
MINISTRY OF FINANCE

4.07—Retail Sales Tax Program

(Follow-up to VFM Section 3.07, *Special Report on Accountability and Value for Money—2000*)

BACKGROUND

The *Retail Sales Tax Act* currently imposes a general sales tax of 8% on the retail price of most goods and services sold to final consumers. Various tax exemptions cover thousands of items and are aimed at reducing tax regression or promoting economic or social objectives. Examples of such exemptions include children's clothing, equipment for use by people with disabilities, and goods purchased by Status Indians under certain conditions.

At December 31, 1999, approximately 380,000 vendors were registered to collect and remit retail sales tax (RST) to the province. RST receipts for the 1999/2000 fiscal year totalled approximately \$12.6 billion, net of \$159.5 million in refunds, and represented 21% of the province's total revenue. For the 2001/02 fiscal year, RST receipts totalled approximately \$13.8 billion and represented 28.6% of the province's total taxation revenue.

Although RST revenues had increased significantly as of 1999/2000, and the Ministry had made improvements to its administration of this program since we last audited it in 1995, we concluded that the Ministry needed to further improve its procedures because it did not:

- conduct research into the underground economy in order to identify sectors of the economy in need of more rigorous compliance and enforcement action;
- have adequate procedures in place to ensure that all vendors that should have been registered with the Ministry to collect RST were in fact registered;
- include all segments of the small vendor population in its audit coverage;
- select vendors for audit more representatively with a view to encouraging broad-based voluntary compliance;
- follow up on all overdue vendor sales-tax returns on a timely basis; and
- often make adequate or timely collection efforts, particularly for the many smaller outstanding balances.

We made a number of recommendations for improvement and received commitments from the Ministry that it would take corrective action.

CURRENT STATUS OF RECOMMENDATIONS

The Ministry had taken or was in the process of taking corrective action on all of our recommendations. The status of each of our recommendations as of June 30, 2002 is detailed in the following.

TAX ROLL

Recommendation

To help ensure that the tax roll for vendors that sell taxable goods and services is complete and accurate, the Ministry should:

- *work with the Ministry of Consumer and Commercial Relations [which has since become the Ministry of Consumer and Business Services] to ensure that it is appropriately advised of newly registered businesses for potential inclusion in the tax roll; and*
- *implement additional procedures needed for identifying non-registered vendors selling taxable goods and services through data matching with other government databases or at their places of business.*

Current Status

The Ministry advised us that information technology business requirements and programs are being developed to link the retail sales tax and corporations tax databases (corporate registrations received from the Ministry of Consumer and Business Services) during the 2002/03 fiscal year. In addition, initial contact with the Ministry of Consumer and Business Services has been established to explore opportunities to match the business names registry with the RST database. Details are being worked out, and the Ministry hopes to obtain the necessary data during the 2002/03 fiscal year.

The Ministry has matched the RST and the federal GST databases for certain high-risk sectors and advised us that the number of non-registrants identified was somewhat less than originally anticipated. The Ministry is awaiting the results from matching other business sectors.

OVERDUE SALES TAX RETURNS

Recommendation

To identify and follow up on outstanding retail sales tax returns and required remittances more promptly, the Ministry should ensure that:

- *vendors with overdue tax returns are contacted within the required time periods; and*
- *when necessary, estimated assessments are issued on a more timely basis.*

Current Status

In May 2001, the Ministry received approval from Management Board of Cabinet to temporarily double staffing in this area to address the backlog. The extra staff were on board and fully trained as of December 2001, at which time the Ministry anticipated that the backlog would be eliminated within two years. The Ministry is currently assessing the impact of the labour disruption in the spring of 2002 on its goal of eliminating the backlog.

COLLECTIONS

Recommendation

To help maximize the collection of all outstanding accounts receivable, the Ministry should ensure that all accounts receive timely action by a collector, including those under \$10,000.

Current Status

The Ministry has improved the management information available in its information technology system in several important respects and is developing the necessary reports to effectively monitor the level of activity at all stages of the collection function. The Ministry also intends to conduct a series of operational reviews of the collection function commencing in September 2002.

ENFORCEMENT

Tax Gap

Recommendation

To help reduce the tax gap, the Ministry should conduct the research necessary to identify significant aspects of the underground economy and focus its compliance and enforcement efforts on these aspects.

Current Status

The Compliance Planning and Research Unit referred to in the Ministry's response to our recommendation was established in February 2001, and all staff were on board by October 2001.

The Ministry is part of the National Working Group on the Underground Economy. Joint compliance research at a national level is expected to move forward over the next year along with several pilot initiatives in the areas of data sharing, enforcement, and education. We were also informed that the Ministry regularly exchanges data and information on audit assessments and non-registrants with the Canada Customs and Revenue Agency.

Audit Coverage

Recommendation

To detect unpaid retail sales taxes owed to the province and to encourage broad-based voluntary compliance, the Ministry should include all segments of the small vendor population in its audit coverage and attain overall audit coverage levels that will ensure visibility in the broader vendor community.

Current Status

In October 2001, the Ministry completed a detailed review of small vendor audit coverage by profile code to identify areas requiring greater audit visibility to achieve balanced coverage. We were advised that the results of the review were discussed by the appropriate senior managers and that a plan of action to increase small vendor audit coverage was developed for implementation in the 2002/03 fiscal year.

Audit Selection

Recommendation

To help ensure that it meets its objectives for encouraging voluntary vendor compliance as well as for recovery of retail sales taxes owing, the Ministry should:

- *select vendor files for audit on a more representative basis, with a view to encouraging broad-based, voluntary compliance; and*
- *ensure that selected audits commence and are completed on a timely basis.*

Current Status

The Ministry has commenced a review of its audit selection approach and strategy in consultation with the regional tax offices. We were also advised that the development of a centralized divisional audit selection system is under review.

In addition, joint committees of staff from the Canada Customs and Revenue Agency and the Ministry now meet quarterly to better co-ordinate their respective audit efforts and share audit-related information.

The Ministry also has established timelines for the completion of audits and has developed quarterly management reports to monitor compliance with these requirements, effective October 31, 2001. However, a ministry review found that timely completion of audits continues to be a concern in some cases.

Tax Refunds

Recommendation

To help ensure that only eligible refunds of retail sales tax are made, the Ministry should maintain a list of refunds issued subject to audit and ensure that, where refunds are issued subject to audit, the necessary follow-up work is performed.

Current Status

A quarterly report on refunds processed subject to audit is regularly being provided to the appropriate offices for monitoring purposes.

Penalties

Recommendation

To provide an effective deterrent, the Ministry should consider imposing the legislated 25% penalty in cases where correct retail sales tax amounts are not remitted as a result of taxpayer neglect, carelessness, willful default or fraud. When a penalty is not imposed, the Ministry should ensure that the reasons are clearly documented.

In addition, the Ministry should review and determine whether the threshold amount below which penalties are not assessed is appropriate.

Current Status

We were advised that all offices were instructed to adhere to the existing policy.

The Ministry is also in the process of reviewing the current threshold amount under which penalties are not imposed. A draft briefing paper outlining a revised policy for the 25% penalty is currently being reviewed. Upon approval of the briefing paper, the Ministry intends to make appropriate revisions to the Audit Handbook regarding the 25% penalty.