

# Internal Audit Report

## Verification of the Validity of Supplier VAT Registration Numbers.

### Business Management

April 2019

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<b>For Action</b>		
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**Wirral Internal Audit Service**

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# **1. Executive Summary**

- 1.1 In February 2019, Internal Audit was commissioned to evaluate the existing controls in operation regarding the validity of VAT registration numbers on Council suppliers invoices; and whether there are any current statutory or mandatory requirements imposed by HMRC on commissioning organisations.
- 1.2 The conclusions reached from the review are that:
  - 1.2.1 The current system of inputting VAT registration numbers from information provided by the supplier is the system employed by the majority of Councils throughout the North West of England area and, as there are no statutory requirements placed on the Council to verify the registration number, satisfies HMRC's requirements.
  - 1.2.2 Discussion with the HMRC confirmed that the Council is not duty bound to verify suppliers' VAT numbers but is required to report anyone suspected of committing VAT fraud directly to HMRC.
  - 1.2.3 Advice and guidance received by professional bodies is consistent with this approach.
  - 1.2.4 A number of actions have been identified in this report for consideration by senior managers that would further strengthen control arrangements in this area.

## 2. Introduction

2.1 In February 2019, Internal Audit was commissioned to evaluate the existing controls in operation regarding the validity of VAT registration numbers on Council suppliers invoices and whether there are any current statutory or mandatory requirements imposed by HMRC on commissioning organisations.

2.2 The aims of this audit review were to assess:

- Whether existing controls in this area are effective and comply with current best practice particularly with regard to checking the validity of supplier VAT registration numbers contracting with the Council;
- Whether it is necessary for the Council to introduce any additional controls to reduce the risks in the future of VAT being claimed incorrectly as a result of an invalid VAT number being provided by a company on their supplier invoice.

## 3. Audit Objective and Scope

3.1 The purpose of the report is to provide the Director of Governance and Assurance with the findings and recommendations resulting from the audit review of the documentation, assessment of existing processes and the discussions held with relevant officers.

3.2 The report focuses on the Verification of the Validity of Supplier VAT Registration Numbers and has involved discussions with relevant officers, evaluation of systems procedures and the review of appropriate documentation relating to internal processes and procedures. Outcomes and actions arising from the work are identified at section 4.

## 4. Findings

### 4.1 Current Procedures

4.1.1 The Supplier Creation / Amendment procedure is well established. Within the procedure notes it states that when creating a new supplier, '**All fields** [on the new supplier form] must be completed **including VAT number**, telephone & fax numbers, e-mail addresses etc.'

4.1.2 Under the section 'Validating a New Supplier' it states that '**all the information must be checked** and amended if incorrect' but this does not specifically mention validating the VAT number.

4.1.3 As well as the Supplier Creation / Amendment procedure, there is a 'New Supplier Form' to complete. This form requires a VAT registration number to be included (where applicable) for the supplier and is marked with an asterisk symbol denoting that completion of the box is compulsory. The form does not, however, state that a validity check should be made on the VAT registration number.

### 4.2 Advice from the Council's VAT Officer

4.2.1 Contact was made with the VAT Officer to ascertain whether there was any statutory or best practice obligation for the Council to check the VAT numbers of the companies that we (the Council) deal with either before a first payment is made or on an ongoing basis,

or is the fact that there is a VAT number provided enough to justify payment of the invoice with 'no questions asked'.

4.2.2 The reply received stated categorically that there is no actual legal requirement for the Council to verify the VAT registration number of a supplier before we conduct any business with them. The VAT Officer stated, however, that it may be viewed as "good housekeeping" to do so, but that given the size of the Councils supplier database it may not always be possible or practicable. This was confirmed by HMRC – see 4.6 below.

#### **4.3 What other Local Authorities in the area are doing.**

4.3.1 Internal Audit have contacted local Councils across the North West and established that the type of checks referred to in 4.2.2 are not common practice in these organisations. We are however aware that colleagues at one Council are about to start checking the validity of VAT numbers on the suppliers that they have on their preferred suppliers list and there are plans to introduce the verification requirement to all suppliers on an ongoing basis.

4.3.2 Enquiries made with colleagues within the Mersey Regional Fraud Group area found that only two of the 10 authorities verify new suppliers' VAT numbers only, with one of those two currently looking for additional resource to verify all suppliers' VAT numbers on a regular ongoing basis.

#### **4.4 Private Sector Organisations Checks**

4.4.1 Contact was made with the Confederation of British Industries (CBI) via email from their website. As at 26 March 2019, no reply has been received. Having contacted the CBI again on 1 April it was not possible to speak with anyone within the organisation to obtain an answer.

4.4.2 The 'VAT People' an organisation that provides specialist guidance for business were contacted to confirm what advice and guidance they currently provide to businesses regarding undertaking routine checks to confirm the validity of VAT registration numbers. They advised that they merely suggest that companies contact HMRC directly to confirm whether VAT registration numbers are valid if a problem is identified. Internal Audit have contacted HMRC directly and include their feedback at 4.6 below.

#### **4.5 Advice from Professional Financial Bodies**

4.5.1 Contact was made with the Chartered Institute of Public Finance Accountants (CIPFA) using our member's account and a reply advising that the query has been passed to CIPFA's VAT Committee for discussion/debate at a forthcoming meeting was received on 22 March 2019. Having made further enquiries, the next meeting of the CIPFA VAT Committee is not scheduled until 6 July 2019.

4.5.2 In response to a post on the CIPFA VAT Forum regarding this matter the advice was that if, having contacted the supplier and not received a valid explanation for the VAT number being invalid, the Council should refer the supplier to HMRC using the usual channel i.e. via the Customer Compliance Manager (CCM) – in Wirral Council's case, the VAT Officer. This reply was posted by a member of the CIPFA VAT Committee.

4.5.3 The advice from the Association of Accounting Technicians (AAT), through their partner company Croner Business Support, was not specifically for an organisation to undertake

any ongoing routine checks but to notify HMRC immediately if an invalid VAT number was encountered.

#### **4.6 Advice from HMRC.**

4.6.1 Contact was made with HMRC via their online help facility and the webchat identified a due diligence leaflet that offers the following advice:

- Taxable persons should not undertake due diligence and risk assessments just to satisfy HMRC but to help ensure that the business is managed effectively and to ensure the integrity of their supply chains. The due diligence and risk assessments should be reasonable and proportionate.

4.6.2 This due diligence leaflet has links to VAT Notice 726 (Joint and several liability for unpaid VAT) which gives ideas as to how to verify VAT numbers. Notice 726 suggests that an existing business should **consider** whether it is appropriate to:

- obtain copies of certificates of incorporation and VAT registration certificates;
- verify VAT registration details with HMRC; and
- check details provided against other sources, for example website, letterheads, BT landline records.

4.6.3 Notice 726 goes on to state that *'In each case, HMRC will be seeking to identify what actions or precautions you took in response to any indicators of risk. This will focus on the due diligence checks you undertook and, most importantly, the actions taken by you in response to the results of those checks'*.

4.6.4 In answer to the direct question of 'does the person paying for the suppliers' services need to verify the VAT numbers of those suppliers?' the answer was categorically 'No'.

4.6.5 Once registered for VAT purposes with HMRC, the supplier must ensure that their tax arrangements with HMRC are correct. Any failure to comply is the sole responsibility of the supplier and not any other third party organisation engaging their services, such as a Local Authority. It will be the HMRC who will take action against any supplier over any issue relating to VAT.

#### **4.7 Verification of VAT numbers of current Suppliers**

4.7.1 A management report has been prepared as part of this review identifying a total of 15,391 current suppliers. Of these, 3,395 have what is considered to be a genuine VAT number.

4.7.2 A sample of 34 (1%) was tested by Internal Audit from the 3,395 and VAT numbers tested by using the VIES (VAT Information Exchange System) website. Of the sample, 6 of the 34 were found to not be a valid VAT number. One of the six was found to be as a result of input error and so can be discounted. Consequently five entries from the sample tested (14.7%) are unverified VAT numbers. The reason that they are unverified can be varied, including:

- the companies may have legitimately re-registered with HMRC and been given a new VAT registration number that they have failed to notify us;

- the companies may have merged into a business group and be operating under a group VAT registration number and failed to notify us of that;
- the companies may have left a business group and no longer be operating under a group VAT registration number and failed to notify us of that; and
- there could be other valid explanations.

#### **4.8 Council's VAT Position in relation to companies with invalid VAT numbers**

4.8.1 From discussion with the VAT Officer it is acknowledged that the Council have accepted VAT invoices from suppliers in good faith and paid those invoices accordingly. If it is subsequently found that VAT numbers quoted are invalid it is not the fault of the Council.

4.8.2 The VAT Officer for the Council will make some further enquiries relating to the suppliers with invalid VAT numbers identified during this audit and discuss his findings with HMRC, confirming that this is the only way to identify when the VAT numbers become invalid and whether any VAT corrections are required. Advice received from HMRC states that corrections may not necessarily be required as the Council would likely not be judged to have acted incorrectly and therefore not be liable for repayment of any VAT reclaimed.

## 5. Conclusion

- 5.1 The current system of inputting VAT registration numbers from information provided by the supplier is the system employed by the majority of Councils throughout the North West of England area and, as there are no statutory requirements placed on the Council to verify the registration number, satisfies HMRC's requirements.
- 5.2 Discussion with the HMRC confirmed that the Council is not duty bound to verify suppliers' VAT numbers but is required to report anyone suspected of committing VAT fraud directly to HMRC.
- 5.3 An HMRC VAT Notice suggests that a business may want to consider obtaining prima facie and third party evidence to satisfy itself that the VAT registration number is valid.
- 5.4 Contact with the Chartered Institute of Public Finance Accountants (CIPFA) produced no response to date but, having posted a question on their VAT Forum, the advice was to report the invalid number to HMRC. Similarly, advice from the Association of Accounting Technicians (AAT), through their partner company Croner Business Support, was not specifically to introduce checks on suppliers but to merely notify HMRC immediately if an invalid VAT number is identified.
- 5.5 The 'VAT People', a private sector organisation providing specialist guidance for business confirmed that advice currently provided by them was for companies to merely contact HMRC directly to confirm if VAT registration numbers are valid if a problem is identified. No recommendation is provided by them for businesses to undertake routine checks.
- 5.6 During the review a sample of 34 suppliers (1%) was evaluated by Internal Audit from the 3,395 utilised by the Council and VAT numbers tested by using the VIES (VAT Information Exchange System) website. Of the sample, six of the 34 were found to not be a valid VAT number. One of these six was found to be as a result of input error and so can be discounted. Consequently five entries from the sample tested (14.7%) are unverified VAT numbers. The VAT Officer is making enquiries into these and may contact HMRC to discuss the cases if issues are found.
- 5.7 In light of the above the Council should consider undertaking a cost/benefit analysis to determine whether it would be appropriate to undertake some form of regular checks to validate Supplier VAT Registration Numbers. These due diligence checks may take the form of:
- Checking the validity of VAT registration numbers for all new supplier accounts and when an existing supplier makes a change to their details, such as the company bank account by:
    - obtaining copies of certificates of incorporation and VAT registration certificates;
    - verifying VAT registration details with HMRC; and
    - checking details provided against other sources, for example website, letterheads, BT landline records.
  - Undertaking spot checks to ensure that VAT registration numbers quoted on supplier invoices are valid and retaining evidence of such checks for future reference.

## **6. Next Steps**

- 6.1 Many thanks for the pro-active and assured steps taken during the end of audit process.
- 6.2 It is acknowledged that, in advance of issuing the report as final, you have taken the very positive step in formulating an achievable plan for implementing the recommendations; and this is reflected for reference within Section 7.
- 6.3 Please ensure your 'Plan for Implementation' is progressed in-line with the 'Expected Implementation Date' as detailed in Section 7.
- 6.4 Please ensure that I am kept updated of your progress in implementing the recommendations.
- 6.5 Internal Audit will undertake a follow-up audit within four months of the date of this report, so as to obtain evidence of your progress in implementing the recommendations. If you have not implemented recommendations within a reasonable timescale, the Audit and Risk Management Committee and Chief Executive will be notified. It is likely that you will be asked to attend the Committee to explain your reasons for this.
- 6.6 Your feedback is very important to us. Please complete the Customer Feedback form in Section 8, and return this with your completed report. We may contact you to discuss this.
- 6.7 Thank you for your help and co-operation during the audit. Please contact Mark Niblock if you wish to discuss the report further.

## 7. Action Plan - Recommendations

	Recommendation	Priority Level	Agreed Y/N	Plan for Implementation	Expected Implementation Date	Name of Responsible Officer
1.	<p>The Council should consider undertaking a cost/benefit analysis to determine whether it is appropriate to undertake regular checks to validate Supplier VAT Registration Numbers. These due diligence tests may take the form of:</p> <ul style="list-style-type: none"> <li>• Checking the validity of VAT registration numbers for all new supplier accounts and when an existing supplier makes a change to their details, such as the company bank account by: <ul style="list-style-type: none"> <li>○ obtain copies of certificates of incorporation and VAT registration certificates;</li> <li>○ verify VAT registration details with HMRC; and</li> <li>○ check details provided against other sources, for example website, letterheads, BT landline records.</li> </ul> </li> <li>• Undertaking spot checks to ensure that VAT registration numbers quoted on supplier invoices are valid and retaining evidence of such checks for future reference.</li> </ul>	<p>Low (A matter that requires attention and would improve the system under review)</p>	Y	<p>Checks on the validity of VAT registration numbers for all new supplier accounts and when existing suppliers make a change to their details will be made.</p> <p>If an invalid VAT number is found, the supplier will be contacted to ascertain the reason for this. Once a satisfactory explanation and relevant evidence is provided the supplier will then be added. If an explanation or relevant evidence is not provided, the supplier will not be added or in the case of existing suppliers, removed until such time as the explanation or evidence is provided.</p> <p>Spot checks for the validity of VAT numbers will be</p>	1 May 2019 following a revision of current forms to include the new necessary information/checks	Shaer Halewood / Phil McCourt.

	Recommendation	Priority Level	Agreed Y/N	Plan for Implementation	Expected Implementation Date	Name of Responsible Officer
				added. Internal Audit advice will be sought as to the frequency and number of these.		
2.	The Council should consider whether it is appropriate and cost effective to undertake checks on the whole suppliers' database to verify the validity of the 3,395 VAT numbers currently identified.	Low (A matter that requires attention and would improve the system under review)	Y	As HMRC guidance specifies that spot checks should be undertaken and this has been agreed, this recommendation will not be implemented. It is the responsibility of the supplier to ensure VAT numbers are valid and the level of resource precludes the Council from undertaking this task.	Will not be implemented.	Shaer Halewood / Phil McCourt
3.	The Council should report contractors where invalid VAT numbers are identified to the VAT Officer for investigation and possible reporting to HMRC for further investigation by them.	Medium (A matter that is significant to the system under review)	Y	Once the Council's VAT Officer has identified the reasons for the invalid VAT numbers, if any reason provides cause for concern these will be reported to HMRC for their further investigation.	Immediate, currently ongoing.	Shaer Halewood / Phil McCourt

## 8. Customer Feedback

<p align="center"><b>How satisfied were you with the overall service received from Internal Audit? (please ✓ to indicate)</b></p>							
<p><b>Very Satisfied</b></p>		<p><b>Satisfied</b></p>		<p><b>Dissatisfied</b></p>		<p><b>Very Dissatisfied</b></p>	
<p align="center"><b>Please provide any additional comments:</b></p>							

If you would like to discuss any aspect of this audit, please contact the Chief Internal Auditor.

Completed by: ..... Signed: ..... Date: .....