

Head 246 – Department of Inland Revenue

1. Financial Statements

1.1 Qualified Opinion

The audit of the financial statements of the Department of Inland Revenue for the year ended 31 December 2019 comprising the statement of financial position as at 31 December 2019 and the statement of financial performance, and cash flow statement for the year then ended, was carried out under my direction in pursuance of provisions in Article 154(1) of the Constitution of the Democratic Socialist Republic of Sri Lanka read in conjunction with provisions of the National Audit Act No. 19 of 2018 . The Summary Report containing my comments and observations on the financial statements of the Department of Inland Revenue was issued to the Accounting Officer on 26 June 2020 in terms of Section 11 (1) of the National Audit Act No. 19 of 2018. The Annual Detailed Management Audit Report of the Department of Inland Revenue was issued to the Accounting Officer on 30 September 2020 in terms of Section 11 (2) of the Audit Act. This report is presented to Parliament in terms of Section 10 of the National Audit Act No. 19 of 2018 which is read in conjunction with Article 154 (6) of the Constitution of the Democratic Socialist Republic of Sri Lanka.

In my opinion, except for the effects of the matters described in Paragraph 1.6 of this report, the financial statements prepared in accordance with the provisions of State Accounts Circular No. 271/2019 dated 03 December 2019 give a true and fair view of the financial position of the Department of Inland Revenue as at 31 December 2019 and its financial performance and cash flow for the year then ended, in accordance with Generally Accepted Accounting Principles.

1.2 Basis for Qualified Opinion

I conducted my audit in accordance with Sri Lanka Auditing Standards (SLAuSs). My responsibilities, under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of my report. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

1.3 Responsibilities of Chief Accounting Officer and the Accounting Officer on Financial Statements

The Chief Accounting Officer and the Accounting Officer are responsible for Preparation of financial statements in a manner that reflects a true and reasonable position and determines the internal control required to enable financial statements to be prepared without inadequate false statements that may result from fraud and error in accordance with Generally Accepted Accounting Principles and the provisions of Section 38 of the National Audit Act, No. 19 of 2018 .

As per Section 16 (1) of the National Audit Act No. 19 of 2018, the Department is required to maintain proper books and records of all its income, expenditure, assets and liabilities, to enable annual and periodic financial statements to be prepared.

The Accounting Officer shall ensure that an effective internal control system is maintained and maintained for the financial control of the Department in terms of sub-section 38 (1) (c) of the National Audit Act and it should be periodically reviewed the effectiveness of the system and make any necessary changes to keep the system running efficiently.

1.4 Auditor's Responsibility on Audit of Financial Statements

My objective is to express a reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue the Summary Report of the Auditor General that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Sri Lanka Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with Sri Lanka Auditing Standards, I exercise professional judgment and maintain professional skepticism throughout the audit. I also furthermore;

- Appropriate audit procedures were designed and implemented to identify and assess the risk of possibility of quantitative misrepresentations occurred in financial statements due to fraud or errors in providing a basis for the expressed audit opinion. More than the impact of quantitative misrepresentations due to misrepresentation, the effect of fraud is strong because of malpractice, forgery, intentional evasion, misrepresentation, or evasion of internal controls can lead to fraud.
- Although it is not intended to express an opinion on the effectiveness of internal control , obtained an understanding of internal control in order to plan appropriate audit procedures occasionally.
- Evaluated the appropriateness of the accounting policies followed, fairness of accounting estimates and related disclosures made by Management.
- Evaluated whether the transactions and events underlying the structure and content of the financial statements are appropriately and fairly consisted in and presentation of financial statements including disclosures as a whole.

The Accounting Officer was made aware of important audit findings, key internal control deficiencies and other matters identified in my audit.

1.5 Report on Other Legal Requirements

I declare the following matters in terms of Sub-section 6 (1)(d) and Section 38 of the National Audit Act No. 19 of 2018 .

- (a) The financial statements are in consistent with those of the preceding year,
- (b) The recommendations made by me regarding the financial statements furnished for the preceding year had not been corrected as per the observations shown in Paragraphs 1.6.1(a), (b) and (c) of this report.

1.6 Comments on Financial Statements

1.6.1 Statement of Financial Performance

The following observations are made.

Audit Observation	Recommendation	Comments of the Accounting Officer
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(a) The revenue collected on the Value Added Tax by the Department is credited to the control account maintained by the Treasury. The money so credited is being accounted for the three Value Added Tax Revenue Codes of financial services, other services and products. The amount of Rs. 314,321,679 remained in the control account as at the end of the year under review after taking into accounts by monthly account summaries, the Value Added Tax had been credited to the other service revenue code by a transfer slip without identifying as per Revenue Codes. Accordingly, the accuracy of the net income in three Revenue Codes of financial services, products and other services based on value added was not ascertained in audit.	It should be credited to the accurate Revenue Code accurately identifying the income and categorizing as per the Code.	It has been brought to accounts with a transfer sheet on the difficulty of classifying income by a transfer

- (b) The Other Income Code No. 1004-02-99 under Non-Collective Income Tax, acts as a revenue code as well as a control account as per the information submitted to audit. Even though a sum of Rs.508,145,885,296 had been credited to the above control account during the year under review as per the information of the Treasury, as a result of the Department had identified the income of the control account as Rs.508,213,925,648 in the income classification, there was a difference of Rs.68,040,352 . It had been matched with the Treasury Books by adjusting to the other revenue codes in the Departmental Books without identifying the reasons for this difference and adjusting to the relevant revenue codes.
- Adjustments should be made correctly identifying differences between Treasury information and Departmental Books.
- This adjustment was made to nullify the revenue control accounts.
- (c) Since it was observed that the steps have not been taken to reconcile the money credited to the Treasury through the revenue collection bank accounts with bank accounts estimates and rectify the differences identified therein periodically, it was observed that there were weaknesses in the accounting control system.
- Preparation of revenue reconciliation reports in a timely manner and to take steps to rectify deficiencies identified and carrying out follow up actions on that.
- A considerable time will, be taken correct identified deficiencies.

1.6.2 Statement of Financial Position

The following observations are made.

Audit Observation	Recommendation	Comments of the Accounting Officer
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(a) Even though the balance of property, plant and equipment as at 31 December 2019 was Rs. 5,635,976,225 as per the financial statements of the	When preparing financial statements, the financial statements should be prepared on the basis	The year-end balance is accurate and as a result of the defects remained in the system, this difference had occurred.

Department, thus that balance as per the information of the Treasury was Rs.5,374,525,446. A difference of Rs. 261,450,779 was observed of accurate balances as comparing with treasury books.

- (b) The balance of Property, plant and equipment as at 31 December 2018 as per the financial statements of the preceding year was Rs.5,248,351,927. As per the information provided to audit , the opening balance after adjusting the assets amounted to Rs.110,591,245 identified during the year under review and acquired in the year 2018 and in previous years should have been Rs.5,358,943,172. Nevertheless, as that balance had been stated in the ACA-6 form of the financial statement as Rs.5,635,976,225 , a difference of Rs.277,033,053 was observed in the opening balance of non-financial assets. Proper adjustments should be made and start-up balances should be included in the financial statements correctly. It has not been uploaded accurately as a result of an error remained in CIGAS System.
- (c) The details relating to acquisition of property, plant and equipment amounting to Rs.406,872,711 and the disposals amounting to Rs.129,839,658 during the year under review had not been mentioned in the ACA-6 Format in the financial statements and Treasury printouts and those had been adjusted to the opening balance of the year in the Departmental books. Accordingly, the balance obtained amounting to Rs.5,635,976,225 had been stated in the financial statements as the closing balance of the property, plant and equipment. Information on non-financial assets acquired and disposed during the year should be reported to the Treasury and shown in the prescribed format of financial statements. The shortcoming has occurred as a result of a technical error in the system.

1.6.3 Deficiencies in Maintaining Documents and Books

Audit Observation	Recommendation	Comments of the Accounting Officer
The Register of Losses and Damages which should be maintained in accordance with Financial Regulations 110 had not been updated.	The Register of Losses and Damages should be updated and maintained in accordance with Financial Regulations 110.	It has been updated.

1.6.4 Certifications that should be made by the Accounting Officer

Audit Observation	Recommendation	Comments of the Accounting Officer
The Chief Accounting Officer and Accounting Officer should ensure that an effective internal control system for the financial control exists in accordance with the Provisions of Section 38 of the National Audit Act No. 19 of 2018 and carry out periodic reviews to monitor the effectiveness of such systems and accordingly make any alterations as required for such systems to be effectively carried out. Even though such reviews should be made in writing and submitted a copy to the Auditor General, statements that such reviews were made had not been furnished to audit.	Actions should be taken in accordance with the Provisions of Section 38 of the National Audit Act No. 19 of 2018 .	Answers have not been given.

1.6.5 Non-compliance with Laws, Rules and Regulations

The instances of non-compliance with the provisions in Laws, Rules and Regulations observed at the audit test checks carried out are analyzed below.

Audit Observation	Recommendation	Comments of the Accounting Officer
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(a) Even though the Nations Building Tax collected under the Nation Building Tax Act No. 9 of 2009, had been abolished from 01 December 2019, Parliamentary approval had not been obtained for that.	Actions should be taken to obtain the Parliamentary approval properly in accordance with policy decisions.	Actions have been taken on the instructions of the Ministry of Finance.
(b) The tax rates can be changed by a Gazette Notification as per the order of the Minister in terms of Section 2 (a) of the Value Added Tax Act No. 14 of 2002 as amended by the Value Added Tax (Amendment) Act No. 6 of 2005 and those regulations should be passed in Parliament as soon as possible. Nevertheless, even though the Value Added Tax rates on goods, imports and other services had been revised to 8 per cent with effective from 01 December 2019 it had not been presented to Parliament and passed.	The tax rate revisions should be presented to Parliament and passed in terms of the Provisions of the Act..	An Extraordinary Gazette Notification has been issued.

2. Financial Review

2.1 Revenue Management

The following observations are made.

	Audit Observation	Recommendation	Comments of the Accounting Officer
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(a)	Accounting Officers for State Revenue should try to prepare Revenue Estimates in full, as accurate as possible and in a realistic manner in accordance with Financial Regulations 85 (1)(c) and Financial Regulations 128 (2) (a) . Nevertheless, even though the Annual Revenue Estimate of the Department of Inland Revenue for the year under review was Rs. 1,038.1 billion, thus the actual collection was Rs. 975.9 billion, there was a variance of Rs. 62.2 billion and it was 6 per cent out of the Estimated Income. Accordingly, it was observed that the revenue estimation had not been properly made.	Steps should be taken to prepare revenue estimates as accurately as possible complying with Financial Regulations.	Even though the estimates have been made based on existing tax policies at the beginning of the year, the policy changes that took place during the year had caused to this.
(b)	Even though the Department had not estimated revenue under 7 Revenue Codes, a Rs. 1,555 million had been collected under those 7 Revenue Codes by the end of the year under review.	Steps should be taken to prepare revenue estimates as accurately as possible complying with Financial Regulations.	Only the collection of arrears and fines have taken place.
(c)	The net value of collection of Income Tax was Rs. 427.6 billion as per the financial statements for the year under review and the corresponding	A system for providing Tax Returns by dividing the Tax revenue collected as arrears collections in previous years and on self-assessment and	A complete answer has not been given.

net income tax collection of the preceding year was Rs. 310.4 billion. It was observed that the collection of income tax had increased by Rs.117.2 billion as compared to preceding year and that is, an increase by 37.8 as compared to preceding year. The information requested for the audit was not provided by the Department even by 25 August 2020 .

additional assessment in the year under review should be formulated.

- (d) The Value Added Tax Revenue and the Nation Building Tax Revenue under tax collection on local goods and services had decreased by Rs. 17,773 million and Rs. 685 million respectively in the financial statements as compared to the preceding year. The information requested for audit to analyze the impact of government policy decisions taken on these taxes during the year under review had not been provided by the Department even by 25 August 2020 .
- A system for providing Tax Returns by separating the Tax revenue collected as arrears collections in previous years and on self-assessment and additional assessment in the year under review should be formulated.
- A complete answer has not been given.
- (e) Even though it had been identified that the arrears of taxes and fines totalled to Rs. 290,812,600,505 pertaining to Legacy System and RAMIS System as Rs.127,762,151,321 and Rs.163,050,449,184 per each respectively can be recovered, it was observed that the Department had not recovered them even by 30 June 2019.
- Taking formal actions against officials who did not collect/ settle arrears of taxes and fines in a timely manner and arrangements should be made to take steps to expedite the collection / settlement of all arrears of taxes and fines which can be recovered / settled from the aforesaid arrears balance by implementing all the actions for collecting as mentioned in the relevant Tax Acts.
- Actions will be taken to settle.

- (f) It was observed that the balance of total arrears of taxes and fines amounted to Rs.192,663,476,619 remained in relation with Legacy System as at 31 December 2012 had been increased up to Rs.309,934,567,851 that was 61 per cent up to by 30 June 2019 and the unsettled arrears of taxes and fines under the RAMIS System had also been increased by Rs.2,529,558,269,902 that was 190 per cent was observed as at 30 June 2019 as compared to the year 2018 .
- (g) The total of the collectible and temporarily suspended arrears of taxes and fines as at the beginning of the year under review as per the Arrears Tax Report was Rs. 1,608.1 billion as Rs.287.5 billion and Rs.1,320.6 billion respectively. Nevertheless, these figures had not been stated in the opening balance of arrears of taxes of the year in the Form ACA-1 (i) of the financial statements.
- (h) The collectible arrears of taxes and fines as at 31 December 2018 Had been stated as Rs. 287.5 billion as per the financial statements of the preceding year and no details whatsoever had been stated with regard to the collection of arrears income in the ACA-1 Format of the financial statements. Nevertheless, it was observed that the Legacy Division had
- Taking formal actions against officials who did not collect/ settle arrears of taxes and fines in a timely manner and arrangements should be made to take steps to expedite the collection / settlement of all arrears of taxes and fines which can be recovered / settled from the aforesaid arrears balance by implementing all the actions for collecting mentioned in the relevant Tax Acts.
- The opening balances of the financial statements should be stated accurately.
- The details relating to the collection of arrears of tax revenue should be disclosed in the financial statements.
- Actions will be taken to settle.
- That only the facts contained in the Arrears Tax Returns have been used.
- Arrears of taxes and fines are also included within collections of the year under review.

collected Rs. 5.6 billion for the tax period before 31 December 2015 as revealed in the audit test check carried out.

- (i) The total of arrears of taxes and fines was Rs. 579.2 billion at the end of the year under review as per the Arrears tax Reports furnished to audit. Only Rs. 264.4 billion of that amount, which had been identified as collectible arrears of taxes and fines, had been stated as the arrears of taxes relating to the year under review and as at the end of the year. Details of arrears of taxes that the collections were suspended temporarily amounted to Rs. 314.8 billion had not been disclosed in the financial statements. Further, there were also instances where arrears of taxes were not classified separately according to Revenue Codes.
- Details of arrears of tax that have been suspended temporarily should be disclosed in financial statements and the arrears income should be shown in financial statements as per the Revenue Codes.
- Because of the recovery of the suspended tax depends on the factors that affect the suspension, it has not been included in financial statements.
- (j) Even though the Casino Industry Income Tax totalled to Rs. 4,000 million from 04 Casino Businesses as Rs. 1,000 million from each should be collected on or before 15 November 2015 in terms of the provisions of the Finance Act No. 10 of 2015, out of that only a sum of Rs. 1,330 million had been collected even by the end of the year under review. Accordingly, there was a sum of Rs. 2,670 million further to be recovered.
- Actions should be taken to recover the arrears of taxes implementing the provisions of the Act.
- Judicial actions are being taken to recover the arrears.

- (k) A suspense balance of Rs.6,423 million recorded as income from taxpayers, but had not settled and not recorded in taxpayers' accounts as a result of shortcomings and errors had remained in the Revenue Administration Management Information System (RAMIS) as at 30 June 2019 . It was observed in audit that the arrears of taxes were overstated by that amount due to the suspense account had not been settled.
- Prompt actions should be taken to accurately identify the balances related to the suspense account and to settle making appropriate adjustments.
- Steps will be taken to settle the suspense account and not to occur again.
- (l) After the establishment of two new Divisions in 2018 to settle the arrears in 2018 Legacy System, it had fallen from 90.1 per cent to 58.7 per cent of the total arrears as at 31 December 2018 in comparing the temporarily suspended arrears balance with the opening balance of 2018. Further, it was observed that the collectible balance had increased from 9.9 per cent to 41.3 per cent. Similarly, the settlement of arrears of taxes amounted to Rs. 52.3 billion from 01 January 2018 to 30 June 2019 by those two divisions were also observed.
- Since proper actions have been taken as compared to identify and settle the arrears of taxes by the two new Divisions established in 2018 to settle arrears of taxes under the Legacy System , steps should be taken to strengthen those Divisions to expedite their activities.
- The necessary arrangements will be made.
- (m) It was observed that a sum of Rs.106,022,099,057 out of arrears of taxes and fines under the Legacy System that is, 83 per cent consisting of Income Tax, Value Added Tax and Nations Building Tax . Of that, arrears taxes and fines on Value Added Taxes collected from a third party by taxpayers
- Taking formal actions against officials who did not collect/ settle arrears of taxes and fines in a timely manner and arrangements should be made to take steps to expedite the collection / settlement of all arrears of taxes and fines which can be recovered / settled from the aforesaid
- Steps will be taken to settle the arrears balances

that is, non - collection of 42 per cent of the total collectible tax even by 30 June 2019 was observed. Further, the Income Tax amounting to Rs.99,400,948,822, Value Added Tax Rs.46,061,315,513 and Nation Building Tax Rs.15,871,714,318 identified as collectible arrears taxes and fines remained under the RAMIS System but not recovered even by 30 June 2019 was observed.

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| (n) | <p>A time analysis had not been provided for tax arrears under the RAMIS System and all arrears of tax and balances of fine receivable were the balances from the year 2016 to 30 June 2019 . A time analysis for the arrears of taxes and fines that can be recovered under the Legacy System had been submitted as at 31 December 2018 and since a sum of Rs. 16,196,825,309 relating to the year 2018, Rs.73,679,926,589 relating to the year 2013 to 2017 and Rs.28,692,788,374 relating to the year 2012 and for the years before that had remained therein, it was observed that actions had not been taken in timely manner to recover the arrears of taxes.</p> | <p>Taking formal actions against officials who did not collect/ settle arrears of taxes and fines in a timely manner and arrangements should be made to take steps to expedite the collection / settlement of all arrears of taxes and fines which can be recovered / settled from the aforesaid arrears balance by implementing all the actions for collecting as mentioned in the relevant Tax Acts.</p> | <p>Steps will be taken to settle the arrears balances.</p> |
| (o) | <p>According to the reasons given for the suspension of the balance of arrears of taxes and penalties as at 30 June 2019 submitted to the audit of the Legacy System, the balance</p> | <p>Except for arrears of taxes and fines suspended due to appeals and court proceedings under the Legacy System, settlement of all arrears of taxes and fines suspended due</p> | <p>Steps will be taken to settle the arrears balances</p> |

suspended due to tax appeals and court proceedings was Rs.107,033,708,919 and it was observed that the recovery of them had determined on resolving of those appeals and the judicial proceedings. Nevertheless, it was observed that the Department had not taken steps periodically to rectify them although there was a possibility of settling the balance of Rs. 5,926,962,430 identified as reasons. Further, an arrears of tax amounted to Rs.45,632,059,767 and an arrears of fine amounted to Rs. 23,579,685,414 that had not given reasons for suspension were also observed within the balances where charges were suspended temporarily.

to other reasons promptly and perform a quick inspection of all individual balances for which the reasons for suspension have not been identified and identifying reasons thereon, actions should be taken to settle them.

- (p) It was not observed that the proper actions had been taken to recover or settle the old tax balances receivable amounting to Rs. 8,632,395,894 under the Legacy System in respect of Repealed Tax Acts. Proper steps should be taken to recover the tax arrears balances pertaining to Repealed Tax Acts periodically. Steps will be taken to settle the arrears balances
- (q) Even though it had elapsed for more than 8 years transferring of a tax amounting to Rs.21,727,891,075 and a fine amounting to Rs.11,535,311,638 from taxes and fines transferred in 2010 to the Default Tax Recovery (DTRU) Unit to charge or settle, it was observed that the arrangements had not been made to recover or settle even by 30 June 2019. Steps should be taken to recover or settle defaulted taxes implementing the provisions in the Special Provisions Act for the Recovery of Defaulted Taxes. Steps will be taken to settle the arrears balances

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| (r) | Failure of the Department to maintain the updated information of the taxpayers to settle arrears of taxes pertaining to Repealed tax Acts. | A relevant internal control system should be established to keep the information safety until the tax arrears are settled . | Further actions will be taken in this regard. |
| (s) | It was observed that a proper internal control system was unavailable to monitor at the time of arrears had occurred until it is settled and to take follow up actions. | Actions should be taken to establish a formal internal control system. | Further actions will be taken in this regard. |

2.2 Expenditure Management

The following observations are made.

Audit Observation	Recommendation	Comments of the Accounting Officer
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(a) Although the Accounting Officer should be responsible to ensure that the annual expenditure estimates were prepared as fully and accurately as possible in terms of Financial Regulation 50(II), it was observed that the provisions for budget estimates for 9 expenditure objects had been changed from 14 per cent to 128 per cent by Financial Regulations 66 and 69 transfers for the year under review.	Steps should be taken to act in accordance with Financial Regulations and prepare estimates as accurately as possible.	The factors that affected the transfer of funds have been revealed.
(b) Out of net provision totalled to Rs. 100,050,000 allocated for 2 expenditure objects from the Estimate for the year under review, no money	The Action Plan and the Procurement Plan should be properly prepared and the provisions should be utilized effectively.	Matters that had affected to save provisions have been revealed.

whatsoever had been utilized. Further, Further, since out of the net provision totalled to Rs. 3,262,095,000 provided for 08 capital expenditure objects and 06 recurrent expenditure objects, only Rs. 1,026,197,083 had been utilized, the savings had been Rs.2,235,897,917 and those savings had ranged from 11 per cent to 97 per cent of net provision.

2.3 Deposit Balances

The following observations are made.

Audit Observation	Recommendation	Comments of the Accounting Officer
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(a) It was observed that the actions had not been taken in terms of Financial Regulations 571 with regard to the deposit balances totalled to Rs.22,220,583 remaining for more than 02 years in 03 General Deposit Accounts.	Actions should be taken in terms of Financial Regulation 571 in connection with relevant balances.	It will be taken into income in the year 2020, by acting as applicable.
(b) The Stamp Duty revenue amounted to Rs.474,118,508 to be collected by the Department of Inland Revenue and remitted to the Provincial Councils had been retained in a General Deposit Account even by the end of the year under review without remittance to the Provincial Councils.	Actions should be taken to remit the Stamp Duty revenue collected to the Provincial Councils promptly.	Payments will be made as per the receipt of allocations from the Treasury.

2.4 Reconciliation Statements on Advances to Public Officers Account

The following observations are made.

Audit Observation	Recommendation	Comments of the Accounting Officer
(a) It was observed that a debt balance totalled to Rs. 330,750 had not been settled in relation to three officers who had transferred from the Department of Inland Revenue to the Provincial Councils. Further, debt balances due from deceased, retired, suspended and dismissed officers amounted to Rs.301,414, Rs.665,900, Rs.350,348 and Rs.621,428 respectively had also not been settled even by the end of the year under review.	Debt balances should be settled in terms of the provisions of the Establishments Code and Circulars.	Actions will be taken to settle in the year 2020 .
(b) The total outstanding debt balance for more than 20 years relating to 10 officers was Rs. 189,773 .	Debt balances should be settled promptly Need to checking information.	Since these loan balance details cannot be found, the requests have been made for a write off.

3. Operating Review

3.1 Performance of the Tax Administration System

The following matters were observed with regard to the Revenue Administration and Management Information System.

Audit Observation -----	Recommendation -----	Comments of the Accounting Officer -----
(a) A number of 764,251 Tax Returns issued to 329,979 taxpayers in the period up to 31 December 2019 based on the audit from 01 January 2016 the date launching the implementation of the new Tax Administration Management Information System (RAMIS) of the Department had not been returned to the Department even by 31 December 2019 . It was observed that the Department had not taken steps to bring these tax records in a timely manner and to collect the accurate tax revenue on the Returns and to collect additional taxes. Out of these Tax Returns, only 148,329 Returns had remained uncompleted work item in the RAMIS system and it was observed that the work item were not focused to officers through the system to take action to obtain 615,922 Tax Returns.	Actions should be taken to bring Tax Returns promptly by directing officers through the system and focusing on work subjects of the officers and it should act in accordance with the provisions of the Tax Acts regarding taxpayers who do not submit reports.	Many Tax Returns are entitle to recent tax periods and prompt actions will be taken to obtain Tax Returns.

- (b) A number of 283,055 Tax Returns received from 210,572 taxpayers from the year 2016 to 2019 as per the information obtained from the Revenue Administration Management Information System (RAMIS) had not been processed even by 27 February 2020 (Permanent Acknowledgement had not been issued) . If there is a tax arrears on the returns as a result, it was observed that the tax administration was not carried out efficiently due to non-issuance of relevant assessment reports and non-reporting as arrears, unavailability of an opportunity to Divisions to take actions to collect arrears, lack of comparison of tax schedules, lack of selection of Tax Returns for tax audit.
- A methodology should be formulate to process all receiving Tax Returns into the system as soon as possible.
- Even though there were gaps between Tax Returns and Schedules, a system of inclusion in the Tax Return System will be developed.

3.2 Management Activities

The following matters relating to management of Tax Returns were observed.

Audit Observation	Recommendation	Comments of the Accounting Officer
<p>(a) Even though an investigation had been commenced in the year 2018 regarding the tax file No. 114015198 based on information received from an external party in November 2017, the Department had not taken steps to complete the investigation and issue assessment reports even by 11 May 2020. Details pertaining</p>	<p>The taxes and fines should be collected by issuing of assessment reports for accurate tax liability identifying income through bank credits accurately and subject it to tax and to expedite the investigations of the Investigation Division</p>	<p>Actions will be taken to issue assessment reports after comparing the bank credits discussing with the taxpayer .</p>

to 12 bank accounts of the lessee from the assessment year 2014/15 to the assessment year 2018/19 had been brought by the Department in the year 2019. As per those details, the total deposit of Rs.5,551,811,189 and the total of US \$ 725,902 had credited during the period under review. It was observed that the Department had not taken actions even by now to check these bank credits and assess the taxpayer's accurate tax credit.

and establish an internal control system that oversees it.

- (b) It was observed in comparing the income shown in the financial statements submitted by a taxpayer to the Colombo Municipal Council for a procurement activity and the revenue in the financial statements submitted to the Department of Inland Revenue along with income tax returns for the assessment years 2016/17 and 2017/18, that the taxes had been calculated showing the income in less by Rs.587,339,848 and Rs.539,724,082 respectively. Even though this taxpayer had collected an income amounted to Rs.83,564,169 and Rs. 333,907,330 providing services to Colombo Municipal Council only in the years 2018 and 2019 respectively with the a total of Rs. 54,452,804 Value Added Tax, it had been reported that the value added tax amounted to Rs. 3,665,147 only was collected from the Municipal Council as per the Schedules

Actions should be taken to levy additional taxes on accurate income to take legal action against the taxpayer for non-submission of accurate reports in accordance with the provisions of the Tax Acts.

Information has been called from the Municipal Council and the taxpayer and investigations are being carried out.

given to the Department for that period. Even after the audit pointed out these facts, the Department had not taken action to issue additional assessments for all relevant taxes on the accurate income.

- (c) A total of Rs.99,237,612 had been collected as Value Added Tax as Rs. 13,675,284 from 02 Institutions from 15 June 2010 to 31 December 2015 and Rs. 85,562,328 from 05 Institutions from 01 January 2016 to 31 December 2019 by the Taxpayer who holds Tax File No. 593120988. Nevertheless, the taxpayer had disclosed only Rs. 423,768 as Output Tax under Value Added Tax during the period under review. The Department of Inland Revenue had not audited this Tax Returns in a timely manner and even though an investigation was carried out in 2019 and an additional estimate of Rs. 58,047,389 had been issued, it was observed that only Rs. 11,000,000 had been recovered from the assessment even by 31 December 2019. The Department had not taken actions to take legal action against the taxpayer under Section 66 of the VAT Act for non-submission of accurate reports.

Actions should be taken on levying additional tax on accurate tax liability by calling for detailed information and to take legal actions against the taxpayer as per the Value Added Tax Act.

The additional assessments will be issued and recovered.

- (d) The Department had conducted an audit pertaining to the Tax File No. 174008957 and a difference of Rs. 1,029,007 in turnover had been identified in the Value Added Tax and Nation Building Tax Reports therein. Even though the above difference had been mentioned in the letter rejecting the report on the results of the tax audit, the tax computation had been done understating the Value Added Tax Turnover within the RAMIS system by Rs.1,029,007.
- Assessments should be issued on the accurate tax liability and collect the tax.
- An additional assessment will be issued for the accurate tax amount.
- (e) Taxpayers were required to submit Tax Returns and Schedules on time in terms of Section 21 (1) of the Value Added Tax Act No. 14 of 2002 as amended by the Value Added Tax Act No. 20 of 2016 and in terms of Gazette Notification No. 1991/35 issued on 02 November 2016. Nevertheless, the Colombo Municipal Council had submitted only one Tax Report and a Schedule for the tax period from 01 January 2016 to 31 December 2019. It was observed that there was no comparisons of input and output taxes in the tax administration system due to non-submission of Tax Returns and Schedules. It was also observed that the Department had not taken legal actions against the Municipal Council for non-submission of reports.
- Taking steps to obtain Tax Returns and sub-documents from the taxpayer and it should act in accordance with the provisions of the Act regarding non-submission of Tax Returns and Schedules.
- The discussions have been carried out by calling officers of the institution to submit the Tax Returns and Schedules.

3.3 Transactions in Fraudulent Nature

The following matters were observed during the special audit inspection conducted to examine the process carried out by the government agencies in respect of Value Added Tax.

Audit Observation	Recommendation	Comments of the Accounting Officer
<p>(a) It was observed at the audit test check carried out that a Value Added Tax amounted to Rs.1,031,172,093 collected from 668 taxpayers from 83 government agencies had not been included in the Output Schedules submitted with the Value Added Tax (VAT) Returns by the taxpayer as per the information furnished to audit.</p>	<p>Actions should be taken to recover the taxes receivable in accordance with the provisions of the Act by re-checking the information that is currently updated in the computer system and obtaining further information from the relevant government institutions.</p>	<p>Further arrangements will be made by checking the information.</p>
<p>(b) Even though 14 government agencies had paid a Value Added Tax amounting to Rs.18,123,901 to 33 taxpayers on obtaining procurement of goods and services, as revealed in the audit test check carried out, it was observed that they were inaccurate tax file numbers in the examination performed as per the computer system.</p>	<p>Actions should be taken to recover this tax amount in accordance with the provisions of the Value Added Tax Act and all the government institutions should be made aware to pay Value Added Tax (VAT) only after verifying the registration of the taxpayers in future.</p>	<p>Further arrangements will be made by checking the information.</p>
<p>(c) Even though VAT amounted to Rs. 15,848,913 had been collected from 04 Government Institutions out of 5 taxpayers as revealed in the audit test checks carried out, any Output Tax had not been</p>	<p>Actions should be taken to recover the taxes to be recovered in terms of the Act by re-checking the information that is currently updated in the computer system and obtaining further</p>	<p>Further arrangements will be made by checking the information.</p>

reported relating to that period and it was observed that only the blank Tax Returns had been submitted.

information from the relevant government institutions.

- (d) Even though a sum of Rs.28,769,492 had been collected from three 21 government institutions by 21 taxpayers, it was revealed at the audit test checks carried out that the only a sum of Rs.8,514,732 that is, Rs.20,254,760 in less out of the amount collected from state institutions had been shown in the Tax Returns. Accordingly, it was observed that there were instances where taxpayers report a low amount less than the amount collected from government agencies as the value of Output Tax.

Actions should be taken to recover the taxes to be recovered in terms of the Act by re-checking the information that is currently updated in the computer system and obtaining further information from the relevant government institutions.

Further arrangements will be made by checking the information.

- (e) Even though 36 government agencies had paid a Value Added Tax totalled to Rs. 309,805,817 to 178 taxpayers, in cases where output documents had not been submitted under the relevant tax file numbers to check whether they have been properly reported to the Inland Revenue Department and there were instances where the records were not included in the computer system .

Actions should be taken to recover the taxes to be recovered in terms of the Act by re-checking the information that is currently updated in the computer system and obtaining further information from the relevant government institutions.

Further arrangements will be made by checking the information.

3.4 Losses and Damages

The following observations are made.

Audit Observation -----	Recommendation -----	Comments of the Accounting Officer -----
<p>(a) The following matters were observed during the examination of the actions taken by the Department of Inland Revenue to recover the money for returned cheques which were received from the taxpayers</p> <p>but returned as at 30 June 2019.</p>		
<p>(i) A number of 8,060 cheques totalled to Rs.3,031.8 Million received as 5,558 cheques under the Legacy Tax Administration System and 2,502 cheques under the RAMIS Tax Administration System had not been settled even by 30 June 2019 .</p>	<p>Prompt actions should be taken to recover for checks or to check and settle</p>	<p>Prompt actions will be taken to resolve.</p>
<p>(ii) It had been revealed that the reason for the returning of approximately 89 per cent of cheques out of the cheques returned was the failure to provide proper bank payment facility by the taxpayer. Nevertheless, it was observed that the Management had not</p>	<p>Attention of the Management should be drawn to introduce modern technology payment methods instead of cheques for the collection of taxes.</p>	<p>Actions will be taken to introduce new payment methods.</p>

drawn attention to levy taxes, to introduce bank advices or other modern technical payment methods.

(iii) A number of 4,028 cheques totalled to Rs.2,039,529,515 out of returned cheques were observed that the cheques pertaining to Value Added Tax and it had exceeded 67 per cent of the total value of the returned cheques. The Value Added Tax is an indirect tax collected by the taxpayer from a third party and remitted to the Department of Inland Revenue. Accordingly, returning of the cheques related to these indirect taxes had occurred and actions had not been taken to recover cash quickly for returned cheques.

(iv) A fine of 10 per cent of the value of the cheque is charged for returning cheques. It was observed that the levying of fines is carried out by the officers of the Department only on the basis of the letter issued by the Commissioner of Clearance Division and the Commissioner General of Inland

It should recover the money promptly for these returned cheques and it should follow a formal programme to prevent this situation in future.

Steps should be taken to formalize the legal basis furthermore in levying fines.

Steps will be taken to settle these returned cheques.

Arrangements will be made to reveal the legal basis.

Revenue had reported to the audit that there was no other written approval for that.

(v) Even though the Payments and Reconciliation Division had provided details of returned cheques to the Divisions of the Head Office and Regional Offices, it was observed that the internal control systems on follow-up the functions of relevant settlement procedures had not been properly implemented.

A proper internal control system should be formalized.

The existing internal control system will be further formalized.

(b) All the Divisional Secretaries were made aware by Circular No. SEC / 2019/02 dated 14 May 2019 by the Commissioner General of Inland Revenue for collection of arrears of stamp duty which had not been charged by the Divisional Secretariats in issuing liquor licenses. Out of the arrears stamp duty receivable From 23 Divisional secretariats amounting to Rs.82,712,000, only a sum of Rs.2,815,000 was collected and remitted to the Department. Accordingly, it was observed that the stamp duty arrears had not been periodically brought to the Department.

Actions should be taken to make aware all the Divisional Secretariats and to bring the outstanding stamp duty on liquor licenses to the Department promptly.

Actions will be taken to make aware the Divisional Secretariats and follow up actions will be carried out and recoveries will be made.

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| <p>(c) In paying remuneration, taxes on employee income should be deducted and sent to the Department of Inland Revenue by employers in accordance with the Provisions of the Inland Revenue Act No. 24 of 2017 . PAYE Tax Returns in the assessment year 2018/2019 and Schedules relating to two Departments, a Board and a State Company out of the reports so sent were checked with the computer system. It was observed that the above 4 institutions had sent a total of Rs. 11,081,661 charging in less as PAYE tax in computing the income tax according to the tax rates of the Inland Revenue Act based on the remuneration given in the Schedules.</p> | <p>Prompt actions should be taken to recover the accurate tax amount and proper steps should be taken to prevent such situations.</p> | <p>The discussions will be made with the relevant institutions in this regard and future actions will be taken.</p> |
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3.5 Procurements

Audit Observation

The physical progress in procurements relating to computer and information technology had ranged from 0 to 40 per cent as per the Procurement Plan of 2019 and its' progress. Since the Department had started the New Information Technology System Tax Administration since 2016, it was observed

Recommendation

Planning should be carried out in proper manner to conduct procurement activities efficiently.

Comments of the Accounting Officer

Certain procurement activities have not been completed.

that the lack of carrying out proper procurement could affect the efficiency of the system.

3.6 Assets Management

Audit Observation	Recommendation	Comments of the Accounting Officer
----- The Gampaha Regional Office of the Department of Inland Revenue is maintained in a rented building and a total of Rs.12,975,000 as rent from the year 2014 to March 2019 for that and a sum of Rs.7,036,425 for office interior settings in the year 2018 had been spent. Nevertheless, the Department had failed to obtain the required infrastructure facilities optimally from the building owner for about 52 staff and the taxpayers arrive to the office and it was observed during checking of the file that there was a complicated situation in between the two parties regarding the rent .	----- Actions should be taken to obtain the relevant facilities from the supplier as per the agreement.	----- The disagreement existing with the lessor regarding the rent of the building had affected this.