



Audit Conclusion

18/07

Information support of the tax administration agenda

The audit was included in the audit plan of the Supreme Audit Office (hereinafter the “SAO”) for 2018 under number 18/07. The audit was headed and the Audit Conclusion drawn up by the SAO member Ing. Daniel Reisiel, MPA.

The aim of the audit was to verify the effectiveness, economy and efficiency of spending funds on the information support of the tax administration agenda.

The audit was conducted with the audited entities between March and October 2018. The period audited was from 2011 to 2017, and the preceding and subsequent periods where relevant.

Audited entities:

Ministry of Finance (hereinafter the “MF”),
General Financial Directorate (hereinafter the “GFD”).

The **Board of the SAO** at its 4th session, which took place on 25 March 2019, **approved** by Resolution No. 7/IV/2019 **the audit conclusion** in the following wording:

KEY FACTS

CZK 8.3 billion

Total amount of expenditure on the Financial Administration ICT in the period under review of 2011-2017

CZK 437 million

Total expenditure on the E-sales project, which introduced and implemented the electronic register of sales

IS ATIS

One of the most obsolete information systems in the state, through which the Financial Administration of the Czech Republic administered tax revenues of almost CZK 796 billion in 2017

45%

Share of the financial volume of ICT contracts related to the IS ATIS awarded without competition in the period under review of 2011-2017 out of a total of about CZK 5 billion

CZK 428 million

Total value of uneconomically executed public contracts audited under Audit 18/07

CZK 70 million

Value of ineffectively acquired information technologies related to the electronic register of sales; the performance of those information technologies could have been provided by the GFD through the already acquired HW

CZK 824 thousand

Average amount paid by the GFD for one routine service intervention of after-warranty support of HW servers for the electronic register of sales

1.40%

Average utilisation rate of the computing power of servers acquired for the purposes of data processing under the electronic register of sales

I. Summary and evaluation

The SAO carried out an audit of the funds spent on information support of the tax administration agenda in terms of effectiveness, economy and efficiency. A key element of the information support for tax administration is the *Automated Tax Information System* (hereinafter the "IS ATIS"), which was put into operation in 1993 and the administration of which was taken over from the MF by the GFD in 2011. The Financial Administration of the Czech Republic, through the IS ATIS, provides the administration of taxes (in 2017, almost CZK 796 billion).

Compared to comparable EU countries, the Financial Administration of the Czech Republic shows an extreme level of utilisation of its employees due to routine administration of tax accounts kept in the IS ATIS at the expense of taxpayer support and control activities. According to an analysis published by the Financial Administration of the Czech Republic, this is one of the direct consequences of the obsolescence and lack of user-friendliness of the IS ATIS. According to that analysis, the lack of user-friendliness and the associated low efficiency of working with this information system is one of the causes of the dissatisfaction of employees of the Financial Administration of the Czech Republic with their daily work with this information system. Not even a significant, approximately one-fifth, increase in the average salary of employees of the Financial Administration of the Czech Republic compared to the average salary in the Czech Republic in the years 2013-2017 thus did not prevent a very significant increase in the fluctuation of the employees of the Financial Administration of the Czech Republic from a 3.3% fluctuation rate for 2013 to a 9% fluctuation rate for 2017.

The audit focused, inter alia, on the strategic and project management of information support for tax administration and the award of public contracts for the development of the IS ATIS, including, for example, the implementation of control reporting and electronic register of sales.

The SAO concluded that the funds for the operation and further expansion of the outdated IS ATIS had been spent ineffectively, uneconomically and inefficiently. When expanding the IS ATIS with the electronic register of sales and other application components, the GFD did not respect the rules for approving ICT projects by the main eGovernment architect. The GFD deepened the dependence on the existing supplier of the IS ATIS and unjustifiably opted for non-competitive procedures for the award of public contracts worth over CZK 400 million. In this way, the GFD acquired information technology worth approximately CZK 70 million, which could have been provided using the already acquired hardware.

1. Funds for the acquisition of software for the information support of the electronic register of sales in the amount of CZK 63 million were spent by the GFD in violation of legal regulations

The GFD was preparing the development of the software part of the electronic register of sales (hereinafter EET) in cooperation with a state-owned enterprise for about one year. That enterprise was supposed to deploy the developed software and operate it within a separate information system of EET. However, the GFD eventually withdrew from the

cooperation and provided the information support of EET through the IS ATIS supplier in the form of the supply of new application components for both the IS ATIS and the new separate IS. **The award of this public contract was contrary to the Public Procurement Act, as the GFD awarded it in a negotiated procedure without prior publication (hereinafter the “NPWPP”) although the conditions for its use were not fulfilled, thereby increasing the dependence on the supplier of the IS ATIS.** The funds spent on the cooperation with the state-owned enterprise in the amount of CZK 2.9 million and the unauthorised use of the NPWPP in the case of a contract in the amount of CZK 60.5 million were assessed by the SAO as a breach of budgetary discipline. **In addition, the GFD implemented this solution without obtaining a positive opinion from the main eGovernment architect,** who approves significant ICT projects of public administration before spending any funds.

2. The GFD, in the public contract, limited the range of potential suppliers of standard hardware products by specifying the products of the current IS ATIS supplier

The GFD violated the principle of non-discrimination when expanding the IS ATIS infrastructure for the needs of the electronic register of sales. **The supplier of the IS ATIS decided on the participation of potential bidders for the public contract for the expansion of the IS ATIS infrastructure in an open tender,** since the GFD had unjustifiably made the performance of this public contract (hereinafter the “PC”) subject to the provision of IS ATIS specialists authorised by the IS ATIS supplier. Furthermore, the GFD specified in the tender documentation the required hardware products by indicating specific products of the IS ATIS supplier. The SAO assessed such spending of funds in the total amount of CZK 186 million as wasteful (resulting in a breach of budgetary discipline). According to the SAO findings, **the GFD, as part of the public contract, purchased, for example, optical transceivers at a unit price of 2.62 times the price for which another public-sector entity purchased the same components at about the same time.**

3. The GFD did not use XML accelerators, acquired for the electronic register of sales for CZK 33 million, of which CZK 22 million was spent ineffectively for four out of six of the acquired accelerators, efficiently

The GFD acquired six identical XML accelerators under the PC for the expansion of the IS ATIS infrastructure for the needs of the newly built information system *Transaction parts of the electronic register of sales*. According to the results of a stress test of this information system, **only two would have been sufficient to ensure its projected performance. Therefore, the other four were purchased by the GFD ineffectively,** which is evidenced, among other things, by the monitoring of the peak use of the transactional performance of all six XML accelerators.

They were used, at peak times between the start of the operation of EET (i.e. December 2016) and the end of July 2018, at no more than 6.08 % of their transactional performance.

4. The GFD inefficiently used a pair of servers purchased for EET for CZK 48 million. At the same time, their acquisition was ineffective, as the required computing power could have been ensured by the GFD by activating the unused installed capacity of already operated servers

In July 2016, the GFD acquired two identically powerful servers, which can be equipped with up to 160 processor cores, for the expansion of the IS ATIS infrastructure under the PC. However, until the end of July 2018, the GFD used, on a long-term average, only two-thirds of the performance of a single processor core of the first of those servers, and only less than a fifth of the performance of a single processor core of the second server. After the end of the agreed annual hardware support for the servers, the GFD paid CZK 6.59 million per year for their after-warranty hardware support, i.e. more than CZK 824 thousand for each GFD-documented after-warranty servicing, such as “*optical cable reconnection*”. The GFD spent funds on the acquisition of the servers ineffectively, as it did not provide the necessary computing power by utilising the previously installed but unused computing power of the servers already operated.

5. The development and maintenance of the IS ATIS were uneconomical and in conflict with the law

The GFD wrongly awarded public contracts for the provision of information support for the control report and the special regime of one stop shop (the so-called Mini One Stop Shop, hereinafter also “MOSS”) in the form of a NPWPP, as the conditions for the application of the NPWPP were not met. The SAO therefore assessed this conduct as a breach of budgetary discipline, in the amount of CZK 79.3 million for the public contract related to the acquisition of the control report and another CZK 99.9 million for the public contract related to the acquisition of MOSS. According to the SAO’s findings, the GFD also acted uneconomically and in breach of the law as, based on IS ATIS post-warranty service contracts, the GFD did not exercise any claim for contractual penalties related to the limitation of the IS ATIS availability. The SAO also found that selected legislative changes had been incorporated into the IS ATIS by the GFD with a delay. The development of the IS ATIS by the GFD was not based on an information concept that is mandatory by law for almost seven years. The GFD did not implement the objectives set out in the *Public Administration ICT Service Development Strategy* in its strategic management.

6. The actual implementation costs of the *E-sales* project including its ICT infrastructure exceeded the costs reported by the GFD by at least CZK 71 million

The GFD paid for the construction of the infrastructure of EET from the funds of the asset reproduction programme, the specification of which does not include any information on EET. Due to the GFD having failed to update the documentation under the funding of EET under that programme, the individual actions could not have contributed to the fulfilment of the specified objective of the entire programme, which the SAO assessed as a breach of Section 5(1) of Decree No. 560/2006 Coll.

The GFD reported a total cost of implementing the *E-sales* project in the amount of CZK 366 million in the project completion report. However, the GFD did not include the related costs of operating the hardware part of the *E-sales* project amounting to at least CZK 71 million. During the project implementation, management of the project by a project manager was not provided for almost two months. The position of finance manager with an unambiguous responsibility for project financing was set up by the GFD only in the phase of technical implementation of the *E-sales* project after the so-called budgetary committee had fulfilled

this role. **The MF did not proceed economically as, instead of engaging its own department (Project Office), it spent money on the services of a private company.**

7. The introduction of the information support for the receipt lottery was in accordance with the law

To make the communication operational, it was necessary to ensure communication between the receipt lottery system and the IS ATIS application components EET. The MF purchased this information support, for which it expended CZK 15.5 million until the end of this Audit, in accordance with the law.

Based on the identified shortcomings in the information support of the tax administration agenda, the **SAO recommends to:**

- Reduce the IS ATIS development costs, with the exception of the most urgent implementation of changes in legislation, and concentrate both human and financial resources on the fastest possible introduction of a new information system to support the tax administration agenda;
- Follow the architectural principles of the national architecture of the public administration of the Czech Republic in any further expenditure on information support of the tax administration agenda, namely follow the principle of technological neutrality through the independence of the chosen ICT solution;
- In providing information support to the tax administration agenda, make full use of the already acquired ICT infrastructure and, when acquiring new components, choose those that will be optimally utilised in the shortest possible time and with reasonable cost-effective support (maintenance);
- In the concluded contracts, consistently specify sanctions for any breach of the guaranteed availability of the existing and new information systems to support the tax administration agenda so that these sanctions can be enforced against the performance supplier.

II. Information on the audited area

The **MF** is an organisational unit of the state and a central state administration body, which is also responsible for preparing legislation in the tax administration agenda. The MF was also the initiator of the introduction of the control report and the project of EET, in which the MF employees were involved through their participation in the project team, e.g. in the project management committee, in the legislation team, in the PR and communication team and in the expert team. The MF is the administrator of asset reproduction programmes under which the information support to the tax administration agenda is financed. In 1993-2010, the MF was also the administrator of the IS ATIS.

The **GFD** is an organisational unit of the state. The Financial Administration of the Czech Republic consists of the GFD, the Appellate Financial Directorate, 14 tax offices, the Specialised Tax Office and local offices. Since 2011, the GFD has also been the administrator of the IS ATIS, which is used by the Financial Administration of the Czech Republic as a basic tool for supporting the tax administration agenda. This information system is used by more

than 14 thousand employees of the Financial Administration of the Czech Republic who deal with the tax administration agenda. Among other things, the GFD participates in the preparation of draft legal regulations related to the tax agenda, as well as the provision of analytical and conceptual services. Taking into account all legislative changes and tasks of the GFD in the IS ATIS is very laborious and expensive, as this information system is mainly created in an obsolete programming language dating back to the late 1980s and early 1990s.

In connection with the reorganisation of the Financial Administration of the Czech Republic, the GFD assumed responsibility for adapting the IS ATIS to its new organisational structure and subsequently for further modifications and expansions of this information system, such as information support for control reports, Mini One Stop Shop and EET, as of 1 January 2013.

The control report was introduced as a means of detecting tax evasion and fraud. Its aim and purpose was to enable the tax administrator to obtain information on selected transactions carried out by VAT payers and, in conjunction with other data, identify risk associations of persons drawing funds illegally from the public budget. As of 1 January 2016, selected entities were obliged to provide data from tax documents that were already required by law to be recorded. These data were to be reported in a control report based on tax documents issued and received (including simplified tax documents) and other documents on the delivery of goods or the provision of services. The institute of the control report was introduced by Act No. 360/2014 Coll., amending Act No. 235/2004 Coll., on Value Added Tax, as amended, and other related acts.

The MOSS application was created for providers of selected services (electronically supplied services, telecommunications services, broadcasting services) who provide services to customers from the European Union and who, thanks to this application, do not have to register for VAT in each country of their customers. MOSS is designed for tax entities based in the Czech Republic, the European Union and beyond. The basic legislation for MOSS in the Czech Republic is Act No. 235/2004 Coll., on Value Added Tax, as amended.

The first attempt to record sales in the Czech Republic was initiated by Act No. 215/2005 Coll., on Cash Registers and on Amendments to Certain Acts (the Cash Register Act), which had been in preparation since 1999. This act obliged taxpayers to operate certified cash registers with fiscal memory as of January 2007. This obligation was abolished by Act No. 261/2007 Coll., on the Stabilisation of Public Budgets.

In the Government Declaration of February 2014, the MF priorities included measures necessary to improve the efficiency of tax and customs collection and prevent abuse and circumvention of tax legislation through EET. The preparation and implementation of EET in the Czech Republic was officially launched by the MF on 1 January 2015 through a project called E-sales. The project involved the MF, the GFD and a state-owned enterprise. The managing authority of the project was a Steering Committee, composed of representatives of the MF, the GFD and the state-owned enterprise. The basic legal regulation for the electronic register of sales in the Czech Republic is Act No. 112/2016 Coll., on Registration of Sales.

Information and communication technologies (ICT) are used in developed countries as a useful tool for increasing the efficiency and user friendliness of state services. The key tool for increasing efficiency is the use of ICT to reduce the administrative burden on public administration employees while using the capacity thus released to increase the state's user friendliness. The structure of utilisation of employees for administration and other activities in the Financial Administration of the Czech Republic, after more than twenty years of expanding the IS ATIS, and the same indicators in tax administrations of some comparable European countries (headed by Estonia as the European leader in the development of electronisation of public administration and e-government) can be seen in the international comparison prepared by the OECD (Table 1).

Table 1: Selected activities of the employees of the Financial Administration of the Czech Republic in 2015

State	Account management and other tax-related acts	Tax audit and other audits	Recovery and appeal	Taxpayer support	Other support
Czech Republic	55.6 %	20.2 %	7.2 %	4.3 %	12.7 %
Estonia	10.1 %	41.7 %	5.2 %	28.3 %	14.7 %
Austria	7.4 %	52.6 %	7.7 %	18.7 %	13.6 %
Belgium	4.7 %	38.2 %	18.1 %	28.6 %	10.4 %

Source: OECD, *Tax Administration 2017 – Comparative Information on OECD and Other Advanced and Emerging Economies* (see https://www.oecd-ilibrary.org/taxation/tax-administration-2017_tax_admin-2017-en).

Further expansion of agendas of the Financial Administration of the Czech Republic, e.g. with the preparation of control reports or the introduction of EET, according to the reports on the activities of the Financial Administration of the Czech Republic, was associated with the increase in the number of its employees in 2013-2017 (see Table 2).

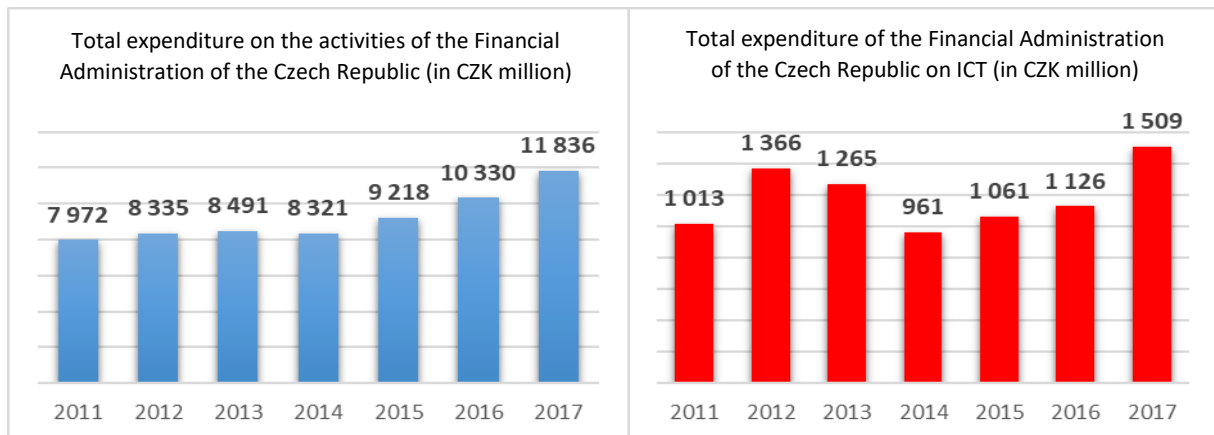
Table 2: Development of key indicators of economy and efficiency of the Financial Administration of the Czech Republic

Indicator/year	2013	2014	2015	2016	2017
Number of employees of the Financial Administration of the Czech Republic	14,919	15,015	15,252	15,273	15,448
Average salary in the Financial Administration of the Czech Republic/average wages in the Czech Republic	97.9 %	98.6 %	103.5 %	111.9 %	118.5 %
Fluctuation rate of employees of the Financial Administration of the Czech Republic	3.30 %	4.70 %	7.30 %	8.40 %	9.00 %
Expenditures per CZK 100 of adjusted revenues	CZK 0.97	CZK 0.88	CZK 0.94	CZK 1.00	CZK 1.07

Source: *Report on the Activities of the Financial Administration of the Czech Republic for 2017*; the ratio of average salaries in the Financial Administration of the Czech Republic and wages in the Czech Republic calculated according to data from the information system on average earnings (see <https://ispv.cz>).

The total expenditure on the activities of the Financial Administration of the Czech Republic increased from 2011, except for 2014. The total expenditure for 2017 thus increased by 48 % compared to 2011 (see Graph 1).

Graph 1: Expenditure of the Financial Administration of the Czech Republic on activities and ICT in 2011-2017



Source: reports on the activities of the Financial Administration of the Czech Republic.

In preparation for the introduction of a new information support to the tax administration agenda instead of the IS ATIS, the GFD announced, in September 2017, a public contract entitled *Services of the provision of project, process and architectural management, including the preparation of variant solutions to the change of the Tax Information System*, on the basis of which a framework agreement on the provision of services was concluded on 12 November 2018, totalling CZK 83 million. At the time of the audit, the GFD stated, concerning the new information support of tax proceedings, that the period of performance of Part I of the PC, i.e. the preparation of proposals for variant solutions to the new tax information system for the support of tax proceedings, had been extended from 7 to 12 months. Compared to the schedule set in the tender documentation, the compliance with the date of completion of Part I of the public contract as of 31 October 2018 was not realistic at the time of the audit. The performance will therefore be delayed. The execution of the public contract, i.e. the handover and acceptance of the new information system to support the tax administration agenda, was supposed to be completed on 30 June 2021. The main eGovernment architect of the Ministry of the Interior made its approvals of the implementation of certain projects for further expansion of the IS ATIS in its original form conditional on the completion of that public contract as of the aforesaid date.

Note: The laws and regulations cited in this Audit Conclusion apply as amended for the period under review. All the amounts given in the text of the Audit Conclusion are inclusive of VAT unless otherwise stated.