for the Commissioner to leverage the benefits of the consolidated process.

This Office was informed that, up to the date of the meeting with Senior Management, held earlier in 2017, the major progress related to the IT aspect rather than other areas. It was also explained that a Strategic Plan was submitted to the CR. In addition, responsible officials also highlighted that even though it was crucial for the integration to be a success, to date a Director General Support Services had not yet been appointed.

Moreover, it was stated that a Permanent Secretary (Merger and Administration) within MFIN has been appointed and tasked with the merger of the Revenue Departments within the Office of the Commissioner for Revenue. Following a number of meetings, a project team was set up to administer the project, as well as various working groups. A contractor has been identified to analyse all the processes involved in the directorates. An action plan has been agreed upon with the Principal Permanent Secretary on the new One Stop Shop, with implementation date set as May 2018. The implementation date for the merger of the Revenue Departments is set for December 2018.

Enquiry by this Office on whether any studies have been conducted as to the monetary effect of such merger in respect of revenue collection, led to a negative reply. A similar response was also given when queried about whether the Departments, separately or collectively, considered the use of External Debt Collection Agencies in the process of collection of arrears.

Various ongoing measures are currently being implemented to support the merger implementation:



a. Starting-up a Business

The first phases of the merger were aligned to the Office of the Prime Minister’s initiatives, where current processes were reviewed. Procedures, such as those encountered during the start-up of a business, were facilitated on a nationwide basis. These procedures included key processes to register for a VAT number, as well as to register as a taxpayer and as an employer with the taxation Departments. Malta Enterprise and MITA coordinated the task. Business process reviews were also carried out at the IRD and the VAT Department, allowing for the registration procedures to be automated and for the VAT, Income Tax and Employer (PE) numbers to be issued online when information is received from a central form.

This process will be enhanced throughout 2017 to include general activities related to operating a business, such as changing of address and expanding the business. The IRD and the VAT Department have also consolidated their call centre services with those of servizz.gov. This initiative’s main scope is to have a One Stop Shop for citizens and businesses to be better served by the Government as a whole, rather than by separate entities in piecemeal fashion. As part of the initiative, the officers of the IRD and the VAT Department are also visiting local servizz.gov offices to provide services to taxpayers.

b. Website

A consolidated approach for taxpayers and their representatives, for the use of online services, was implemented in November 2016. In addition, the NAO is informed that a consolidated CR website is planned to be launched by the end of 2017.

c. One Stop Shop

Further work is also in progress to have all Cash Office functions amalgamated into one application, whereby taxpayers will benefit from the services of a One Stop Shop. Additionally, on 10 July 2017, the IRD engaged MaltaPost p.l.c. to provide payment services in a number of branches nationwide. VAT taxpayers also have the facility to effect payment at MaltaPost p.l.c. branches.

d. Joint Enforcement Unit

During November 2016, MFIN launched the Joint Enforcement Unit to enhance enforcement, and fight unfair competition in the Maltese economy. The first phase in the planning of the IT Systems was launched in the second quarter of 2017, in order to enhance the current data warehouse with further information from the DOC, whilst also launching a model using big data concepts for tax compliance purposes. The Unit is currently carrying out tax and VAT risk exercises, as well as assisting all investigative Units. During the second half of 2017, training initiatives are also planned to increase technical knowledge and readiness to improve the inspections related to cash registers and related IT systems by economic operators.

Moreover, the business process relating to the IRD and/or VAT refunds was re-engineered in order to check for any missing returns. As stated by the Department, set-offs are also being effected upon request between the IRD and the VAT Department.

e. Consolidated Debt Collection

Furthermore, a risk analysis is currently being carried out to consolidate the debt collection processes across the taxation Departments, such that a new modern solution is implemented in subsequent years.

f. Call Centre

A contract was entered into on 25 January 2012, effective as from 1 April of the same year, for the setting up of a call centre with a private company specialising in call centre operations. This agreement was originally entered into for a one-year period extendible to another year. Thereafter, the agreement was extended on an ad hoc basis following approval by MFIN until such time that a proposed tender would have been awarded. However, in October 2016, the call centre service was assimilated within the servizz.gov set-up and subject to the conditions and provisions of the overall agreement that the Office of the Prime Minister entered into in October 2015, incidentally with the same supplier. The proposal to issue a tender for such services was therefore discarded in favour of the servizz.gov arrangement. The aim of this centre is to address incoming queries by taxpayers.

Chapter 7

Report Highlights

7.1. Income Analysis

This analysis has delved into the revenues received by the three main revenue-generating Departments during 2016, as well as trends in public income since 2012.

Most noticeable were the upward trends in each of their relative incomes:

- €329.5 million increase in absolute terms in Income Tax over the reporting period, with material spikes in Capital Gains Tax for 2014 (25%) and 2015 (20%) as well as Provisional Tax which experienced a 21% increase in 2015.
- An increase of €51.6 million in Duty on Documents and Transfers over the period 2012 to 2016. In particular, a 29% increase was experienced in 2015, partially attributed to the First Time Buyers Scheme as well as the UCA Scheme, which contributed to increased contracts of sale due to the decreased rates of Duty on Documents.
- VAT income experienced a steady upward trend since 2012, with a total increase of €191 million.
- A €124.1 million growth in the DOC income, which was mostly due to significant increases in Import and Excise Duties in 2014 to 2016 over the previous years.

7.2. Enforcement Action

An assessment of the various enforcement actions taken by the Departments was also provided throughout this analysis.

In the case of the IRD, the most commonly used tool were remission of interest agreements in relation to arrears of company tax and tax due by individuals, which totalled 744 during 2016 and contributed to the collection of €4,072,557 by 31 May 2017.

Similarly, during the year under review, 92 remission agreements were also entered into by the VAT Department, which resulted in collections of €2,983,697. Collection efforts by this Department also included issues of 760 Demand Notices, 59 Judicial Letters, as well as 137 Civil Court sittings.

Legal action taken by the DOC during 2016 included 118 cases at the Criminal Courts, as well as 32 cases at the Civil Courts. The Department also settled 111 cases out of Court, issued 18 Letters to Prosecute and 265 Seizure Notes.

7.3. Staff Complement

In spite of the considerable increases registered by way of revenue collection, the various staffing requirements across the revenue-generating Departments, which, as can be seen throughout this analysis appears to be lacking, require urgent attention. It is important that, as far as possible, any justified human resources' shortfalls are properly addressed to ensure that the work carried out with regards to revenue collection is made efficiently and to the highest standards.

7.4. Integration of Revenue Departments

(Source: Merger of the Revenue Departments into One Entity – The Accountant – Winter 2014 Edition)

This Report has also considered the process for the amalgamation of the Revenue Departments, which due to its inherent complexity, involves considerable work. Nevertheless, this development will provide the opportunity to review existing legislation and operations with the objective of simplifying the whole tax system. The result will ensure that compliance costs are reduced, the system is fair, and taxes are collected on time through better enforcement, as well as ultimately providing a better service to the businesses and public in general.

2016-2017 (to date) Reports issued by NAO

NAO Work and Activities Report

March 2017 Work and Activities of the National Audit Office 2016

NAO Audit Reports

November 2016 Performance Audit: Managing and Monitoring the State Schools' Transport Services

December 2016 Annual Audit Report of the Auditor General - Public Accounts 2015

December 2016 Annual Audit Report of the Auditor General - Local Government 2015

December 2016 An Investigation of Property Transfers between 2006 and 2013: The Transfer of Land at Ta' L-Istabal, Qormi

December 2016 An Investigation of Property Transfers between 2006 and 2013: The Acquisition of 233, 236, and 237 Republic Street, Valletta

January 2017 Contribution of the Structural Funds to the Europe 2020 Strategy in the Areas of Employment and Education

February 2017 Information Technology Audit: Cyber Security across Government Entities

May 2017 Performance Audit: Protecting Consumers through the Market Surveillance Directorate's Monitoring Role

June 2017 Performance Audit: Procuring the State Schools' Transport Service

July 2017 An Investigation of Property Transfers between 2006 and 2013: The Transfer of the Property at 83 Spinola Road, St Julian's

July 2017 An Investigation of Property Transfers between 2006 and 2013: The Expropriation of the Property at Fekruna Bay, St Paul's Bay

September 2017 Performance Audit: Landscaping Maintenance through a Public-Private Partnership

October 2017 Performance Audit: Maintaining and Repairing the Arterial and Distributor Road Network in Gozo

November 2017 Follow-up Reports by the National Audit Office 2017

November 2017 Performance Audit: Outpatient Waiting at Mater Dei Hospital

November 2017 Report by the Auditor General Public Accounts 2016