Chapter

8

Canada Revenue Agency
Collection of Tax Debts

All of the audit work in this chapter was conducted in accordance with the standards for assurance engagements set by the Canadian Institute of Chartered Accountants. While the Office adopts these standards as the minimum requirement for our audits, we also draw upon the standards and practices of other disciplines.

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Canada Revenue Agency
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Main Points

What we examined

We examined the Canada Revenue Agency's collection of tax debts, which we last audited in 1994 (when the Agency was Revenue Canada). In that audit, we reported that the Department's automatic risk-scoring systems, developed to help prioritize accounts for collection action, were ineffective. We also found that the Department lacked profiles of tax debtors, a fast-track approach to collecting all large tax debts, consistency in the way it assessed taxpayers' ability to pay, quality standards for the work of individual collectors, and adequate information on results to assess performance properly.

This time we examined whether the Agency uses efficient and timely processes to collect the unpaid personal tax, corporate tax, goods and services tax, and payroll deductions by employers that together constitute 86 percent of all tax debts.

Why it's important

In the vast majority of cases, taxes and payroll deductions owed are paid to the Agency on time. However, there is always a significant amount of taxes, penalties, and interest that the Agency has assessed but not collected. At 31 March 2005, the total amount in undisputed tax debt stood at $18 billion, of which the Agency expects to collect only about $13.3 billion—it considers the rest to be doubtful accounts and not collectible. The Agency also writes off a certain amount in uncollectible unpaid taxes every year—in 2004–05 the amount was $2.7 billion.

Managing and collecting tax debt is a complex activity involving more than 4,000 full-time-equivalent staff and many information technology systems. In 2004–05, the Agency collected tax debts of about $9 billion. Any improvement in its ability to collect tax debts efficiently and within a reasonable length of time could add millions of dollars in revenues to the Crown every year.

What we found

- Overall, the Agency has not made satisfactory progress in addressing the recommendations of our 1994 audit. Its approach to assessing files for risk continues to lack sophistication and has major weaknesses that impede the timely collection of tax debts. Further, the Agency still lacks information needed to manage its collection of the tax debt effectively.

- The Agency has made some significant changes to its collection systems and some of its practices. It has updated its automated system that manages low-risk tax debts, opened a national call centre, and established national pools to better manage workload. It has improved the procedures to collect large tax debts.
- Cash collected by collectors working at Tax Services Offices has increased since 1994 and now stands at about $9 billion annually, or an average of about $2.3 million for each collector. Yet despite this increase, the tax debt has grown at a faster rate than total taxes paid. At the same time, management is not collecting the data it needs to understand both why the amount of tax debt is growing and what it comprises.
- Management also lacks important information on performance. The information used to manage the collection of the tax debt is focussed mainly on activities at Tax Services Offices, where the most complex accounts are handled. Little information is available on automated transactions and accounts processed at the national call centre. Information is not available on the effectiveness of the various types of collection actions, although it would be valuable in helping collectors select the best ones.
- The Agency has set ambitious goals in its strategic vision for the future of collections. However, there is still no detailed plan outlining the steps the Agency will take to address the specific challenges outlined in the vision or the measures that will be used to gauge progress toward its goals.

The Canada Revenue Agency has responded. The Agency has agreed with our recommendations and has indicated the actions it plans or has under way to address them.

Introduction

8.1 The vast majority of personal income tax, corporate tax, goods and services tax, and payroll deductions owed by individuals and businesses is paid on time. However, there is always a balance of unpaid taxes and payroll deductions—at 31 March 2005, about $18 billion in undisputed assessed taxes, interest, and penalties remained uncollected. Each year the Canada Revenue Agency writes off a certain amount of tax debt that it considers uncollectible; in 2004–05 it wrote off $2.7 billion in taxes, penalties, and interest.

8.2 Collecting outstanding tax debts is one of the responsibilities of the Agency's Taxpayer Services and Debt Management Branch (see "How the collection system works," page 240). In 2004–05 the Agency had over 4,000 full-time-equivalent staff—mainly collection officers, team leaders, and managers—collecting tax debts in Tax Services Offices across Canada and at the national call centre in Ottawa. The 2005–06 budget for collecting tax debts was $215.9 million.

8.3 The Agency is obligated to collect all taxes and related interest and penalties owed to the Crown; unlike a private sector creditor, it cannot choose its clients. Nor can it refuse services or credit to taxpayers with a poor payment history. A private sector creditor can mitigate its credit risk by charging higher interest rates for riskier clients or demanding security when extending credit, options unavailable to the Agency. However, the Agency can take certain legal actions more easily than private sector creditors; for example, it can issue a garnishee without going to court.

8.4 As well as collecting federal income taxes, the Agency has agreements with all provinces but Quebec to collect provincial income taxes on their behalf. The federal government pays each province the total amount assessed for its provincial income taxes, whether or not the Agency ultimately collects that amount. The federal government keeps any interest earned and certain penalties owed.

8.5 As of 1 August 2005, the Agency also collects debts for Human Resources and Social Development Canada (formerly Human Resources and Skills Development Canada and Social Development Canada) on accounts such as Canada Student Loan, Employment Insurance, and Canada Pension Plan.

Key findings in 1994

8.6 We last audited the collection of income tax debts in 1994, when it was managed by Revenue Canada. In that audit we reported that the Department's automatic risk-scoring systems, developed to help prioritize accounts for collection action, were ineffective. We said it needed to develop profiles of tax debtors, institute fast-track collection of all large tax debts, ensure that collectors used consistent practices in assessing taxpayers' ability to pay, strengthen quality standards for the work of individual collectors, and develop better information on results for use in assessing the performance of collection activities.

How the collection system works

When tax assessments or reassessments are not paid, the unpaid balances are drawn from the appropriate accounting system and become collection accounts. There is a separate accounting system for each revenue line—personal income tax, corporate tax, goods and services tax (GST), and payroll deductions by employers.

The Agency tries to collect the full balance of a tax debt or make an arrangement for payment in full within a certain amount of time. When it is not possible to arrange a payment, legal action can be taken. Legal actions include, but are not limited to

- garnisheeing wages or pensions or accounts receivable,
- setting off the debt against other government payments,
- seizing assets,
- certifying the debt in Federal Court, and
- putting a lien on a taxpayer's assets.

The Agency can take tax debtors to court to collect the unpaid debt.

A combination of procedures, both automated and by human intervention, is used to collect outstanding tax debts. The procedures used include computer-generated letters, telephone calls, field visits, and legal actions. Collection actions take place automatically through REMITS (Revenue Enforcement Management Information Tracking System), at a national collections call centre in Ottawa, at eight locations that collect for two national pools of accounts (personal tax and GST), and at Tax Services Offices across Canada. The size and complexity of an account determine which collection mode will be used.

REMITS sends out letters to tax debtors and handles some accounts for which arrangements have been made. The call centre conducts mainly outbound calls to tax debtors whose debts are below a certain dollar limit. The call centre has a telephone system that allows it to automatically dial out to taxpayers. The national pools conduct mainly outbound calls to tax debtors, regardless of geographic boundaries, for individual tax and GST owed below a certain dollar limit. The pools also conduct limited enforcement actions such as garnishees. The Tax Services Offices work on the larger and more complex accounts and conduct a full range of legal actions, such as seizing assets and placing liens on the property of tax debtors.

Information technology systems. The Agency has several systems that help it undertake and manage collection activities. Because the Agency collects debt on all revenue lines, its information technology systems have to connect to the information technology systems of all revenue lines. The unpaid balances of tax, penalty, and interest for personal and corporate tax are transferred from the accounting systems into two collections systems: the management information system STARS (Statistical Tracking Analysis and Reporting System) and REMITS. The unpaid balances of goods and services tax and payroll deductions are transferred to ACSES (Automated Collections and Source Deductions Enforcement System).

The STARS system provides information to staff to manage their operations. It provides information on new debt assessed but not paid, cash collections, write-offs, debt aging, and revenue line. A query facility allows for queries of accounts.

REMITS applies a risk model to individual and corporate tax debts to determine whether they should be handled by REMITS, the call centre, a national pool, or Tax Services Offices. REMITS then handles some accounts automatically and routes others to the appropriate location.

Collection officers use a system called ACSES to manage their accounts. ACSES allows collection officers to document the details of day-to-day collections activity on each account in a diary, bring forward work, refer work to team leaders and managers for review and approval, and link to other Agency systems.

Important changes since 1994

Fairness provisions—Legislation that allows the Minister of National Revenue to waive or cancel all or part of any interest or penalty owed by a taxpayer because of a delay or error by the Agency, circumstances beyond the taxpayer's control, or the taxpayer's inability to pay. (Amounts waived have not yet been charged; amounts cancelled have already been assessed.)

8.7 In 1995, the House of Commons Standing Committee on Public Accounts expressed concern about the Department's estimate of the realizable value of tax debts, its lack of effective risk scoring and fast tracking of large debts for collection, the lack of information and consistent guidelines on applying the **fairness provisions**, and a lack of information for parliamentarians. The Department's plan of action to address the Committee's concerns included completing an integrated revenue-collections system, making early contact on large accounts, setting up call centres, and enhancing the assessment and scoring of accounts for risk.

8.8 Also in 1995, Revenue Canada completed a study of the collections process. The study questioned the effectiveness of sending multiple letters to advise debtors of the amounts they owed. It found that Revenue Canada's existing system did not identify potentially high-risk debtors and that long delays occurred before collection officers took action. It also found that industry good practice was to contact tax debtors early in the collections process and recommended that a national call centre be set up.

8.9 To address these weaknesses, Revenue Canada developed and installed the Revenue Enforcement Management Information Tracking System (REMITS) in 1997. This automated system was designed to route accounts to the appropriate mode of collection, based on risk. It was also designed to manage the movement of accounts through the collections system. A national call centre was set up the same year to handle high-volume, uncomplicated collection accounts.

8.10 The Canada Revenue Agency was established in 1999. Its Board of Management oversees the organization and administration of the Agency and the management of its resources, services, property, personnel, and contracts. The Minister of National Revenue remains accountable for the Agency.

8.11 In 2002, the Agency found that it was still having difficulty dealing with the volume of collection accounts and the increasing number of aging accounts. It decided to establish national pools to handle certain more complex accounts from anywhere in the country and accounts that the call centre was not able to collect. The pool concept, and the call centre concept before it, changed the traditional assignment of work based on geographical boundaries. National pools of personal tax debt accounts were established in April 2003 and of goods and services tax debt accounts in April 2004. Depending on their size and complexity, collection accounts can now be handled by REMITS, the call centre, a national pool, or a Tax Services Office.

8.12 The Agency has created the Continuous Improvement and Quality Assurance Section (CIQAS) to monitor collections at the Tax Services Offices. The Section reviews the application of collection policies and procedures, identifies and shares best practices, and reviews active and written-off accounts.

8.13 In 2004, the Agency split the Assessment and Collections Branch into the Assessment and Client Services Branch and the Revenue Collections Branch. Each Branch is headed by an Assistant Commissioner. In January 2006, the Revenue Collections Branch was given additional responsibilities and became the Taxpayer Services and Debt Management Branch.

Focus of the audit

8.14 The objective of our audit was to examine whether the Canada Revenue Agency uses efficient and timely processes to collect tax debts. Our audit focussed on the personal tax, corporate tax, goods and services tax, and payroll source deductions that constitute about 86 percent of all tax debts. We also considered whether the Agency has made satisfactory progress on the issues that we reported in 1994 and that Revenue Canada also reflected in its 1995 action plan to the Public Accounts Committee (see "Progress in addressing our 1994 recommendations on collecting income tax debts," page 260).

8.15 We did not examine debts for which the taxpayers were disputing the assessment that gave rise to the debt, given that in most such cases the law prevents the Agency from taking any legal collection action. Nor did we examine miscellaneous tax debts, which include non-residents' taxes, other levies, excise fees, and customs fees.

8.16 We did not include write-offs or fairness provisions in our audit, as in 2002 we reported that the Agency had reasonable controls in place to guard against inappropriate write-offs of taxes owed and had improved its administration of the fairness provisions (April 2002 Report, Chapter 2, Canada Customs and Revenue Agency—Tax Administration: Write-Offs and Forgiveness).

8.17 Further details on the audit can be found in **About the Audit** at the end of the chapter.

Observations and Recommendations

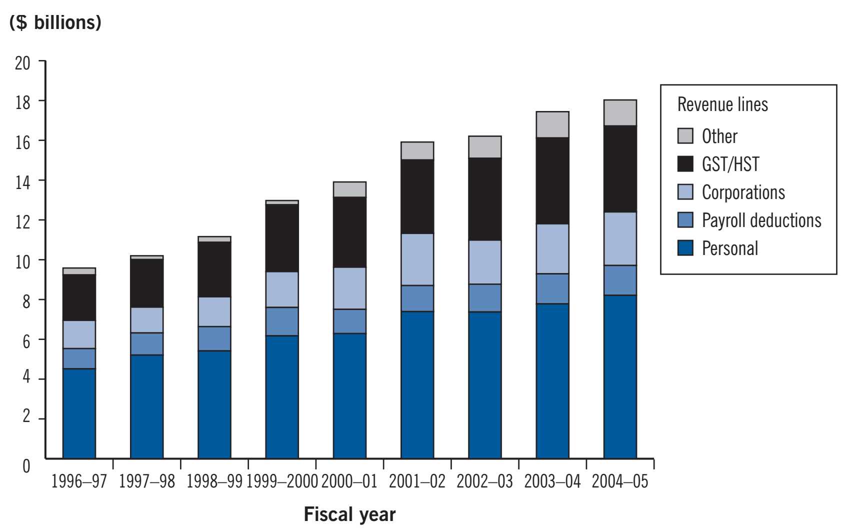
The tax debt continues to grow

Undisputed tax debt is more than $18 billion

8.18 At 31 March 2005, uncollected taxes, interest, and penalties owed and undisputed totalled about $18 billion and involved about 3.3 million accounts. Debts for which taxpayers were disputing the assessment that gave rise to the debt accounted for about $6 billion more. Debts related to personal income tax are about 45 percent of the total, a proportion that has not changed since 1996–97 (Exhibit 8.1).

8.19 Cash collections have risen and targets have been exceeded. Cash collections at Tax Services Offices (including national pools) rose from $5.3 billion in 1996–97 to $8.8 billion in 2004–05—an average increase of $0.5 million for each collector. In 2000 the Agency estimated that the total tax debt could reach about $28 billion by 2004–05, and it requested added resources to help it slow the growth. It received the requested resources for the fiscal years 2001–02 to 2004–05 and made a commitment to keep the tax debt below a certain level for each of those years. It also made a commitment to collect a specified amount of cash in each fiscal year of that period. It has exceeded its targets in both cases (Exhibit 8.2).

Exhibit 8.1 The composition of the tax debt by revenue line



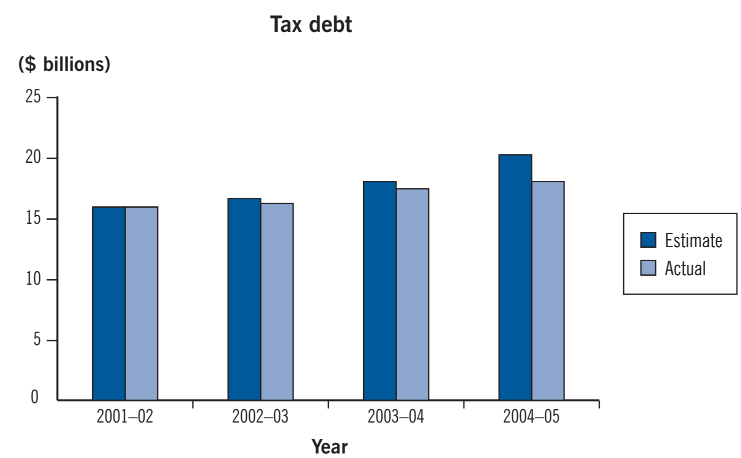
Personal income tax debt makes up the largest portion of the tax debt. The proportion of personal to total income tax debt has not changed since 1996–97.

Source: Canada Revenue Agency

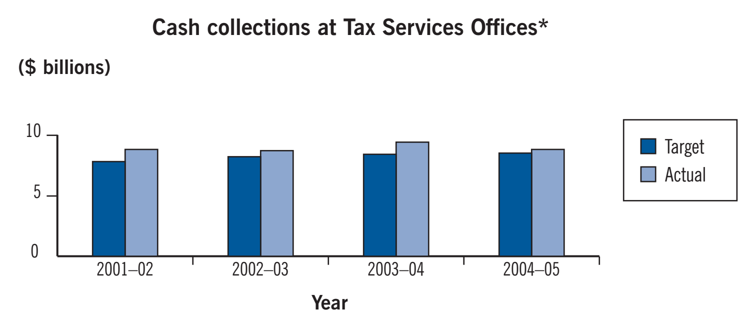
8.20 Despite these efforts, however, the tax debt has grown 88 percent since 1997, while the Agency's total cash receipts (taxes paid) have grown 48 percent (Exhibit 8.3). In other words, the tax debt is growing at a faster rate than total cash receipts. The Agency needs to understand why this is happening so that it can develop strategies to slow the growth of the tax debt.

8.21 The ratio of tax debt to total cash receipts is a trend indicator of how well the Agency is managing the tax debt, and this ratio has grown from 4.27 percent to 5.43 percent since 1997. From 2003–04 to 2004–05, there was a small reduction in the ratio due mainly to increased write-offs of uncollectible accounts. (The write-offs amounted to $2.7 billion; annual write-offs have historically averaged about $1.3 billion.)

Exhibit 8.2 The Agency has kept tax debt below estimated levels while cash collections at Tax Services Offices have exceeded targets



The goal was to keep tax debt at or below the estimate.



The goal was to meet or exceed the target for cash collections.

*Includes national pools

Source: Canada Revenue Agency annual reports

Exhibit 8.3 The tax debt is growing at a faster rate than total cash receipts (taxes paid)

	1996–97	1997–98	1998–99	1999–2000	2000–01	2001–02	2002–03	2003–04	2004–05	Growth since 1996–97
Total tax debt ($ millions)	$9,583	$10,199	$11,161	$12,974	$13,907	$15,913	$16,208	$17,439	$18,027	88%
Total cash receipts ($ millions)	$224,554	$244,777	$255,864	$274,535	$294,788	$300,058	$305,656	$314,519	$332,088	48%
Total tax debt as a percentage of cash receipts	4.27%	4.17%	4.36%	4.73%	4.72%	5.30%	5.30%	5.54%	5.43%	

Source: Canada Revenue Agency annual reports and cash receipts reports

Management lacks information on why the tax debt is growing

8.22 **Poor understanding of the makeup of tax debt.** We found that the Agency does not have a full understanding of the composition of the tax debt and why it is growing. In 2003 and again in 2004, the Board of Management expressed concern about the increase in tax debt. It indicated a need for a clear and concise explanation of the reasons for growth and for an action plan to address them. A recent Internal Audit review set out to identify trends and factors that have contributed to the growth of tax debt and to provide the explanation requested by the Board. However, that review was hampered by a lack of consistent data to analyze. The review suggested some possible causes for the growth but was unable to provide a clear and concise explanation. The Agency presented an action plan that included establishing a framework for analyzing trends in tax debt growth by revenue line.

8.23 We also found a lack of consistent data to help the Agency understand the makeup of the tax debt, explain why the tax debt is growing, and develop a strategy for collecting it. For example, the Agency does not track how much of the tax debt represents initial assessments, reassessments requested by the taxpayer, or reassessments initiated by the Agency. Debts are sometimes harder to collect when the Agency initiated the reassessment than when the taxpayer requested it, and those cases call for a different collection strategy.

8.24 Allowance for doubtful accounts is more than one quarter of total tax debt. The recent Internal Audit review noted that the allowance for doubtful accounts was at an "unhealthy" level. Although the $2.7 billion write-off of accounts in 2004–05 significantly reduced the allowance as a percentage of tax debt, it is still equivalent to over 26 percent of the total tax debt (Exhibit 8.4). This indicates that the Agency continues to carry many accounts with little potential for recovery.

8.25 For the last three years the Agency has conducted an exercise to determine, for financial statement purposes, what allowance to make for doubtful accounts. The allowance for doubtful accounts reflects management's best estimate of the collectibility of amounts assessed but not yet paid. The Agency reviewed about 3,000 accounts for the year ended 31 March 2005 to evaluate how collectible each tax debt was. It did not use the information gathered in this exercise to help it understand why some accounts become uncollectible in order to develop better strategies for dealing with aged accounts. However, in the fall of 2005, the Agency initiated a separate review of uncollectible tax debts to understand why accounts become uncollectible. It will review a sample of uncollectible accounts and analyze the results to identify factors that may reduce or eliminate the Agency's potential to recover the debts.

8.26 Instalment remitters are an ongoing concern. Employed taxpayers generally have income taxes deducted from their pay and remitted to the Agency by their employers. Others are required to pay instalments themselves throughout the year to cover their taxes. The Agency charges interest on instalments that are insufficient or not paid on time but has few other means to enforce the requirement. About 40 percent of accounts in the sample we selected from personal income tax debts involved instalment remitters, suggesting a compliance problem in this category. The Agency estimates that the number of instalment remitters with tax debts who have not paid their assessed

Exhibit 8.4 Allowance for doubtful accounts shows many tax debts are likely uncollectible

Year	2002–03	2003–04	2004–05
Tax debts ($ billions)	$16.2	$17.4	$18.0
Allowance for doubtful accounts ($ billions)	$5.4	$5.7	$4.7
Allowance for doubtful accounts as a percentage of tax debts	33.3%	32.8%	26.1%

Sources: Canada Revenue Agency annual reports and allowance for doubtful accounts documents taxes is about 85,000; they account for about 38 percent of total taxes owed by individuals. However, the Agency does not have more detailed information about these remitters that would allow it to understand the extent of the non-compliance and the reasons for it, so that it could develop strategies to promote compliance.

8.27 The Agency has tried to address the problem of the many instalment remitters who have not paid their assessed taxes. It has provided information on its Web site and, in 2003–04 and 2004–05, collection officers at the call centre telephoned taxpayers who had not paid their quarterly tax instalments and reminded them to send in the payment.

8.28 **Recommendation.** The Canada Revenue Agency should identify and collect the data it needs to analyze the makeup of its tax debt and to develop better collection strategies.

The Agency's response. The Agency agrees that understanding the makeup of tax debt is an important factor in developing its strategies, although the Agency's efforts have resulted in increased collector productivity since 1994. In addition, the Agency has exceeded important program delivery commitments made to the Treasury Board, as noted in this chapter.

The Agency has taken important steps to increase its capacity in the area of tax debt research by launching the Agency's Integrated Revenue Collections (IRC) project, which is developing advanced data-warehousing and data-mining capabilities. In addition, the Agency has set up a team within its organization dedicated to conducting debt management research. These initiatives will support the horizontal approach to compliance research across the Agency. The Agency is taking important steps to ensure that the IRC project is being managed in accordance with accepted project management practices. Some deliverables have already been released, such as the All Revenue Tables.

Management lacks important information on performance

8.29 Management needs to have the right performance information to ensure that its strategies are working and its resources are assigned to the right areas. Our review of good practices found that organizations are building flexible management information systems to allow for customized management reports that can answer a wide range of questions. Combined with a data analysis tool, this gives them more ability to analyze their operations and improve their performance.

Lack of information on different modes of collection

8.30 The Agency's Statistical Tracking Analysis and Reporting System (STARS) provides monthly summary-level information on new accounts received, cash collected, amounts written off, and the aging of accounts. We found that management information covers mainly the collection actions at Tax Services Offices. For example, STARS keeps track of cash collected at the Tax Services Offices (including the national pools). It does not track cash collected by the automated system and at the call centre. Information on automated transactions and on call centre and national pool activities is difficult to obtain and is lacking in reports to management and to Parliament. When Revenue Canada installed the call centre and the REMITS system, it noted the need to maintain certain key performance measures such as dollars collected by the various collection modes, but this has not been done. Furthermore, we found that reports to management contain no information on the significant portion of tax debt that is managed by automated systems—about 2.4 million accounts totalling about $2.6 billion.

8.31 It is important that the Agency track amounts collected by each collection mode. Because the Agency is not tracking these amounts, it is difficult to determine whether the call centre has been a worthwhile investment, or whether the national pools are more efficient than the Tax Services Offices were at collecting similar accounts. Furthermore, without this information it is difficult to optimize the allocation of resources among the four collection modes, taking into account the need for fair and consistent treatment of all taxpayers and the need to encourage compliance.

Lack of information on results of collection actions

8.32 We found that good collection practices are aimed at getting the best return on investment. Collectors can use a range of approaches that produce different results. Like the Agency, other collectors typically lack enough resources to act on every account but, through careful analysis of return on investment, they can use the collection tools that bring the highest returns.

8.33 In our sample of Agency accounts, we noted that collection officers record many collection actions in their diaries. But there is no automated summary of these actions or their results to help collection officers and their supervisors understand which actions are the most effective. For example, there is no summary of

- requirements for information (notices issued to financial institutions and others);

- garnishees (requirements to pay);
- certificates filed in federal court to secure the debt;
- liens entered in the land registry or personal property registry; and
- credit bureau searches.

8.34 Nor is management given a useful periodic summary of collection actions taken and their results. Such a summary would help it identify which actions are getting the best results. That information could then be used to analyze the Branch's collection strategy and to help determine how to use collection tools more effectively.

Lack of comprehensive information

8.35 **No information on frequency of danger-of-loss reviews and jeopardy applications.** Legislation prevents the Agency from starting legal collection action on most categories of debt until 90 days after it issues a notice of assessment. This is to allow the debtor time to file a notice of objection. However, a provision of the legislation allows the Agency to enforce payment immediately by making a jeopardy application—that is, satisfying a judge that it has reasonable grounds to believe a delay would jeopardize the ultimate collection of the debt. We noted in 1994 that Revenue Canada was not keeping track of how many cases involving danger of loss had been referred to legal counsel by collectors, how many had proceeded to court, and how many had been decided in the Crown's favour. Our follow-up audit found that the Agency is still not tracking this information and therefore does not know how effectively the legislative provision works.

8.36 **Lack of information on insolvency files.** Usually in a case of insolvency, the amount of tax debt the Agency can collect is quite small. Yet insolvency accounts can consume a significant amount of a collector's time. The Agency does not have complete data on the number of accounts, and the size of debt affected by insolvencies. Nor does it have information on the amount of time collectors are spending on these accounts, although it plans to start collecting it. Such information is essential to developing a good collection strategy for managing insolvency files.

8.37 **A new system to capture results shows promise**. In 1994 we found that information on results was insufficient to properly assess collection performance, by team or by individual. In the early stages of the present audit, team leaders and managers told us that the management information system still did not show results by team or by individual collector; team leaders and managers were collecting the information themselves. In the summer of 2005, a new system, All Revenue Tables (ART), began operating in three regions. Team leaders and managers told us they find ART a useful tool for capturing information on individual and team performance.

A key performance indicator has weaknesses

8.38 One of the key performance indicators the Agency uses is the ratio of the value of accounts resolved to the value of new accounts and interest owed on old accounts. In our view, this indicator does not provide a clear measure of performance because it compares unlike elements—such as cash collected on old accounts compared with the intake of new accounts (Exhibit 8.5). Furthermore, the indicator is not complete because it considers only accounts handled at the Tax Services Offices and national pools, ignoring the accounts that are managed by the automated system or handled at the call centre.

Exhibit 8.5 Key performance indicator

$$\textbf{Performance indicator} = \frac{\begin{array}{c}\textbf{accounts resolved at Tax Services Offices}\\ \text{(cash collections on new and old accounts +}\\ \text{accounts written off)}\end{array}}{\begin{array}{c}\textbf{intake of accounts at Tax Services Offices}\\ \text{(new accounts assigned +}\\ \text{interest on old accounts not resolved)}\end{array}}$$

The indicator does not provide a clear measure of performance because it compares unlike elements and is incomplete.

Source: Canada Revenue Agency

8.39 Using this indicator, the Agency reported to Parliament that accounts resolved matched the intake of new debt in 2004–05, a result the Agency had not achieved in some time. The Agency was able to report this result in part because the indicator includes write-offs of uncollectible tax debts. In 2004–05, write-offs amounted to $2.7 billion, about double the historical average.

8.40 The Agency's Report on Plans and Priorities has proposed a new indicator of performance for 2005–06: the percentage of intake resolved in the year of intake. The annual target for performance is 60 to 65 percent. This represents an improvement, if it includes cash collected on all accounts by all modes of collection (automated system, call centre, national pools, and Tax Services Offices) and does not include write-offs in the calculation.

8.41 Recommendation. The Canada Revenue Agency should significantly improve its management information to make it complete and comprehensive. It should develop reliable techniques and information sources to determine on a regular basis the results of its collection efforts and use that information to guide its decision making for each of its major collection modes and actions.

The Agency's response. The Agency agrees that improvements are needed to enhance its management information systems—improvements that are currently being addressed through its Integrated Revenue Collections project. However, the Agency believes that the performance indicators it has established for its collections program appropriately reflect program activities, including write-offs.

The Agency continues to review its performance indicators in order to ensure their accuracy and appropriateness. This review is in line with the OAG's annual performance assessment on the fairness and reliability of the program information described in the Agency's Annual Report to Parliament.

The Agency continues to manage uncollectible accounts in accordance with the procedures that were favourably reviewed by the Auditor General in 2002.

Risk management is deficient

Managing risk is critical to collection efforts

8.42 Risk management is widely acknowledged as a critical factor in the proper management of any collection function. It is even more critical when that function lacks enough resources to handle a growing and aging backlog of tax debt. Our review of good practices found that public and private sector organizations are not only using risk management widely but are using sophisticated risk management models in collection activities.

8.43 These organizations are scoring accounts based on risk to help their collectors identify the accounts that involve the highest risk and the highest potential payback. With this information, they can direct their efforts more effectively. Generally, an account is assessed for characteristics that signal a risk of uncollectibility, and the combined characteristics (risk factors) yield an overall risk score. Risk scoring is then used to determine collection procedures. For example, high-risk accounts could be subject to aggressive action, whereas a more moderate approach would be used for accounts that are likely to be paid.

Some improvements have been made to risk assessment systems

8.44 The Agency does not have a collections risk management framework as such, but it does use certain elements of risk assessment. For example, the installation of REMITS in 1997 updated the risk-scoring system for individual and corporate accounts. The Agency has not yet extended the system to goods and services tax or payroll deduction accounts, although that was originally intended.

8.45 REMITS applies a risk model to individual and corporate tax debts and, based on either the dollar value of an account or the risk score, it assigns one of several collection strategies. The size of the tax debt is the main factor that determines the collection strategy. Generally, accounts with small balances are managed by REMITS, with letters sent automatically to the tax debtor. Others are handled by the national call centre or the national pools. Accounts with a high balance and a high risk score are generally routed to Tax Services Offices.

8.46 The Agency intended to review the risk-scoring system on a regular basis but has never done so. Furthermore, the Agency has not done a complete test of REMITS since its inception to ensure that it is working as intended. Documentation of the system's risk-scoring module has been poor, so we were unable to determine how the risk scores are calculated and whether they are appropriate. Nor were we able to determine whether REMITS was assigning accounts to the appropriate collection strategies.

Deficiencies identified in 1994 remain

8.47 Our 1994 audit recommended that action be taken to address the several risk management deficiencies we identified:

- The automatic risk scoring of delinquent accounts was ineffective because the risk assessment was limited mainly to the outstanding balance and the age of the account; other important risk factors either were not considered or did not weigh heavily in the risk scoring.
- The risk scores were rarely updated or used to prioritize workload.
- There were no profiles of tax debtors for use in modifying basic collection strategies to improve recoveries from debtors who posed a high risk of non-payment.

- When individuals or corporations had tax debts in more than one revenue line, their total tax debt was not provided automatically. Collectors had to search manually for tax debts across several systems, leaving open the possibility of untimely, inconsistent, or no collection action and thereby raising the risk of loss.

In our follow-up audit, we found that the Agency has not yet dealt with these deficiencies adequately.

8.48 **Key factors are not integrated into the initial risk assessment.** REMITS performs the initial risk assessment of personal and corporate tax debts. The risk assessment does not appear to formally consider key factors such as whether the debtor can likely pay, whether the debtor owes in another revenue line, whether the debt arose from a self-assessment or an Agency action, or whether the debtor has previously filed for bankruptcy. The debt and debtor history are not factored into the risk score. Because the initial risk assessment does not formally consider any of these key factors, the Agency has no assurance that the riskiest files are given priority.

8.49 **Insolvency risk factors are not incorporated into risk assessment**. The Agency has completed four studies that have identified criteria historically associated with insolvency. To date, these criteria have not been used in assessing a file for risk when it first enters the collections inventory, or even when it is assigned to a Tax Services Office for collection. Using indicators of potential insolvency in the screening of files could lead to changing the collection approach in high-risk cases—for example, moving faster to certify the debt, or issuing an enhanced "requirement to pay" if the taxpayer has been bankrupt before.

8.50 **Automated system is not used by collectors to prioritize workload.** When accounts are routed to Tax Services Offices, they are given a risk score by the Automated Collections and Source Deductions Enforcement System (ACSES). ACSES risk scores are used in the national pools and some of the Tax Services Offices to assign cases to collection officers. However, we found that collection officers do not understand or use the ACSES scores. They do their own risk assessments to set their workload priorities. Collectors' risk assessments are not part of the automated system.

8.51 **Risk assessments are not updated to reflect changes in risk levels.** The initial risk assessment is just one element of proper risk management. It is important to also continue modifying and updating the assessment with additional information as new developments occur in the handling of the account. We found no evidence that updating the automated risk assessment for factors other than the size or age of the debt is an ongoing activity. For example, the Agency now allows collection officers to obtain the tax debtor's credit history from a credit bureau, but this information is not used to update the risk scores.

8.52 **Recommendation.** The Canada Revenue Agency should establish a more comprehensive automated risk-scoring system for tax debts, update the risk scores on an ongoing basis, and use the risk scores to prioritize workload throughout the collections process.

The Agency's response. The Agency agrees. Additional investments in risk management systems are needed, and are being made, to realize the full potential of the Agency's collections program and to address the continued growth in accounts receivable. The Agency's Integrated Revenue Collections project is focussed on addressing both past and current concerns raised by the Auditor General with respect to risk assessment and file management, in addition to the above-mentioned management information system improvements.

Efficiency improvements needed

Early action is important in collecting tax debts

8.53 Our review of good practices found that taking action early in the lifecycle of a tax debt account is important to successful collection. Debts become significantly less collectible over time. Moreover, the sooner action is taken, the more likely it is to result in collecting the full debt.

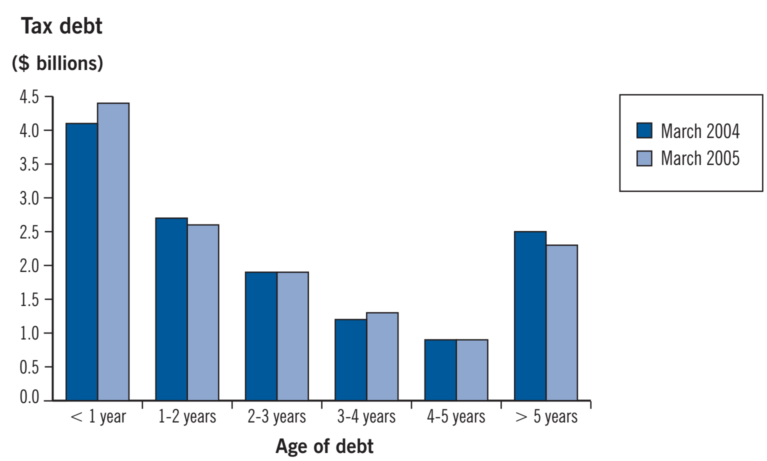
8.54 **Some improvement since 1994 on procedures to collect large debts.** In 1994 we noted that most large tax debts were not fast-tracked for collection. In this follow-up audit, we found that about 76 percent of accounts over $100,000 in our audit sample were looked at within 10 days of their transfer to the Branch. Assistant directors of collections at the Tax Services Offices we visited conduct quarterly reviews of high-value accounts. The reports we looked at by the Continuous Improvement and Quality Assurance Section indicate that the appropriate reviews of large-dollar active accounts are done about 70 percent of the time. The new ART system also provides information on high-value accounts, which helps managers in Tax Services Offices manage their large tax debts.

8.55 **Reporting on timeliness.** The Agency has recognized the importance of timeliness by including it as an expected result in its Report on Plans and Priorities and in the Branch's Strategic Plan for 2005 to 2010. However, its Annual Report is silent on how quickly accounts are moving through the collection systems. The Agency does not maintain data on the time that elapses between collection actions on an account. Nor does it maintain data on the time that elapses between the date when a debt becomes payable and the date when it is fully paid. Therefore, it is difficult to determine whether the Agency's handling of collections is timely.

Aging accounts are a problem

8.56 The Agency's 2004–05 Annual Report stated that 47.8 percent of the value of the tax debts handled at the national pools and the Tax Services Offices was more than two years old, slightly down from 48.8 percent in March 2004 (Exhibit 8.6). Our analysis of the value of the tax debts in the Agency's inventory at the end of March 2005, including accounts handled by the automated system, showed similar results.

Exhibit 8.6 **Almost half of the tax debt at Tax Services Offices* is over two years old**



*Includes national pools

Source: Canada Revenue Agency 2004–05 Annual Report

8.57 **Some files are handled by several collectors.** In our audit sample of active accounts, we found that an average of 5.3 collectors had worked on each account (with the exception of automated accounts) and that each account had an average age of 3.2 years. This meant that each account averaged a new collection officer every seven months. Staff at Tax Services Offices told us that accounts are reallocated among collectors fairly often, for a number of reasons—collectors leave, teams reorganize, and managers feel that accounts frequently need to be seen through "fresh eyes." These reallocations can result in several months of inattention to an account—delays that can be costly to debt recoveries.

8.58 **Some files need stronger collection action.** We also noted in the sample that collectors focussed on collection actions such as letters, telephone calls, and garnishees. Often, they did not take stronger enforcement actions to secure the debt until much later in the collection process, if at all.

Case management system needs improvement

8.59 The number of accounts that collection officers maintain in their inventories varies between 15 and 300. The more senior officers maintain a low number of complex cases and also act as a resource and trainer for less experienced staff. The more junior officers maintain a higher number of less complex cases in their inventories and spend most of their time working on their accounts.

8.60 Collection officers depend heavily on information technology systems and use ACSES in the day-to-day management of their accounts. The most important tool in ACSES is the diary where they record the collection actions they have taken. These actions include making telephone calls, sending legal warning letters, sending requirements for information to financial institutions and other third parties, garnisheeing bank accounts or wages, registering the debt, seizing assets, and placing liens on property. The length of the diaries can run from a few pages in a straightforward case to many pages in a more complex case. Reviews by team leaders and managers are also recorded in the diaries.

8.61 Collection officers told us that ACSES is not user-friendly or efficient. They described the following as major problems:

- The system still does not present the collection officer with all tax debts in the various revenue lines that are associated with one tax debtor. Officers have to locate the tax debts and associate them with the debtor.
- No common diary is established for debtors who have unpaid balances in more than one revenue line; collectors have to move back and forth between diaries.

- Officers have to use function keys rather than a mouse, making the system tedious to use.
- It is difficult to summarize the information contained in a very detailed diary.
- Accessing other Agency systems is time-consuming.

8.62 **Tax Services Offices have developed their own tools.** To try to overcome these problems, Tax Services Offices have developed new tools that collection officers are using. The tools are designed to reduce the time spent on repetitive tasks, develop electronic forms, and convert ACSES to a point-and-click system. Collection officers told us that the tools have indeed cut down the time they spend on repetitive tasks and have improved their efficiency. We note that the use of these tools is uneven across Tax Services Offices.

8.63 The new tools present a higher risk that data integrity will be compromised, because they are easily written, easily altered (deliberately or inadvertently), and not subject to the organizational development, maintenance, and control procedures that other applications usually undergo. Furthermore, they access many different applications that contain sensitive information on taxpayers. Headquarters is trying to understand the use of the new tools by building an inventory and developing controls. It recently approved some tools for use in collection activities. While we appreciate the efficiency improvements that the new tools bring, we are concerned about the risks involved and the length of time it has taken to develop controls.

Some steps have been taken to improve efficiency

8.64 In addition to setting up the national call centre and the national pools, the Agency has taken other steps to improve efficiency and incorporate good practices. These include the following:

- The Branch integrated the goods and services tax debt workload into its operational systems.
- The Branch has an electronic collection manual easily accessible by all collection officers. We heard positive comments from staff about the manual.
- The collection manual includes guidance on monitoring debtors' ability to pay. The guidance outlines when and how to determine both an individual's and a corporation's ability to pay.
- The Branch participates in the International Debt Management Committee of six countries' representatives who are responsible for debt management. The committee members compare approaches to debt management and share good practices.

- The Agency provides a wide variety of payment options for tax debtors. These include payment by cheque, post-dated cheque, or pre-authorized debit, and payment at financial institutions, on-line, or by telephone.

8.65 **Recommendation.** The Canada Revenue Agency should minimize the number of collectors who work on each account, record their collection actions in a more systematic way, and improve the case management tools they have at their disposal.

The Agency's response. The Agency agrees. The Agency will undertake an initiative to identify file management inefficiencies and improve the effectiveness of collector actions on case inventories.

The Agency will build on process improvements it has made, such as the national collections call centre and national pools, to further improve its file management. More specifically, the Integrated Revenue Collections project will improve the case management tools available to perform all Agency collection activities.

Future vision is ambitious

8.66 The Agency recently developed a strategic vision for the Revenue Collections Branch. The vision sets out ambitious goals to be achieved by 2010. It incorporates many good practices used or planned in other jurisdictions and in the private sector. For example, the vision calls for better management of tax debt risks, using a new technological platform.

8.67 The strategic vision includes five strategic directions:

- an integrated client-centred approach that will allow for a progressive integration of the Branch's workload so that all issues surrounding a particular debtor will be identified and dealt with by one Agency officer;
- a new technological platform that will allow the Agency to start using information strategically and improve the way it identifies, manages, and distributes workload;
- the pursuit of legislative amendments to address compliance and collection issues and to improve the framework under which the Agency and taxpayers operate;
- improved support for employees to help them adapt to a new work environment; and
- the creation of new strategic partnerships and the strengthening of existing ones, with a view to assuming additional collection responsibilities.

Vision extends 1994 concepts that have not been fully developed

8.68 In 1994 we noted that the Department intended to have the same collector follow up on unpaid assessments of the various kinds of taxes owed by a given taxpayer—a client-centred approach for collections. Since then the Agency has made some progress toward this approach, although difficulties with its computer systems have prevented it from fully achieving the goal. The Agency now plans to extend the concept of a client-centred approach to integrate both the collections and compliance workloads handled by the Branch—a significant challenge, since the collections workload itself is not yet fully integrated.

8.69 In 1994 we noted that the scoring of delinquent accounts by risk was ineffective and that profiles of tax debtors did not exist. The Department agreed that it needed to establish an appropriate system for risk scoring and to develop debtor profiles. Since then the Agency has updated the rudimentary risk scoring in its computer systems, but it still has no profiles of tax debtors. The Agency expects the new technological platform called for in the strategic vision to help it prioritize and allocate work based on assessed levels of risk. Since little of the information needed to do comprehensive risk assessments currently exists in a usable form, it will have to be assembled and incorporated into existing or new technology platforms before results can be achieved.

Implementing the vision will require detailed planning and diligent attention

8.70 The vision identifies the major challenges in collecting tax debts—namely, the consistent growth in the number of tax debts, the gap between "intake" (new assessments not paid and interest on old debt) and "production" (cash collected and amounts written off), and the aging of the debt portfolio. However, at the time of the audit, the Agency had not prepared detailed plans that set out how it will meet the challenges outlined in the strategic vision. Moreover, the Agency lacks the information it needs to create such a plan and measure progress toward it.

8.71 The Agency's slow progress on risk assessment and workload management since 1994 can be explained in part by technology problems and the slow development of technology solutions. But much of the strategic vision hinges on significant investments in a new technology platform, and these investments need to be carefully managed.

Progress in addressing our 1994 recommendations on collecting income tax debts

Recommendation	Progress
1994 Report of the Auditor General, Chapter 29	
The Department should establish an appropriate system for risk scoring of delinquent debts, develop debtor profiles and customize collection procedures as required (paragraph 29.64).	○
The Department should introduce procedures for collecting on all large debts soon after they become due (paragraph 29.75).	●
The Department should monitor the number of danger-of-loss cases referred to legal counsel by collectors, the number presented to courts and the extent to which favourable judgments are granted, and should assess the extent to which legislative provisions are sufficient to shelter the Crown from potential loss (paragraph 29.75).	○
The Department should establish clear standards for assessing, documenting and verifying information pertaining to debtors' ability to pay, together with expected time frames for making and updating such assessments. The Department should monitor collectors' adherence to such standards (paragraph 29.80).	●
The Department should clearly define standards of performance at the collector level and institute procedures to monitor collectors' adherence to such standards. Performance standards would include such things as nature and frequency of debtor contacts, time frames for resolving accounts, and use of legal action and other methods to collect amounts outstanding (paragraph 29.85).	○
The Department should assess the feasibility of using standard codes as a means of identifying and aggregating collection action taken by collectors in a timely, summarized manner and capturing results associated with those actions (paragraph 29.91).	○
Actual dollars collected and dollars written off should be tracked separately for individual collectors and teams and taken into account when assessing collectors' performance (paragraph 29.91)	●
The Department should monitor time spent by collectors in both cash-generating and non-cash-generating activities (paragraph 29.91).	○
The Department should conduct an annual review of all of its accounts and write off amounts that are deemed uncollectible. In estimating the realizable portion of tax debts remaining in inventory, the Department should consider the age of unpaid assessments, as well as remissions and other adjustments that can reduce the balance of reported amounts outstanding (paragraph 29.106).	●

● **Satisfactory**—Progress is satisfactory, given the significance and complexity of the issue, and the time that has elapsed since the recommendation was made.

○ **Unsatisfactory**—Progress is unsatisfactory, given the significance and complexity of the issue, and the time that has elapsed since the recommendation was made.

8.72 For example, the Agency is working on the Integrated Revenue Collections (IRC) project. The project was initiated in 2001, and by March 2005 the Agency had spent $13 million on it. However, no comprehensive business case was prepared and certain fundamentals of project management were missed. Since September 2005, the Branch has taken important steps to control the project, including establishing a project management office and preparing detailed planning documents. By March 2006, the Agency will have spent about $30 million, almost 40 percent of the estimated total cost of the project. It has received some deliverables, such as the first release of All Revenue Tables, and has many others in progress. We note that some parts of the project were falling behind the schedule that was developed in January 2005. The Agency will need to be diligent in the months ahead if the project is to be delivered on time, on budget, and with the expected deliverables.

Conclusion

8.73 While the Agency has made improvements in the collection of tax debts since our 1994 audit, the tax debt continues to grow at a faster rate than total taxes paid, and aging accounts are a problem. We found that the Agency's approach to assessing tax debts for risk continues to have major weaknesses that impede their timely and efficient collection. We also found that the Agency has taken some steps to handle tax debts efficiently, but much more needs to be done. Management lacks the information it needs to understand the makeup of the tax debt and to develop strategies and allocate resources in a way that would significantly improve the situation. It also lacks the information it needs to determine whether it is using efficient and timely processes to collect tax debts.

8.74 The Agency has known for many years what it needs to do to improve the collection of tax debt, but it has had difficulty achieving significant breakthroughs. It now has a strategic vision that sets a course for the future. The major challenge for the Agency is to turn that vision into reality through detailed planning, focussed management attention, and measurement of results.

About the Audit

Objective

The objective of our audit was to examine whether the Canada Revenue Agency uses efficient and timely processes to collect tax debts.

Scope and approach

We examined the collection of tax debts in four of the Agency's revenue lines—personal tax, corporate tax, goods and services tax, and payroll source deductions—that together constitute about 86 percent of all tax debts. We interviewed staff, reviewed files and management reports, and analyzed data.

From the four revenue lines in our audit scope, we selected for audit a sample of 151 tax debts that were active at 31 March 2005. The sample included

- 72 personal tax debts,
- 32 corporate tax debts,
- 26 goods and services tax debts, and
- 21 payroll deduction debts.

Within each revenue line, more high-value tax debts were audited than low-value tax debts. A total of 110 high-value tax debts were examined, accounting for about one percent of the value of the total tax debt of the revenue lines that we audited. All files were selected in a random and unbiased fashion from the tax debts of the four Tax Services Offices that were visited during the examination phase of the audit. Tax Services Offices have policies and guidelines that require the handling of tax debts in a uniform manner. All sample items were given an equal weight when results were calculated.

We also considered whether the Agency has made satisfactory progress on the issues that we reported in 1994 and that Revenue Canada also reflected in its 1995 action plan to the House of Commons Standing Committee on Public Accounts.

We examined good practices in the collections operations of ten organizations. They included two federal revenue agencies, two Canadian provincial revenue ministries, four United States state revenue agencies, and two private sector financial service firms.

In addition to discussions with the Agency at its national headquarters in Ottawa, we visited Tax Services Offices in Vancouver, Calgary, Winnipeg, Toronto Centre and Toronto North, Ottawa, Montreal, and Halifax. We visited the national pool in Toronto North and the national collections call centre in Ottawa. We also visited a credit bureau and the collection department of a large private sector company.

We did not examine debts in which the taxpayer was disputing the assessment that gave rise to the debt because, in most such cases, law prevents the Agency from taking any legal collection action. We did not examine miscellaneous tax debts, which include non-residents' taxes, other levies, excise fees, and customs fees. We did not audit the accounts that the Agency collects on behalf of Human Resources and Social

Development Canada, as this collection activity started during our audit. We did not examine goods and services tax debts in Quebec as they are collected by the Ministère de Revenue de Quebec.

We did not examine write-offs or follow up on recommendations regarding the fairness provisions, given that we had done an audit reported in April 2002, Chapter 2, Canada Customs and Revenue Agency—Tax Administration: Write-Offs and Forgiveness.

Criteria

In order to demonstrate that the Agency was efficient and had timely processes to collect tax debts, the Taxpayer Services and Debt Management Branch should

- have an overall collection strategy with clear goals and objectives;
- have specific strategies to deal with identified problems such as insolvencies;
- measure progress in meeting the goals and objectives of the strategies;
- have a good understanding of the composition of tax debts, including reasons for growth or reduction in the balance;
- base collection of tax debts on appropriate risk models;
- have appropriate procedures to resolve tax debts on a timely basis;
- have a method in place to learn about and incorporate good debt collection practices;
- have appropriate information technology systems to support the collections process; and
- provide collection officers and managers with appropriate guidance to undertake collections activities.

Audit work completed

Audit work for this chapter was substantially completed on 20 December 2005.

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Appendix List of recommendations

The following is a list of recommendations found in Chapter 8. The number in front of the recommendation indicates the paragraph where it appears in the chapter. The numbers in parentheses indicate the paragraphs where the topic is discussed.

Recommendation	Department's response
The tax debt continues to grow	
8.28 The Canada Revenue Agency should identify and collect the data it needs to analyze the makeup of its tax debt and to develop better collection strategies. **(8.18–8.27)**	The Agency agrees that understanding the makeup of tax debt is an important factor in developing its strategies, although the Agency's efforts have resulted in increased collector productivity since 1994. In addition, the Agency has exceeded important program delivery commitments made to the Treasury Board, as noted in this chapter. The Agency has taken important steps to increase its capacity in the area of tax debt research by launching the Agency's Integrated Revenue Collections (IRC) project, which is developing advanced data-warehousing and data-mining capabilities. In addition, the Agency has set up a team within its organization dedicated to conducting debt management research. These initiatives will support the horizontal approach to compliance research across the Agency. The Agency is taking important steps to ensure that the IRC project is being managed in accordance with accepted project management practices. Some deliverables have already been released, such as the All Revenue Tables.
Management lacks important information on performance	
8.41 The Canada Revenue Agency should significantly improve its management information to make it complete and comprehensive. It should develop reliable techniques and information sources to determine on a regular basis the results of its collection efforts and use that information to guide its decision making for each of its major collection modes and actions. **(8.29–8.40)**	The Agency agrees that improvements are needed to enhance its management information systems—improvements that are currently being addressed through its Integrated Revenue Collections project. However, the Agency believes that the performance indicators it has established for its collections program appropriately reflect program activities, including write-offs. The Agency continues to review its performance indicators in order to ensure their accuracy and appropriateness. This review is in line with the OAG's annual performance assessment on the fairness and reliability of the program information described in the Agency's Annual Report to Parliament.

Recommendation	Department's response
	The Agency continues to manage uncollectible accounts in accordance with the procedures that were favourably reviewed by the Auditor General in 2002.
Risk management is deficient	
8.52 The Canada Revenue Agency should establish a more comprehensive automated risk-scoring system for tax debts, update the risk scores on an ongoing basis, and use the risk scores to prioritize workload throughout the collections process. **(8.42–8.51)**	The Agency agrees. Additional investments in risk management systems are needed, and are being made, to realize the full potential of the Agency's collections program and to address the continued growth in accounts receivable. The Agency's Integrated Revenue Collections project is focussed on addressing both past and current concerns raised by the Auditor General with respect to risk assessment and file management, in addition to the above-mentioned management information system improvements.
Efficiency improvements needed	
8.65 The Canada Revenue Agency should minimize the number of collectors who work on each account, record their collection actions in a more systematic way, and improve the case management tools they have at their disposal. **(8.53–8.64)**	The Agency agrees. The Agency will undertake an initiative to identify file management inefficiencies and improve the effectiveness of collector actions on case inventories. The Agency will build on process improvements it has made, such as the national collections call centre and national pools, to further improve its file management. More specifically, the Integrated Revenue Collections project will improve the case management tools available to perform all Agency collection activities.