CHAPTER 3

Status Report on Collecting Tax Debts—Canada Revenue Agency

Performance audit reports

This report presents the results of a performance audit conducted by the Office of the Auditor General of Canada under the authority of the *Auditor General Act*.

A performance audit is an independent, objective, and systematic assessment of how well government is managing its activities, responsibilities, and resources. Audit topics are selected based on their significance. While the Office may comment on policy implementation in a performance audit, it does not comment on the merits of a policy.

Performance audits are planned, performed, and reported in accordance with professional auditing standards and Office policies. They are conducted by qualified auditors who

- establish audit objectives and criteria for the assessment of performance,
- gather the evidence necessary to assess performance against the criteria,
- report both positive and negative findings,
- conclude against the established audit objectives, and
- make recommendations for improvement when there are significant differences between criteria and assessed performance.

Performance audits contribute to a public service that is ethical and effective and a government that is accountable to Parliament and Canadians.

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Status Report on Collecting Tax Debts—Canada Revenue Agency

Main Points

What we examined

The level of tax debt is driven by the economic climate, tax policy, and taxpayer behaviour, as well as by the Canada Revenue Agency's efforts to assess and collect taxes in a timely manner. In Canada, the vast majority of taxes are paid to the Agency on time, without intervention. However, a balance of unpaid taxes and payroll deductions remains, growing over the years. The outstanding balance in undisputed unpaid taxes was $29 billion at 31 March 2012. Each year, the Agency writes off a certain amount of debt that it considers uncollectible. In 2011–12, it wrote off $2.8 billion.

In 2011–12 the Agency had a budget of $242.6 million to collect tax debt, with some 4,000 full-time equivalent staff—mainly collection officers, team leaders, and managers—in tax services offices across Canada and at the national Debt Management Call Centre.

In 2006, we reported that the Agency had not made satisfactory progress on recommendations from our 1994 audit related to tax debts. We said that risk assessment lacked sophistication. Further, the Agency lacked information such as performance measures and strategies, fundamental to assist with managing tax collection.

Our current audit examined how the Agency implemented its action plan to address the recommendations we made in 2006 on the more important weaknesses we had identified. Where the plan varied from our recommendations or the Agency had modified its action plan, we considered whether the actions taken addressed our original underlying observations.

Audit work for this chapter was completed on 23 November 2012. Details on the conduct of the audit are provided in **About the Audit** at the end of the chapter.

Why it's important

The mission of the Canada Revenue Agency is to administer tax, benefits, and related programs and to ensure taxpayer compliance, on behalf of governments across Canada. As Canada's tax administrator, in addition to protecting Canada's revenue base, one of the Agency's primary goals is compliance—ensuring that taxpayers meet their obligations. Under the *Canada Revenue Agency Act*, the Agency is responsible for enforcing the *Income Tax Act* and the *Excise Tax Act*.

The timely collection of overdue accounts is the final element in taxpayer compliance. If taxpayers are not convinced that the Agency will take action to collect taxes owing, compliance will decline. A decline in compliance would affect the country's revenue base.

What we found

- Overall, the Agency has made satisfactory progress on the issues raised in our 2006 audit. It has introduced many new tools to improve the way collectors manage accounts. Under a new national approach, collectors can work on accounts from anywhere in the country, so work can be assigned where collectors are available instead of being delayed by bottlenecks in the busier offices.
- The Agency has taken timely collection action on more than 85 percent of files over $1 million, exceeding its target. However, its target is the same regardless of the size of the account. We note that it may be appropriate to set a higher target for collection action for larger files.
- While the Agency has developed several new models to assess outstanding accounts of individuals for risks to the collection of income tax debts, it did so without first evaluating the effectiveness of its existing methods. It has also delayed the completion of work to improve how it assesses collection risks related to business accounts.
- The Agency has identified and collected the information it needs to analyze the makeup of the tax debt. For example, it can now break down the debt by tax, interest, and penalties and by revenue stream, such as GST or payroll deductions. The tax debt has increased from $18 billion to $29 billion since 2006. The Agency is working to refine and improve its tools and strategies and to encourage taxpayer compliance.
- The Agency has significantly more comprehensive and complete management information than we reported in 2006. However, it has yet to finish developing additional performance measures to show the extent to which it is meeting its program objectives.

The Agency has responded. The Agency agrees with all of the recommendations. Its detailed responses follow the recommendations throughout the chapter.

Introduction

3.1 The mission of the Canada Revenue Agency is to administer tax, benefits, and related programs and to ensure taxpayer compliance, on behalf of governments across Canada. One of the Agency's primary goals is to ensure that taxpayers meet their obligations, while protecting Canada's revenue base. Under the *Canada Revenue Agency Act*, the Agency is responsible for enforcing the *Income Tax Act* and the *Excise Tax Act*.

3.2 In addition to collecting federal income taxes, Employment Insurance premiums, and Canada Pension Plan contributions, the Agency has agreements with all provinces, except Quebec, to collect provincial income taxes on their behalf. In Quebec, le ministère du revenu du Québec collects the goods and services tax (GST) for the Agency. The federal government pays each province the total amount assessed for its provincial income taxes and takes on the risks associated with collecting any outstanding amounts. The federal government earns any interest and penalties collected, but it also incurs the loss if the debt is written off.

3.3 The level of tax debt is driven by the economic climate, tax policy, taxpayer behaviour, and the Agency's efforts to collect taxes in a timely manner. In Canada, 94 percent of individuals and 90 percent of corporations pay their taxes to the Agency on time and without intervention. However, even though most taxpayers pay what they owe on time, there is always a balance of unpaid taxes and payroll deductions that accumulates over the years. By 31 March 2012, $29 billion in **undisputed taxes**, interest, and penalties was outstanding.

Undisputed taxes—The amount of tax that the taxpayer has not appealed. Once an appeal has been filed, the Agency cannot take collection action on the account, except under some special circumstances. In this chapter, reference to the tax debt means undisputed taxes, unless we specify otherwise.

3.4 The Agency employs about 4,000 full-time equivalent staff to collect tax debt—mainly collection officers, team leaders, and managers—at its headquarters, in tax services offices across Canada, and at the national Debt Management Call Centre. In the 2011–12 fiscal year, the Agency's budget for collecting tax debt was $242.6 million. There are additional staff at the Agency's headquarters who do research for a number of program areas, including collections.

3.5 Timely collection of overdue accounts is important, because it is the final element in taxpayer compliance. If taxpayers do not believe the government will collect overdue taxes, they may be less motivated to pay. Not paying debts will have a negative effect on Canada's revenue base over time.

Garnish—The action by Canada Revenue Agency of intercepting funds payable to the taxpayer by a third party, such as wages or other income sources. Usually, once a garnishment action is started, it will not be withdrawn, unless the taxpayer pays the full balance or provides evidence that the action causes undue financial hardship.

3.6 Unlike private businesses, the Agency does not choose its clients based on their credit-worthiness. It cannot charge higher interest rates or refuse to extend credit based on a poor credit rating. However, the Agency does have legislative abilities that private organizations do not have, such as the ability to **garnish** a debtor's source of income to collect taxes owing, without a court order.

Key findings in 2006

3.7 Our 2006 audit (2006 May Status Report of the Auditor General of Canada, Chapter 8, Canada Revenue Agency—Collection of Tax Debts) followed up on our 1994 audit (1994 Report of the Auditor General of Canada, Chapter 29, Revenue Canada—Collecting Income Tax Debts). In 2006, we concluded that the Agency had not made overall satisfactory progress against our earlier recommendations. Risk assessment of debtors lacked sophistication, and fundamental information for managing tax collection (such as performance measures and strategies) was missing. The Agency did not know the makeup of the tax debt, so it could not tailor its collection strategies accordingly. Its case management tools also needed improvement.

Events since our 2006 audit

3.8 Global financial turmoil has affected Canada's economy since our last audit. The economy in the United States has still not fully recovered, and the European economy remains under stress. In Canada, many economic indicators have deteriorated because of the economic slowdown. Between 2007 and 2011, the real gross domestic product (GDP) increased by less than 3.5 percent. The current unemployment rate of more than 7 percent is higher than in 2007. With an economy that has not fully recovered, tax collection can be challenging. Canada needs an effective tax collection program to protect its tax base and its revenues.

3.9 The amount of revenue that the Agency is responsible for has increased, in part, because it now administers the following additional types of taxes:

- In 2009, the Agency began administering Ontario Corporate Tax.
- In 2010, the Agency began collecting harmonized sales tax (HST) for British Columbia and Ontario. (It will continue to collect HST for British Columbia until 1 April 2013).

3.10 In the 2011 Status Report of the Auditor General of Canada, Chapter 2, Large Information Technology Projects, we followed up on our 2006 recommendations on the Agency's Integrated Revenue Collections (IRC) project. The Agency initiated the IRC project to help prioritize and allocate collections work according to level of risk. It had planned to spend $144 million on the project by 2010.

3.11 In 2011, we found that the Agency's overall progress against our recommendations was satisfactory for governance, organizational capacity, and project risk management. The Agency had completed a benefits measurement plan, with benefits attributable to Phase I of the project. It had initially lacked details on when benefits would be achieved; however, in 2010, the plan was refined and approved. The 2011 audit did not assess whether the technology project functioned as intended. Our current audit does not follow up on our 2011 audit; however, it does include some observations related to the IRC project.

Focus of the audit

3.12 The objective of our audit was to determine whether the Canada Revenue Agency has made satisfactory progress in implementing the significant recommendations made in the 2006 May Status Report of the Auditor General of Canada, Chapter 8, Canada Revenue Agency—Collection of Tax Debts.

3.13 We looked at how the Agency implemented its action plan to address our recommendations. When the plan varied from our recommendations, or when the Agency modified its action plan, we considered whether the actions taken addressed our original underlying observations. We focused on the more important weaknesses identified in our 2006 report. We note that the Canada Revenue Agency is a large organization, and it takes time to implement significant changes.

3.14 More details about the audit objectives, scope, approach, and criteria are in **About the Audit** at the end of this chapter.

Observations and Recommendations

3.15 When a tax debt arises, the Agency uses its account management tools to start working on the account. It does risk assessment on the debt to decide how and when to intervene. It then uses a variety of collection strategies, depending on the nature of the debt. Finally, the Agency gathers and reports on its results for both management decision making and for the public. Exhibit 3.1 is a simplified presentation of the Agency's collection process.

3.16 In most cases, the Agency starts collection action soon after the debt arises; for example, by issuing a letter to remind taxpayers to pay their debt owing. However, under the *Income Tax Act*, the Agency is restricted in the types of collection action it can take within the first 90 days.

3.17 During that first 90-day period, there are certain actions that the Agency may take, under specific circumstances. Large accounts are subject to a **danger of loss review**, to see if the taxpayer intends to dispose of assets instead of paying the debt. In such cases, the Agency may use a **jeopardy order** to take action immediately. For payroll deductions and debts associated with the goods and services tax or harmonized sales tax (GST/HST), there are no collection restrictions.

Danger of loss review—A review conducted to determine whether the collection of an outstanding debt would be jeopardized by a delay. For example, the debtor may begin to liquidate assets. If there is a danger of loss, then a jeopardy order may be initiated.

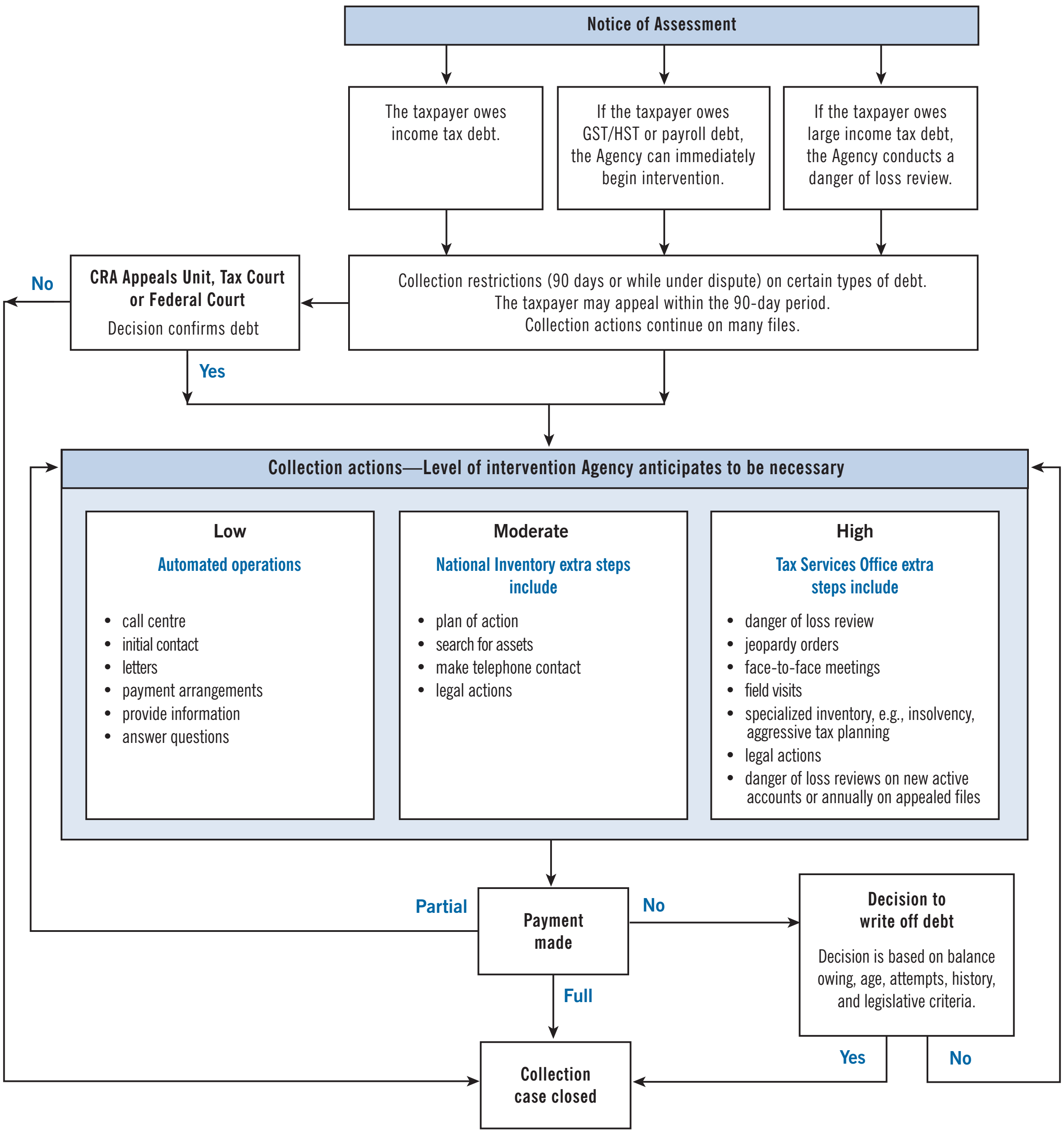
Jeopardy order—An order that allows the Agency to begin collection action immediately, without waiting for 90 days or for an appeal to be settled. The Minister must apply to the Federal Court or a provincial superior court for a jeopardy order, for authorization to take action.

3.18 A first risk assessment determines the level of Agency intervention that is needed: low, moderate, or high (Exhibit 3.1). Examples of interventions include

- sending the taxpayer a reminder letter to pay their outstanding debt,
- having a call centre agent contact the taxpayer, and
- proceeding with more progressive collection actions in the National Inventory (a new approach to inventory that allows accounts to be worked on in any geographic location by available collectors).

3.19 A second risk assessment prioritizes and assigns accounts within the National Inventory. Some accounts remain unassigned based on their risk ranking; they may be assigned to a collector later, when higher priority accounts have been resolved. Accounts that are more complex or difficult to resolve may be routed to senior collections officers for higher-level enforcement action.

Exhibit 3.1 Agency process for the collection of tax debts (simplified version of process)



Account management

3.20 Once Canada Revenue Agency collectors begin work on collecting the debt, they decide when and how to take action on an account and how to focus their activities. There are established practices and procedures to follow.

3.21 In 2006, we recommended that the Agency improve its account management, because we found that action on accounts was not timely, and that accounts were aging (outstanding for a long time). We also found that the collections case management system was difficult to use and did not provide collectors with necessary information.

3.22 The Agency's original action plan, in response to this recommendation, included system changes to improve account management, with components allowing collectors to get an integrated view, as part of the Integrated Revenue Collections (IRC) project described in paragraphs 3.10 and 3.11.

The Agency has addressed many weaknesses in account management

3.23 Based on the Agency's action plan to address our 2006 recommendation, we examined how the Agency implemented actions to improve its account management. The Agency has improved how it distributes accounts to collectors. Accounts that do not require face-to-face action may be assigned to a collector in any geographic location. For example, the Agency may assign the account for a company in Toronto to a collector in Halifax, rather than waiting for a Toronto collector to be available. This new national approach to managing the inventory of accounts allows for a more efficient use of staff and earlier attention to accounts. The Agency also introduced a new national intranet site, so collectors can access required information for any province.

3.24 In addition, some collectors now specialize in certain types of accounts, for example, bankruptcies. Specialization should allow for more effective collection, because the collector would have more knowledge of and experience with a particular type of debtor.

3.25 In 2010, the Agency introduced an interim computer application to gather and summarize information from a multitude of computer systems, to reduce the need for time-consuming, repetitive actions by the collectors. It was introduced because the implementation dates for the IRC case management system were revised.

3.26 The Agency has automated systems that calculate risk to determine how to prioritize an account. Less complex accounts may receive a reminder letter, while more complex accounts are assigned to a collector. If an account is assigned to a collector, the new application shows any other associated accounts. For example, if a business owes money for payroll remittances, corporate tax, and goods and services tax (GST), when the GST account is assigned to a collector, the application automatically shows all three accounts.

3.27 We are satisfied with the actions taken to improve account management for the collection of tax debts (Exhibit 3.2). The Agency has introduced many new tools, such as the account summary application and the intranet site. It also improved how workload is handled with the National Inventory, and it now allows collectors to specialize. The Agency collected more of the tax debt that went into the collections process in 2012 than in 2006. In 2006, it collected $21.5 billion of its tax debt accounts, and in 2012 it collected $40 billion, yet the number of full-time equivalent staff has not increased compared to 2006.

Exhibit 3.2 Progress in addressing our recommendation on account management

Recommendation	Progress
The Canada Revenue Agency should improve the account management tools the collectors have at their disposal. (Based on Recommendation 8.65 of the 2006 May Status Report of the Auditor General of Canada, Chapter 8 Canada Revenue Agency—Collection of Tax Debts)	**Satisfactory**

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.

The Agency is not meeting its targets for danger of loss reviews on accounts over $10 million

3.28 The Agency has specific policies and procedures, as well as quality assurance standards, for handling large accounts. We looked at all accounts over $10 million, whose total value as of 31 March 2011 was $1.8 billion. We also chose a representative sample of 128 accounts from the accounts that were between $1 million and $10 million and that were in collection as of 31 March 2011. The total value of these accounts was $1.9 billion.

3.29 For all the accounts we looked at, we reviewed whether the Agency was acting to collect the debt in a timely manner. The Agency's target is for 85 percent of the accounts to receive timely action. The Agency defines timely action as action or follow-up without extended delays, unless there is a concrete reason. Whether action is timely depends on the dollar value, known risk, and priorities of other accounts.

3.30 We found that the Agency exceeded its target of taking action in a timely manner. However, the Agency's target for taking timely action is the same regardless of the size of the account. We question whether the Agency has set its target appropriately; for larger accounts we would have expected the Agency to have higher targets as the size of the debt increases.

3.31 For all accounts over $10 million, we also reviewed additional Agency criteria, including whether the collector

- completed a danger of loss review; and
- developed an action plan, regardless of the danger of loss decision.

3.32 When we reviewed the additional criteria for accounts over $10 million, we found that the Agency did not meet its targets for danger of loss reviews; they were either missing or not adequately documented in 17 of the 39 accounts that required them. A danger of loss review is important, since it will allow the Agency to act quickly where the taxpayer may be disposing of assets instead of paying a tax debt.

3.33 **Recommendation.** The Canada Revenue Agency should follow its procedures for danger of loss reviews on large files. In addition, it should evaluate whether having one target for taking timely action for all accounts, regardless of size, is appropriate.

The Agency's response. Agreed. As noted in the report, the Agency does take action on a timely basis so that any risk of loss is clearly identified on all large files, and its quality control results exceed expectations in this area. The Agency will, however, ensure that the documentation on this small number of files reflects these actions in the most comprehensive manner possible. In addition, by April 2014 the Agency will undertake a review of its targets for danger of loss reviews on large accounts to determine their appropriateness.

Risk assessment

3.34 As mentioned previously, the Canada Revenue Agency can apply more than one risk assessment to a tax debtor account. The first assessment is based on information that exists at the beginning of the process, including past compliance, sources of income, associated accounts, and dollar amount. The Agency uses this information to determine the most effective and efficient approach to collect the tax debt. While new debt is considered to be easier to collect than older debt, there are other factors that contribute to the risk score assigned to the account. For example, after a debt has been added to the Agency's inventory of tax debts, the risk may change if new events, such as bankruptcy, occur.

3.35 In 2006, we observed weaknesses relating to the Agency's risk assessments. For example, we noted that initial risk assessments were not being updated to reflect changes in taxpayer information and risk factors and that workloads were not being prioritized based on risk.

3.36 The Agency agreed with our observations, and indicated that its Integrated Revenue Collections (IRC) project would address these concerns. Its action plan included establishing processes to use new risk assessment tools and to build and implement risk models and new risk scores.

3.37 To determine whether the Agency improved its risk scoring of tax debts, we examined whether it

- assessed the criteria used for determining the risk;
- established a new comprehensive, automated risk scoring process; and
- updated the risk scoring process on an ongoing basis.

3.38 We also reviewed and analyzed IRC project documentation and compared the progress made to the expected results in the Agency action plan. We considered whether the Agency had reviewed internal or external research to help identify factors that influence risk for accounts receivable.

The Agency has updated individual debtor risk scores but has delayed updating business debtor risk scores

3.39 After our 2006 audit, the Agency made a commitment to improve its risk scoring process for personal and business risk scores. Its original action plan included developing, testing, and implementing individual debtor risk scores by 2009 and business debtor risk scores by 2011. In the 2006–07 Annual Report to Parliament, the Agency indicated that it had decided to defer work on business debtors (corporations) after it was found to be cost prohibitive. Because of this decision, we focused on whether the Agency tested the effectiveness of its risk scoring systems for individual debtors, and whether it made improvements.

3.40 The Agency has developed five risk scoring models for personal income tax debtors. Two models have been tested and are in full use, and another model is used on an ad hoc basis. A fourth model is under evaluation, and a fifth was developed to supplement the Agency's primary risk score for automated processes. This model has been tested and is being used on an experimental basis, with the goal of developing improved compliance strategies.

3.41 In its efforts to improve the collections process, the Agency obtained external data from a credit bureau. It intended to combine this data with internally held data on taxpayers to predict the result of collection actions and improve decision making. For example, the Agency could predict whether a danger of loss review would conclude that an account is in jeopardy. The value of using this third-party data has been inconclusive, and research with this type of data is ongoing.

3.42 We noted that the Agency developed new risk scoring models before evaluating the effectiveness of its pre-existing risk scores. The Agency has evaluated the effectiveness of the new models that it implemented. However, we found that it has only recently completed some of the work needed to determine the effectiveness of one of the two pre-existing risk scores. If the Agency does not complete the evaluation of the existing risk scores, it will not know if they need changes, and so may not be identifying the taxpayers that it should pursue first.

3.43 Since our 2006 audit, the Agency has not made sufficient progress in improving its risk scoring processes for the collection of tax debts (Exhibit 3.3). Planned work on risk scores for personal tax debts is under way. The deadline for implementing the changes to business accounts for the goods and services tax (GST) and harmonized sales tax (HST) was revised from 2011 to 2013. The work originally planned for risk scoring for corporations was determined to be cost prohibitive, so the Agency deferred it.

3.44 Risk scoring is important, because it guides decision making for important steps in the collection process. We identified weaknesses in risk scoring in 1994 and again in 2006. While the new data models that the Agency has developed are promising, the overall lack of timely progress is a concern.

Exhibit 3.3 Progress in addressing our recommendation on risk scoring

Recommendation	Progress
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. (Recommendation 8.52 of the 2006 May Status Report of the Auditor General of Canada, Chapter 8, Canada Revenue Agency—Collection of Tax Debts)	**Unsatisfactory**

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.

Collection strategies

3.45 In 2006, we found that management at the Canada Revenue Agency lacked information on why the tax debt was growing. The Agency also had a poor understanding of the makeup of the tax debt. This information was needed in order to develop better collection strategies.

3.46 To assess whether the Agency had improved its performance in this area, we reviewed and analyzed action plans, research, and other Agency reports. We also examined whether the Agency was meeting its planned timelines to complete its research.

The Agency has collected much of the data it needs to understand the tax debt better

3.47 We found that the Agency has improved its data collection to better understand the makeup of the tax debt. The Agency can now break tax debt information down in different ways, such as by

- tax, interest, and penalties;
- year; and
- revenue stream (GST, HST, payroll deductions, individuals, and corporations).

3.48 Exhibit 3.4 shows the amount of undisputed tax debt at the end of each fiscal year for the past seven years, as well as the amount of tax debt written off in each year. As of 31 March 2012, there was also about $11 billion in disputed tax debt on which the Agency will not be able to take action until the appeals are settled. Although the amount of undisputed tax debt has grown (from $18 billion in 2006 to

$29 billion in 2012), the amount of net revenue collected by the Agency has also increased. The growth in the total undisputed tax debt since 2006 is 57 percent, and the growth in revenue is 29 percent.

Exhibit 3.4 Agency indicators (in billions of dollars) for the last seven fiscal years

Fiscal year (1 April to 31 March)	2005–06	2006–07	2007–08	2008–09	2009–10	2010–11	2011–12
Net revenue	258	279	293	287	279	311	332
Undisputed tax debt at end of fiscal year	18.5	20.0	23.2	24.4	25.0	27.4	29
Tax debt written off	1.9	1.8	1.8	2.5	2.4	2.4	2.8

3.49 The Agency has broken the growth down by revenue stream and has provided some analysis on the reasons for the growth of the tax debt.

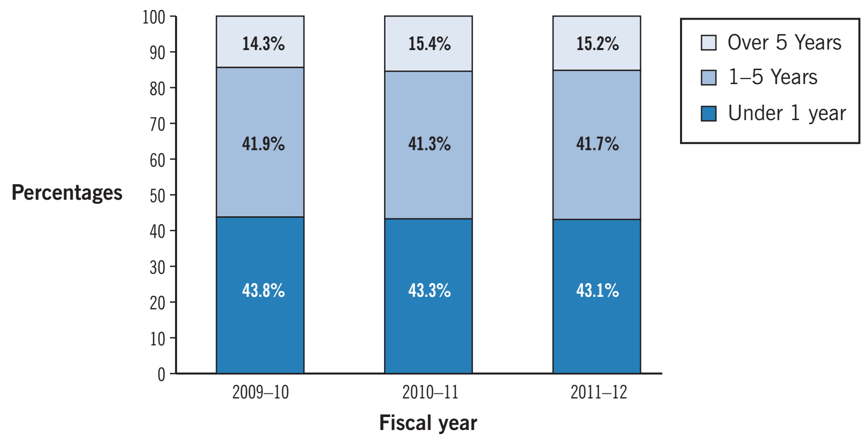
3.50 The Agency explains that the increase in tax debt is, in part, due to many factors, such as

- government tax policies, resulting in increased tax revenues;
- an increase in the number of tax debtors;
- increases in rates of personal and corporate bankruptcies since the 2008 economic downturn;
- more reassessments for aggressive tax planning and transfer pricing; and
- interest charged on unpaid debt that continues to accumulate.

3.51 Exhibit 3.5 shows the tax debt broken down by age (the length of time it has been outstanding). Agency analysis indicates that the older the debt, the more difficult and expensive it is to collect, since a taxpayer is less likely to have kept funds on hand to pay taxes owing. Debts more than five years old are being identified by collectors due to potential new collectability limitations as discussed in paragraph 3.61.

3.52 The Agency has identified and collected the data it needs to analyze the makeup of the tax debt. It has gathered information through debt management and risk management research, and it has increased its research capacity through the Integrated Revenue Collections (IRC) project. Despite this progress, tax debt continues to grow, and so the Agency must continue to improve and refine its tools and strategies to deal with it. Nevertheless, we found progress in this area to be satisfactory (Exhibit 3.6 in the following section).

Exhibit 3.5 Age of the tax debt



The Agency has done much research into the makeup of the tax debt

3.53 In addition, the Agency conducted research in a variety of areas, such as

- how the debt arose and the associated debtor characteristics (for example, initial assessment, reassessment);
- what specific research was conducted on industries that were perceived to be high risk; and
- what impact the economic indicators had on new tax debt.

3.54 We reviewed the documentation on research done since 2006 on the makeup of the tax debt. We found that the Agency met most of its initial deadlines for conducting research. We noted that changes were made to the original plan but that the reasons for those changes were well supported. In one case, the Agency had planned to conduct research on individual tax debtors, to improve its capacity to analyze such cases. The research was more costly and time consuming to conduct than originally anticipated, so the Agency reduced the scope and focused on the components that would yield the most business value.

3.55 The Agency's research on collections is extensive and ranges from narrow tactical analyses, to improve risk scores, to high-level strategic research, to establish an overall picture of the tax debt. The Agency researchers made recommendations in many of the research studies. We therefore found progress in this area to be satisfactory (Exhibit 3.6).

3.56 We observed that many changes relating to this research have been implemented. Examples include

- changing the thresholds for minor balances, below which the Agency takes limited action; and
- creating strategies to allow certain types of accounts to self-resolve.

3.57 Changes have not always been directly linked to the actual recommendations. Some Agency recommendations from the research have not been followed up. One example is the recommendation to tailor debt management strategies to counter differences in taxpayer behaviour. It is taking the Agency a long time to implement some of its recommendations; for example, some from 2008 are not scheduled to be addressed until 2014.

3.58 A comprehensive research plan that reports on the status of all recommendations would allow the Agency to keep track of its progress and document the reasons why it would or would not implement a recommendation.

3.59 We found that the Agency has conducted valuable research, and made some important changes, but it has not followed up on or addressed all of its strategic recommendations. It was difficult to know what was still outstanding, since there was no way to track its progress. Following up and tracking progress would help the Agency to be more efficient with its resources.

Exhibit 3.6 Progress in addressing our recommendation on data collection

Recommendation	Progress
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. (Recommendation 8.28 of the 2006 May Status Report of the Auditor General of Canada, Chapter 8, Canada Revenue Agency—Collection of Tax Debts)	**Satisfactory**

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.

3.60 **Recommendation.** The Canada Revenue Agency should develop a methodology to track and monitor its recommendations from its research to ensure that they are all followed up.

The Agency's response. Agreed. As noted in this report, the Agency has implemented many changes originating from the research it conducted. Further, the Office of the Auditor General observed that the Agency's research is extensive, ranging from tactical analyses, to improved risk scores, to high-level strategic research. The Agency recognizes that there are opportunities to improve how the relevant findings of this research are incorporated into its program planning and reporting processes. By April 2014, the Agency will develop and implement a formal process to achieve this goal.

The Agency is preparing for new time limitations on collecting tax debts

3.61 In addition to following up on our 2006 audit, we looked at a new development that may affect future collections and that is related to the makeup of the tax debt. In 2003, the Supreme Court of Canada, in *Markevich v. The Queen*, decided that a six-year limitation period applied to prevent the Agency from collecting old tax debts.

3.62 Following this decision, Parliament amended section 222 of the *Income Tax Act* and section 313 of the *Excise Tax Act*. As a result of the amendment, the Agency can collect a federal tax debt for 10 years after it is assessed. Therefore, all federal tax debts outstanding on 4 March 2004 may not be collectible after 4 March 2014, although the limitation period may be extended under certain circumstances. For new tax debts, the Agency can collect for 10 years after the assessment is made, again unless extended under certain circumstances.

3.63 To determine what the Agency has done to prepare for this upcoming deadline, we asked for the following information:

- the number of accounts at risk,
- action plans in place,
- whether risk scoring had been revised, and
- overall management information to guide actions and decisions.

3.64 The Agency provided us with an overview of the steps it has taken with respect to the upcoming deadline. It is developing an automated system to identify accounts that are subject to the collection limitation period and to ensure that the Agency is complying with the legislative requirements. However, the Agency has stated that it is highly unlikely that the necessary changes will be implemented by March 2014, when the first debts may expire.

3.65 Since a permanent solution will not be in place in time, the Agency has identified accounts that may need to be considered because of their age and characteristics (to determine whether they will continue to be collectible). The Agency has focused on accounts that are at least five years old. This interim work is labour intensive, since collectors are manually reviewing older accounts. We are encouraged to see the interim steps that have been taken, but we are concerned with the lack of timeliness of the more permanent solution, which will be more efficient.

3.66 **Recommendation.** The Canada Revenue Agency should implement a permanent solution to ensure that it does not lose the right to collect accounts that will be affected by the new limitation on tax debts, and it should report its results to stakeholders.

The Agency's response. Agreed. As noted in this report, the Agency has already begun work on the development of a permanent automated solution to address limitation periods for tax debts. The permanent automated solution is expected to be implemented by October 2016, subject to resource and technological planning constraints. The Agency has transitional measures in place that will provide for the effective management of tax debts before the limitation period expires.

Management information

3.67 In 2006, we found that the Canada Revenue Agency lacked the management information necessary to guide collection efforts and to demonstrate that it achieves its objectives. The Agency developed an action plan to improve performance reporting tools for all major business revenue lines at the national, regional, local, and collector levels.

Management information has improved

3.68 Based on the Agency's action plan to address our 2006 recommendation, we examined how the Agency implemented actions to improve its management information. We found that the nature and volume of available management information have improved. The Agency now has better information on the type of account, tax debt inventory, revenue stream, file aging, bankruptcies, and insolvencies. Management has access to analyses on jeopardy applications and danger of loss reviews. We therefore found progress in this area to be satisfactory (Exhibit 3.7 in the following section).

3.69 The Agency expanded and improved its quality assurance (QA) program, which provides additional information to management. The QA reviews result in ongoing management reports with recommendations for improvements and changes in approach. Danger of loss reviews have improved, but the Agency has not achieved its target yet. This is consistent with what we found in our sampling of accounts for danger of loss reviews (paragraph 3.32). Some of the recommendations resulting from the QA reviews, such as consideration of a director's liability and deemed trust, have not yet been fully addressed.

Performance measures are still weak

3.70 In 2006, we found that management did not have the necessary performance information to determine the results of its collection efforts. We recommended that the Agency improve its performance information.

3.71 Since 2006, the Agency has added more performance measures, and it now includes measures in its annual report to Parliament that it had not reported in the past. Performance measures serve two broad purposes: program monitoring and improvement, and reporting and accountability. Both are important and complement each other. One informative measure that the Agency no longer publicly reports is the cost of collecting $1,000 of tax debt. This measure is useful, since it can show how effective the Agency is from year to year. Similarly, the Agency no longer reports the projected growth in tax debt.

3.72 The performance measures currently used by the Agency in its Annual Report to Parliament include tax services office production, dollar value of tax debts over five years old, and percentage of individuals and corporations who paid their reported taxes on time. When combined, these measures do not provide enough information on the efficiency and effectiveness of the collections program. As a result, we found progress to be unsatisfactory (Exhibit 3.7).

3.73 Recently, the Agency participated in an international benchmarking study that was initiated by its counterpart in the United Kingdom, Her Majesty's Revenue and Customs (HMRC). Published in 2011, the study covered all aspects of a tax administration's business activities. We found that the international benchmarking study contained valuable management information and measures that tangibly demonstrate collection performance. The Agency's collection approach already includes many of the best practices noted in the study.

3.74 The Agency was able to provide data on its performance to HMRC for the study, but it does not use this data in its external or internal reporting. In our opinion, it would be helpful for the Agency to include this type of data in its reporting.

3.75 The Agency developed a Collections Program Logic Model to link its resources, actions, and desired outcomes. Conceptually, a logic model helps organizations measure what matters, by linking its simplest tasks with complex long-term outcomes. Work on the Agency's logic model started in May 2011, and it is still a work in progress; when it is fully implemented, it should include more complex measures that could be used for external and internal reporting and monitoring.

3.76 We found that the Agency has made significant improvements in its management information. It needs to complete its work on the logic model to measure its performance in collecting tax debt and to guide its decision making. The shortcomings we noted in 2006 are still being addressed.

Exhibit 3.7 Progress in addressing our recommendation on management information

Recommendation	Progress
The Canada Revenue Agency should	
• significantly improve its management information to make it complete and comprehensive.	**Satisfactory**
• 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.	**Unsatisfactory**
(Recommendation 8.41 of the 2006 May Status Report of the Auditor General of Canada, Chapter 8, Canada Revenue Agency—Collection of Tax Debts)	

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.

3.77 **Recommendation.** The Canada Revenue Agency should improve how it measures the results of its collection efforts to guide its decision making and to provide better information to stakeholders on its success in meeting its stated objectives.

The Agency's response. Agreed. Performance indicators should evolve and adapt to changes in the program. Existing indicators continue to provide relevant information on program activities, expenditures, and results. However, the Agency will, in line with this recommendation, continue its work on performance indicators to ensure that the most appropriate indicators are in place to support program reporting requirements.

Conclusion

3.78 We concluded that, overall, the Agency has made satisfactory progress in implementing many of the recommendations in the 2006 May Status Report of the Auditor General of Canada, Chapter 8, Canada Revenue Agency—Collection of Tax Debts. Good progress has been made, including

- improvements to account management,
- the introduction of new tools for collectors, and
- a national approach to the management of the inventory of debts.

3.79 The Agency now has much more information about the makeup of the tax debt, which is a major accomplishment. It has completed many research projects to gather this information. The tax debt has continued to increase, from $18 billion in 2006 to $29 billion in 2012. The Agency needs to continue to refine its strategies to deal with this continued growth.

3.80 The Agency still needs to improve its risk scoring and performance measures. It also needs to develop a way to keep track of its research recommendations more strategically. Completing its work on the logic model would enable the Agency to establish more meaningful performance measures.

About the Audit

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.

Objectives

The overall audit objective was to determine whether Canada Revenue Agency has made satisfactory progress in implementing the recommendations in the 2006 May Status Report of the Auditor General of Canada, Chapter 8, Canada Revenue Agency—Collection of Tax Debts.

Tax debt is made up of the

- revenue stream—individuals (T1), corporations (T2), payroll deductions (PAYDAC), and goods and services tax/harmonized sales tax (GST/HST);
- source of the debt—including initial assessment, reassessment as a result of an audit, assessment as a result of non-filer program work, and arbitrary assessment under subsection 152(7) of the *Income Tax Act*; and
- allocation between taxes, interest, and penalties.

We examined whether the Agency

- collected the data it needed to analyze the makeup of the tax debt and to develop better collection approaches;
- significantly improved its management information to guide its collection efforts, strategies, and decisions;
- has performance measures that demonstrate that the collections program is achieving its objectives;
- improved its risk scoring processes for the collection of tax debts; and
- improved its account management for the collection of tax debts.

Scope and approach

We followed up on the commitments and deliverables made in the action plan that the Agency presented to the Public Accounts Committee in 2006, to determine whether the Agency has made satisfactory progress against the recommendations in our 2006 audit.

Our audit approach included

- document review,
- interviews with management and staff,
- analysis of information and data, and
- file sampling for large accounts.

When parts of a recommendation have not been fully implemented, or when the Agency took a different approach altogether, we looked at what the Agency did to address the observations, to determine whether the risk was mitigated.

We analyzed data relating to the management of undisputed GST, personal, and corporate tax debts ranging in value from $1 million to $10 million. Our review included the random sampling of 128 accounts that were in collections as of 31 March 2011. We chose our sample in accordance with statistical sampling methodology, to provide a high level of assurance that the Agency was following procedures when attempting to collect tax debts. Our sample size of 128 is sufficient to project the entire population of 832 with an error rate of 9.38 percent, a confidence interval of +4.92 percent, and a confidence level of 95 percent.

To confirm our understanding of the information we received, we interviewed Agency staff at various levels and locations. We visited five tax services offices and the Debt Management Call Centre. We also conducted interviews with regional program advisors, team leaders, and collections officers. At the Agency's headquarters, we met staff in the Taxpayer Services and Debt Management Branch.

Criteria

Criteria	Sources
To determine whether the Canada Revenue Agency has made satisfactory progress in implementing the recommendations in the 2006 May Status Report of the Auditor General of Canada, Chapter 8, Canada Revenue Agency—Collection of Tax Debts, we used the following criteria:	
The Agency has collected the data it needs to analyze the makeup of the tax debt and to develop better collection approaches.	• 2006 May Status Report of the Auditor General of Canada, Chapter 8, Canada Revenue Agency—Collection of Tax Debts, recommendation 8.28
The Agency has significantly improved its management information to guide its collection efforts, strategies, and decisions. The Agency has performance measures that demonstrate that the collection program is achieving its objectives.	• 2006 May Status Report of the Auditor General of Canada, Chapter 8, Canada Revenue Agency—Collection of Tax Debts, recommendation 8.41
The Agency has improved its risk scoring processes for the collection of tax debts.	• 2006 May Status Report of the Auditor General of Canada, Chapter 8, Canada Revenue Agency—Collection of Tax Debts, recommendation 8.52 • Evaluating the Effectiveness of Compliance Risk Treatment Strategies, Organisation for Economic Co-operation and Development
The Agency has improved its account management for the collection of tax debts.	• 2006 May Status Report of the Auditor General of Canada, Chapter 8, Canada Revenue Agency—Collection of Tax Debts, recommendation 8.65

Management reviewed and accepted the suitability of the criteria used in the audit.

Period covered by the audit

The audit covered the period between 1 April 2010 and 31 March 2012. Audit work for this chapter was completed on 23 November 2012.

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Appendix List of recommendations

The following is a list of recommendations found in Chapter 3. 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	Response
Account management	
3.33 The Canada Revenue Agency should follow its procedures for danger of loss reviews on large files. In addition, it should evaluate whether having one target for taking timely action for all accounts, regardless of size, is appropriate. **(3.28–3.32)**	Agreed. As noted in the report, the Agency does take action on a timely basis so that any risk of loss is clearly identified on all large files, and its quality control results exceed expectations in this area. The Agency will, however, ensure that the documentation on this small number of files reflects these actions in the most comprehensive manner possible. In addition, by April 2014 the Agency will undertake a review of its targets for danger of loss reviews on large accounts to determine their appropriateness.
Collection strategies	
3.60 The Canada Revenue Agency should develop a methodology to track and monitor its recommendations from its research to ensure that they are all followed up. **(3.53–3.59)**	Agreed. As noted in this report, the Agency has implemented many changes originating from the research it conducted. Further, the Office of the Auditor General observed that the Agency's research is extensive, ranging from tactical analyses, to improved risk scores, to high-level strategic research. The Agency recognizes that there are opportunities to improve how the relevant findings of this research are incorporated into its program planning and reporting processes. By April 2014, the Agency will develop and implement a formal process to achieve this goal.
3.66 The Canada Revenue Agency should implement a permanent solution to ensure that it does not lose the right to collect accounts that will be affected by the new limitation on tax debts, and it should report its results to stakeholders. **(3.61–3.65)**	Agreed. As noted in this report, the Agency has already begun work on the development of a permanent automated solution to address limitation periods for tax debts. The permanent automated solution is expected to be implemented by October 2016, subject to resource and technological planning constraints. The Agency has transitional measures in place that will provide for the effective management of tax debts before the limitation period expires.

Recommendation	Response
Management information	
3.77 The Canada Revenue Agency should improve how it measures the results of its collection efforts to guide its decision making and to provide better information to stakeholders on its success in meeting its stated objectives. **(3.70–3.76)**	Agreed. Performance indicators should evolve and adapt to changes in the program. Existing indicators continue to provide relevant information on program activities, expenditures, and results. However, the Agency will, in line with this recommendation, continue its work on performance indicators to ensure that the most appropriate indicators are in place to support program reporting requirements.