

Success of tax auditing activities

The task of the Finnish Tax Administration and its Tax Auditing Unit is to ensure the accumulation of tax revenue, that all taxpayers are treated equally and the overall credibility of the tax system. Tax control is a central tool in combating the tax deficit. Tax auditing is a special type of monitoring that is performed as part of tax control. The Tax Auditing Unit was allocated a total of EUR 41,845,000 to cover its expenses in 2011. The same year, the unit spent slightly more than 700 person work years to conduct its activities. During the past few years, an average of about 3,500 tax audits have been carried out each year and the proposed debiting based on the audits has totalled about EUR 300 million annually.

The purpose of the audit was to examine the success of and the requirements for the tax auditing conducted by the Finnish Tax Administration. The main question posed in the audit was: has the tax auditing performed by the Finnish Tax Administration been successful? The tax auditing has been successful if the achievement of the current performance targets is used as the criterion. However, the performance targets are of such nature that the meeting of the targets does not give an adequate picture of the actual success of the tax audits. At the moment, there is no information available on tax auditing that would allow appropriate verification of the impact of the activities.

The reorganisation of tax auditing into a single national entity as of 1 September 2010 significantly improved the chances to improve on the performance of the activities. It has become increasingly necessary to develop and harmonise tax auditing as part of the oversight and management of the activities, and the chances to do this have also improved.

Current provisions on tax auditing or the preparatory material regarding them do not contain any specification regarding the grounds for maintaining a tax auditing organisation. It is not possible to derive or create performance targets for tax auditing on the basis of these provisions. It can be assumed that the effectiveness of the tax auditing activities is largely due to the fact that taxpayers are aware of the existence of tax auditing and know that they may be subject to credible tax audits.

The current performance targets for tax auditing are mainly intended to guide the manner in which the audits are focused. The effectiveness per-

formance targets are all targeting objectives. It is clear that the procedure in question has a positive impact on the effectiveness and internal efficiency of tax auditing. However, the information on how well individual performance targets are met does not reflect the actual impact of the activities. There are no indicators for productivity and efficiency, two factors that are central to performance-based thinking. Outcome and quality management targets and implementation information are fairly good ways of describing success.

Measuring the impacts of tax auditing and creating performance targets for the effectiveness of the activities are extremely challenging. Examining the impact of tax auditing separately from the overall impact of the work of the Finnish Tax Administration is difficult. It is difficult to measure the overall preventive role of tax auditing, its contribution to the accumulation of the tax revenue or its impact on the grey economy.

The National Audit Office is of the view that the quality of the performance targets should be improved within the framework of the available resources. The process should involve the Ministry of Finance and all those in the Tax Auditing Unit of the Finnish Tax Administration (including individual auditors). In the development of performance indicators, consideration should also be given to cooperation and links with other authorities. In the view of the National Audit Office, considerably more use should be made of the information gathered from research, assessment and findings concerning the effectiveness of the tax auditing activities when measures are taken to steer and manage the activities.

In the opinion of the National Audit Office, particular attention should be paid to the appropriateness of the working hour entries when the accuracy of information on the meeting of the performance targets is checked. It is essential to the data content of the performance information.

At the moment, not enough use is made in quality assurance of the differences between debiting proposals based on tax audits, the final debiting and the reasons for the differences. Furthermore, the monitoring of the claims for adjustment and appeals is insufficient and unsystematic at present.

The quality of the tax audits is ensured by means of extensive procedures incorporated in the auditing process. These procedures have a significant positive impact on the quality and uniformity of audits. However, no systematic monitoring or research information on the quality or quality trends is being produced. Moreover, at the moment, there is no quality system covering the tax auditing activities. The National Audit Office is

of the view that understanding the quality of tax auditing and its quality trends are essential to the guidance and management of operations.

Tax auditing is mainly based on staff input, which means that skilled personnel are essential to the success of the tax auditing activities. The sector is undergoing a transition process as a large number of experienced and skilled auditors are retiring. At the same time, quite a few new auditors have been recruited in recent years. In 2011, the Tax Auditing Unit spent a total of 8.6 days on training per person work year, whereas the target was 12 days. There have been substantial differences in training participation rates. The National Audit Office is of the view that the management of the Tax Auditing Unit should ensure that the quality of training and differences in participation rates do not prevent the meeting of the performance targets.

Those responsible for the oversight and management of tax audits were of the opinion that the competence provisions or taxation or other legislation have not prevented the conduct of operations in an appropriate manner or affected the performance in any significant way. However, the responsible parties are of the view that there is room for development in the provisions so that the quality of tax auditing can be improved. The National Audit Office is of the view that those responsible for the oversight and management of tax auditing should remain active in matters concerning the correction of legislative deficiencies.

Irrespective of the performance targets used, the success of the tax audits crucially depends on which taxpayers are selected for tax auditing. An important development process concerning the selection procedure is currently under way. The focus is shifting to nationwide targeting of audits based on risk analysis. In the opinion of the National Audit Office, the selection of targets is critical to the success of the tax auditing activities.

Tax auditing is a central instrument in the tackling of the problem of the grey economy. There is no unanimity in the Finnish Tax Administration on whether tax audits can help combat the grey economy or on how tax auditing should be used to tackle the problem. Some tax administration officials are of the view that there is a clear need for more audits targeting the grey economy. There are also those who think that the focus should be shifted to real-time audits as these are considered to be a more effective tool in combating the problem of the grey economy than the traditional retroactive approach.

The number of audits targeting the grey economy should be adequate so that they have the necessary preventive impact. The audits on the grey economy often require substantial resources. Shifting the focus to them

would mean fewer audits in other areas and a decrease in the direct tax revenue resulting from audits. The National Audit Office is of the opinion that the focus on audits on the grey economy should be based on sufficient information regarding their economic and other impacts.