HOUSE OF COMMONS

Public Accounts Committee

Oral evidence: HMRC Annual Report and Accounts 21-22, HC 686

Thursday 20 October 2022

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[Watch the meeting]

Members present: Dame Meg Hillier (Chair); Olivia Blake; Sir Geoffrey Clifton-Brown; Mr Louie French; Peter Grant.

Questions 1 – 125

Witnesses

I: Jim Harra, Chief Executive and First Permanent Secretary, HM Revenue and Customs; Angela MacDonald, Deputy Chief Executive and Second Permanent Secretary, HM Revenue and Customs; Justin Holliday, Chief Finance Officer, HM Revenue and Customs; Jane Whittaker, Director for Knowledge, Analysis and Intelligence, HM Revenue and Customs.

Gareth Davies, Comptroller & Auditor General, National Audit Office, Adrian Jenner, Director of Parliamentary Relations, National Audit Office, and David Fairbrother, Treasury Officer of Accounts, HM Treasury, were in attendance.

HOUSE OF COMMONS

Report by the Comptroller and Auditor General

HM Revenue & Customs 2021-22 Accounts (HC 494)

Examination of witnesses

Witnesses: Jim Harra, Angela MacDonald, Justin Holliday and Jane Whittaker.

Q1 **Chair:** Welcome to the Public Accounts Committee on 20 October 2022. Today we are talking to His Majesty's Revenue and Customs, looking at their annual report and accounts for the financial year 2021-22.

Congratulations, first, that we have them to look at, because it has been a challenging time to catch up on accounts because of Covid. Thanks to our colleagues at the National Audit Office as well for that. HMRC brought in record revenue in the year of 2021-22 at £731 billion. Of course, that is partly due to the backlog because of Covid at the start of the pandemic. We will be asking you about that. We also want to touch on a number of other issues in the annual report, which will become apparent as we go through our questions.

I would like to welcome our witnesses today. We have Jim Harra, the chief executive and first permanent secretary at HMRC; Angela MacDonald, who is the deputy chief executive and second permanent secretary and deals with customer service; Justin Holliday, the chief finance officer; and Jane Whittaker, who is the director for knowledge, analysis and intelligence. I think it is your first time in front of us, Ms Whittaker.

Jane Whittaker: It is, yes. Thank you for having me.

Chair: Welcome to the Public Accounts Committee. Just answer our questions and we will love you to bits. It is very simple. Before I go any further, I would like to ask members if they have any interests to declare.

Mr French: Good morning. Just for transparency purposes, I was previously a councillor during the pandemic and was partly responsible for the business support schemes in my local council.

Olivia Blake: I probably was a councillor at the beginning of the pandemic, but I resigned very soon into that.

Q2 **Chair:** Just for clarity, that is good. Before we go into the main session, Mr Harra, I just wanted to ask you about the challenges. When we last spoke, you were modelling a 20%, 30% and 40% reduction in headcount. We now have another new Chancellor, with talk about efficiency savings being modelled in Departments. What are you looking at in your Department in terms of numbers, given that you actually bring money in if you have the right resource in the right place? What is the guidance you are getting and what are you working on at the moment?

Jim Harra: As things stand, we still have our budgets that were set at the spending review 2021. We are continuing with the plans that we have based on those budgets. You are right that in June all Departments were challenged to come up with plans that could reduce the size of the Civil Service back to 2016 levels by 2025. In the case of HMRC, our SR21 plan already brings us back to 2016 levels by then. At a departmental level, we met that objective. However, like all Departments, we did do work for July about what the different options were, which we submitted like other Departments. No decisions have been made on that. We wait to hear if the Government have any changes that they want to make to their spending plans this side of 2025 and also what their longer-term spending plans might be.

My view for HMRC is we will make efficiencies wherever we possibly can. We have investment to do that. The key way of making efficiencies, apart from continuous improvement, is to continue digitalising the tax system and making sure that customers do not have to contact us by the older methods of phone or post but increasingly can self-serve online or can be supported by digital assistance or robotics. That is the key way of continuing to deliver our services with less resource over time. We will obviously respond to any challenge that we get from the Government around our spending.

Q3 **Chair:** You will presumably have some idea before 31 October; you will be given an indication of whether there is going to be an announcement about your budget by then.

Jim Harra: Yes, we wait for it and, as you might expect, Justin in particular has been leading work in the meantime about what it is we might be able to do. That is really based on what we did for July. From our point of view, there are no new breakthroughs since July.

Q4 **Chair:** We have been talking to you for a long while about some of the changes and efficiency programmes. We know that they take some time to deliver. When you say you are trying to find efficiencies where you can, would you like to quantify what efficiencies you could possibly find between now and, say, the end of this financial year? Realistically, it is not going to be very much, is it?

Jim Harra: Realistically, between now and the end of this financial year, no, it is quite difficult.

Chair: It is good to get that clear.

Jim Harra: It is quite difficult to deliver any further efficiencies other than what is already planned. We have been looking at whether we can go further by 2025. In particular, we have investment for the single customer account, which is a single online account for customers we are looking at how we can prioritise reforming and digitalising the income tax and national insurance processes, in particular, which drive a lot of contact from customers that could be handled online, with digital assistance or through contact, where there are staff required to process it, where robotics or whatever could automate that. There should be scope for us to go further if that is what we prioritise and get around.

Q5 **Chair:** You are going to be trimming. It sounds like the mood of Government and the financial need of the country is that will happen. You have talked a bit about prioritisation there. You are prioritising digital access for customers. What are you dropping down the list in terms of priorities?

Jim Harra: At the moment, nothing, because we have a full programme that was funded in SR21.

Chair: It is all going to be fine for HMRC.

Jim Harra: For example, if our investment funding is cut, then we will advise Ministers, depending on what their priorities are, what the projects are that they could defer and what the impact of doing that would be.

Q6 **Chair:** You are going to be looking at deferring projects rather than stopping projects.

Jim Harra: I believe in the Department's strategy and I want to achieve everything that we are trying to achieve, but it all requires money so it might take longer to do if there is less money. It all depends on what the priorities are. You are right that, in the case of HMRC, we bring in a lot more than we cost and, if your priority is fiscal consolidation, it can be a false economy to cut the Department deeper than the efficiencies that we can achieve. That is obviously something that Ministers have listened to over the years.

Chair: That is a very well-worded pitch to the Treasury, Mr Harra. I am sure they are listening.

Q7 **Sir Geoffrey Clifton-Brown:** Good morning, Mr Harra. I am sorry to pose something you probably were not expecting and I do not mind if any of your team answer this question. I am launching, on the Floor of the House, our waste crime report, and I will be featuring something on landfill tax. Given that landfill tax is the biggest tax gap as a proportion of the size of the tax, what more can you do to try to tighten up on landfill tax enforcement? The Chair has said it is in order that I can use your answer on the Floor of the House today, so I give that caveat.

Jim Harra: Obviously, we have had a recent National Audit Office Report and this Committee has looked into landfill tax. From our point of view, you are right. It is difficult to enforce. There are high levels of non-compliance and it is a physical tax, with waste moving at a particular point in time. As you know, we had a major criminal investigation operation, which did not result in prosecutions because of evidential difficulties. We have learned lessons from that.

We have not at all given up on using criminal investigation and prosecution where that is the best way of achieving compliance but, as you know, as is the case across the tax system, we have a range of civil powers available to us as well and we use those. We work very closely with the Environment Agency and its counterparts in other parts of the UK, because this needs to be a multi-agency approach.

We also, in recent years, have extended landfill tax to illegal waste sites as well, which has pushed up the tax gap, because that is an area where inevitably you are going to have a high level of non-compliance, but that gives us an extra lever with which to tackle the people who fly-tip in that way, because imposing a financial liability on them through tax is just an extra way of managing the behaviour. Although it has a perverse effect on the tax gap because it pushes it up, that is an important reform in terms of helping the country tackle waste crime.

Q8 **Sir Geoffrey Clifton-Brown:** Given that you have told us in the past that this is not particularly a tax-raising exercise—it is more a compliance exercise—given the exchanges you have just had with the Chair about possible resources and priorities, can we assume that your priority is still trying to close that tax gap and work in this area?

Jim Harra: Yes, it is, for two reasons. First of all, although landfill tax does raise revenues, the key objective of that tax is to encourage reuse and recycling. It will only work to achieve that objective if it is paid. It will not have that effect if it is evaded. Therefore tackling that evasion is important to helping the tax achieve its environmental objective, quite apart from all the criminality that is associated with it, because that criminality has a wider social effect than simply the loss of revenue. It is a priority for us. One of our key strategic objectives in the Department is not just to raise revenues but to tackle social harms for which we are responsible, and enforcing environmental taxes to achieve their environmental objectives is part of that.

Q9 **Peter Grant:** Mr Harra, I have written to HMRC on a couple of constituency cases over the last six or eight weeks, one of which involves a legitimate business in my constituency that discovered that a bogus company had used their business name and address and had managed to get a VAT registration number of their own. On the back of that, the first that my constituents knew about it was they got a letter from a debt collection agency saying that they were behind with the VAT payments.

There is clearly a lot more in that, and I appreciate it will take a while to get a substantive answer, but I wanted to ask what steps are taken by HMRC in order to confirm that a business is who they say they are. By way of comparison, incidentally, the same people tried exactly the same dodge with the tax authorities in Germany. The tax authorities in Germany refused the registration and reported it to the police as a fraud. There does seem to be a big discrepancy between the rigour that was applied between HMRC and the tax authorities in Germany.

Jim Harra: Two of our taxes in particular, VAT and, to a lesser extent, Self-Assessment, involve a quite a large amount of repayment. It is inherent in the design of the taxes. That makes them targets for organised crime; they want to access those taxes and try to get repayments. It is the case that we have seen concerted criminal attacks on both taxes in the last year with fraudulent registrations for tax. What happens is that the criminals gather sufficient data about a citizen or a business to enable them to get through our registration processes. It is an arms race. We are constantly changing our processes and our risk assessment. They are constantly changing their behaviours to try to get around it. I believe that we are effective at identifying those attacks early and adjusting to them.

Unfortunately, it has meant that, at times in the last year or so, legitimate applications for VAT registration have been delayed because of the extra steps that we have had to put in to check that. There will be a number of people around the country who will have learned that someone has registered for VAT in their name and that we have cancelled those registrations. It is just something we have to be constantly alert to and watching for the signs of. We have had attacks since April on self-assessment and also on research and development, because having closed down the attack on VAT, these people just move to the next scheme, but obviously focus on schemes where they think they can get a payment from Government.

Q10 **Peter Grant:** Given that you clearly appreciate that this is a fraud and that is why it has been done, I have to say that I am even more concerned at how difficult my constituents found it to get anybody at HMRC to see it as a problem. Maybe I will deal with that offline. My question was about what steps you take to verify when somebody writes to you and says, "This is the company that I am. Can I have a VAT number?" What steps do you take to make sure that it is actually the legitimate company that is contacting you?

Jim Harra: I have to be a bit circumspect about what operational information I give you about how we manage that, certainly in a public forum. We do take steps to validate registrations. We have a balancing act to achieve when it comes to VAT registration, because we want people who need to register for VAT to do so, or who are legitimate and wish to register for VAT to do so. We want to make that as quick and easy for them as possible, while also making the VAT system secure. We are constantly changing that. We recently changed the verification steps that we take as a way of combating this. I do not have the number at hand, but we rejected a large number of VAT registrations as a result.

Q11 **Olivia Blake:** I just wanted to ask a couple of questions about enterprise zones. Obviously, at the moment a week is a long time in politics, so I am just wondering if the new Chancellor has a different steer for you around enterprise zones and what assessment has been done of the impact on HMRC income if they were to go ahead.

Jim Harra: I cannot say what advice is given on the formulation of Government policy. Enterprise zones were announced in the growth plan, but there is a lot more detail still to be announced. HMRC and Treasury are working on that and working on advising the Chancellor and his Ministers about that. I would expect further announcements in due course. We stand ready to administer whatever incentives the Chancellor decides that he wants to introduce in due course.

Q12 **Chair:** We are not asking you to tell us advice, but there is obviously a risk that, if there are tax breaks in certain areas, people will try to exploit those. We were just talking about fraud. Presumably you are looking hard at how to build in systems so that you are not losing money.

Jim Harra: Yes, it is in the nature of incentives to get people to do things that they would otherwise not do: they want the incentive but they do not want to do the thing that they did not intend to do. Incentives are targets for abuse, whether that be organised criminal gangs just trying to fictitiously claim it or whether it be legitimate, genuine taxpayers who wish to access the incentive but push at the boundaries. In the case of any new incentive, we would give advice about how to design it effectively so that it achieves its objectives and is secure from abuse.

Q13 **Chair:** We appreciate that this policy is still being formulated. It has been announced as a headline and we will wait to see the detail, which we may want to talk to you about next time, if it is unveiled by then.

Moving on to the report and accounts, ever since these were published there have been major changes, with inflation increasing as one of the key pressures on you. That pushes up the money that is potentially owed to you. Are you factoring that into targets, in terms of what you are trying to get in terms of compliance?

Jim Harra: You are right. Inflation has two effects on us. One is that we have to absorb it in the departmental costs. Therefore, it can impact on what we can achieve with the budgets that we have. The other is that it can have an effect on people's liabilities and therefore on the amount of tax revenues that we will collect. In the case of compliance yield, there tends to be a bit of a lag between receipts and the yield; it is the nature of a lot of our compliance work that we are looking back at previous periods. Yes, we will have to look at what the impact of inflation is and make sure that we are able to distinguish between genuine changes in our performance, for example, and changes that are as a result of inflation in receipts.

Q14 **Chair:** I had predicted you might say there would be a lag, because there is truth in that. How do you work out a formula that means that you are not, for want of a better word, in simple terms, hiding away the performance issues in the inflation issues? How are you making sure that you are driving through real gains?

Jim Harra: I do not have a detailed methodological answer for you at this stage. It is the case that revenues change all the time as a result of policy decisions, changes in the economy and inflation. As you recognised in your opening remarks, we had record revenues last year. That is not all down to our brilliance as collectors. It is down to policy change and just what the economy produces.

When it comes to our compliance, generally speaking, what we are trying to do is have a baseline compliance performance that enables us to maintain the tax gap and prevent it from growing, because that is the assumption on which the Government's scorecard is based. That changes with tax revenues. You would expect that to go up and down as tax revenues go up and down, in terms of the amount that you need to recover in order to prevent the tax gap from worsening. That is the basis on which we will set the targets that we try to achieve.

Q15 **Chair:** We have had one of the most extraordinary upheavals in the economy since the Second World War. We are still experiencing upheavals, but it seems extraordinary that, even with the pandemic, there is not really a significant change to the tax gap. Can you explain that?

Jim Harra: I will bring Jane in because she is responsible for measuring the tax gap. First of all, I would say that you have to look at it over time rather than individual years. We did make some adjustments in the last tax gap measure, so we have slightly less confidence in it than we would normally have, and we will have to do some more work on that, because the pandemic has distorted the data set.

Jane Whittaker: I can give you a little more information. You are right that the overall percentage tax gap has remained constant between 2019-20 and 2020-21 at 5.1%. Of course, the amounts involved have changed because the levels of liabilities were reduced in the pandemic and therefore the total cash value of the tax gap was lower than it would otherwise have been. What the overall level disguises is that there are changes beneath that in individual tax types. We did see a decrease in the VAT gap between those two years, which was offset by increases in corporation tax, excise and income tax self-assessment tax gaps. That is what is happening beneath the surface.

Q16 **Chair:** Even with the increase in the gap in the others, the VAT balanced it out, basically.

Jane Whittaker: Exactly, yes.

Q17 **Chair:** Can you just explain that a little more in lay people's terms, because I am a bit confused?

Jane Whittaker: How we build up the tax gap is that we make estimates for each separate head of duty. To measure the VAT element of the tax gap, we compare the theoretical liability, based on actual consumption data recorded by the Office for National Statistics, with the receipts that are paid. That is quite a timely estimate based on real data. That VAT gap has reduced between 2019-20 and 2020-21. You may think that is consistent with differences in the nature of transactions that were happening over the pandemic period, for example, with a lot of online transactions and fewer face to face and cash in hand. The issue with the VAT gap is that, because it is a top-down methodology, it does not give us lots and lots of information about exactly what is driving year-on-year changes in the results that we see.

The tax gap estimates for the other heads of duty are built up in a more bottom-up way. We undertake random inquiry programmes, which is compliance activity on a random sample of cases for income tax, self-assessment and corporation tax. The results are driven by what our compliance workers find when they look at that sample of cases. The excise duty gaps are based on a top-down methodology, so actually based on observed expenditure against the receipts that we have brought in. During the pandemic period there were some changes in consumption patterns for excised goods, more off sales rather than on sales, for example, with the disruption to the accommodation and food sectors during the time of the pandemic. It is quite a complex picture beneath the headline.

Q18 **Chair:** That is the technical side behind it. In real-world terms, was it just that, because people were doing more things online, they were more compliant because it was all automated? It suggests that there was just more compliance during Covid.

Jane Whittaker: There is a mix of behaviours and economic factors across the different heads of duty, of course, so I cannot quite answer your question directly. The resulting tax gap captures both the impact of HMRC's compliance activity and the economic factors that affect the liabilities and revenues.

Q19 **Chair:** You have this less confident estimate for the tax gap because of everything that has been going on, it is fair to say. Am I misrepresenting?

Jane Whittaker: No, we have said that.

Q20 **Chair:** You looked puzzled; I thought you may be more confident than I imagined. Have you thought about having a bit of a range on what the tax gap is? Is the range wider in terms of what the tax gap will actually crystallise as?

Jane Whittaker: Because our tax gap estimate is built up of lots of separate components, in the tax gap report we talk about the confidence in each of those components, and we have published that in our report. We do not publish an overall range around the tax gap at the moment, but there are some particular factors that add to the uncertainty at the moment. One particularly is we have had to make some assumptions about the underlying level of write-offs and remissions that might happen in respect of activity during that period.

Q21 **Chair:** You have a range, do you?

Jane Whittaker: We do not actually attach a range to all of the individual estimates, but we comment on the level of uncertainty in the individual tax gap components.

Q22 **Chair:** Why do you not have a range for the uncertainty of things? On exactly the point you raised, taking that as an example, why have you made that choice?

Jane Whittaker: It is really because it is quite difficult to quote an overall range from lots of different methodologies of calculations. People sometimes ask why we do not we produce a confidence interval around the tax gap estimate. I am sorry if this is too technical. A confidence interval is a specific measurement where you base your estimates on a sample of cases, and the confidence interval reflects the level to which your sample might not be absolutely representative of the population that you are really interested in.

The difficulty is in aggregating the different ranges around different elements of the tax gap component. We have not presented an overall range in the past. On the insolvency point, in the report on measuring the tax gap we have explained the assumptions that we have made and the impact of making those assumptions. That was a particular methodological issue we had to consider for the latest year's tax gap estimate. We have set out the sensitivity associated with that set of assumptions in the measuring tax gaps report.

Q23 **Chair:** Are you confident that the tax gap has remained the same? What is your level of confidence?

Jane Whittaker: I am confident that the 2020-21 estimate is the best possible estimate we can make, given the data that is available. That is our best view at the moment. We may need to make revisions in due course in line with our standard revisions policy. We always try to make sure that the estimates we put out make use of the best available data at any point in time. Obviously, as time progresses, sometimes we get a little more data and are able to tighten up our published estimates.

Q24 **Chair:** Compliance yields are pretty important on this issue. They declined. We saw the results of the first year of the pandemic. When do you expect that compliance, Mr Harra, will be back to where it was before the pandemic?

Jim Harra: You are right. Compliance yield is the operational proxy we use for managing the tax gap, because there is the lag in measuring that plus the uncertainty. We estimate what level of compliance yield we think we would need to recover in order to maintain the tax gap. We add on top of that additional revenues that we have been given additional funding to collect, which should, all things being equal, reduce the tax gap.

If you look at the last year before the pandemic, 2019-20, we had record compliance yield. There were a couple of very large litigation cases in there that we settled. When you strip those out, the underlying yield in that year was about £32.2 billion. It went down to £30.8 billion and £30.4 billion during the two pandemic years. This year, we would like to see that go up. We are targeting ourselves to see if we can get to £36 billion. That is within the operational forecast range that my compliance group are giving me. It is right at the top of it, so it is a real challenge to deliver that.

Q25 **Chair:** How wide is your range?

Jim Harra: That range goes from about £32 billion up to about £39 billion.

Q26 **Chair:** £36 billion is what your target is.

Jim Harra: Yes, but currently our central estimate is that it is going to be a stretch to hit £36 billion, but that is what I would like to do.

Q27 **Chair:** Does that rely on any large cases that you are taking through?

Jim Harra: To some extent, yes, because there were a couple of large cases, though not as large as 2019-20. There was one very large case. I think it was an aggregate duty settlement, which accounted for about £4 billion by itself, from memory.

Q28 **Chair:** There is nothing on that scale.

Jim Harra: There is nothing on that scale, but there certainly were a few large issues that did not settle at the end of 2021-22, which have been carried over into this year.

Q29 **Chair:** That will help you meet that target then.

Jim Harra: Yes, but at the moment our central estimate from my compliance group does not quite hit the target that I have set them, but that is what I would like to see us achieve.

Q30 **Chair:** For the big stuff, in a way, at least you can see a very big number there, but there are a lot of small compliance issues. How hard is it now, getting to chase down people who perhaps owe money back from previous years as well? Some of this is very small. In terms of the amount of time and effort, when do you get to the point that you are going to write some of this off? Is there enough big stuff in there that you are really going to be confident in hitting that target?

Jim Harra: There is enough compliance risk for us to chase, but it is a matter of landing it. We are not encountering any significant difficulties in the post-pandemic period in terms of engaging with people on their compliance and investigating. We are back to normal ways of working but, as I am sure we will get on to later, we are seeing different payment behaviours from taxpayers. We have to adjust our compliance yield for what it is that we think we can recover. That is definitely a concern in relation to the tax gap and in relation to our management of it, which is the underlying debt level.

Sticking with under-declaration, what we are seeing is pretty regular things that we would have seen pre-pandemic. There are some new risks that we are alert to as a result of the cost-of-living crisis. First of all, we will see people prioritising other spending over paying us. We might also see people taking second jobs or moonlighting, which they are perfectly entitled to do but which are more likely not to be declared to HMRC. Of course, case by case it tends to be quite small and therefore quite challenging for us to deliver.

We have also had, within our compliance group, major recruitment. Last year, we recruited about 4,200 new people into that group. It is a big task to induct those people, train them and mentor them. To some extent we took experienced colleagues away from the frontline work to work on mentoring and supporting those people alongside doing their compliance day job. That has put a bit of a stretch on our performance last year, which we should get dividends for in later years. If you recall, some of our compliance resources were diverted on to Covid-19 error and fraud work. We got funding to backfill for that but, because of the time it takes for those people to become proficient, it will be 2025 before we would expect to recover the compliance yield that we lose as a result of that. You would expect to see a slight underperformance in 2021, 2022 and 2023, and then recovery of that in later years. We have modelled that.

Q31 **Chair:** I am heartened that you have a target. Is that internal? Are you expecting anything stiffer from the Treasury, given you have had these extra resources poured in?

Jim Harra: It has not been a published target.

Q32 **Chair:** You have told us now, so it is public.

Jim Harra: Yes, I am quite happy to talk about it, and we have certainly discussed it with Treasury colleagues as well. There is no direct correlation year on year between the yield that we get and the tax gap. Over time we model what is the level of yield that we think we would need to recover in order to maintain this tax gap. That is why we have set our target for ourselves at £36 billion.

Q33 **Chair:** You want to maintain the tax gap, not reduce it.

Jim Harra: With the resources I was given in SR21, what I promised in return was that we could maintain the tax gap with that resource. We do, however, get additional resources then given to us on top of that from time to time in fiscal events in return for promising additional tax revenues. That would tend to reduce the tax gap. If you look at the tax gap over time, it has reduced from about 7.5%, in 2005-06, down to 5.1%.

Q34 **Chair:** We could have a long discussion about the benefit of investing. You were saying these were short-term investments in staff. That is a challenge. You had to onboard over 4,000 people just recently. Are you hoping for a steady settlement on this? Are you having those discussions about how you could reduce the tax gap?

Jim Harra: I am pretty sure that, if my director general for customer compliance was here, she would say that, yes, she would love a steady long-term picture.

Q35 **Chair:** It seems logical. Other Departments have to go a bit with the ebb and the flow, but in HMRC every pound spent brings in a lot more to spend on other things. It is a bit of a no-brainer. We are champions of HMRC. You might not believe it as a witness here, but we do want to see you get the money in, so we are quite keen to see you have the money to do that.

Jim Harra: I certainly do believe that. First of all, it is very positive that we had the funding to recruit over 4,000 people last year, but it is important for the longer term that they are fully professionalised, competent and able to perform at their full potential. That means we have to invest now in training them and consolidating that training. That does put a bit of a strain on our operational delivery here and now in the same area, but that was a choice that we made and we will get payback for that.

Chair: Most permanent secretaries would not turn down 4,000 extra staff.

Jim Harra: Again, we will not make best use of that extra investment if we do not make sure that those people are properly trained.

Q36 **Chair:** What is the retention level like for those people?

Jim Harra: We do not have any significant issues with retention on the compliance side. We have seen an increase in attrition in our customer service group, higher than our forecast. Angela can probably give you the figures. We think a key reason for that is that we recruited people during the pandemic, some of whom came from sectors of the economy that were closed. As those sectors have opened up, they have preferred to go back to their original sector. We have seen quite a high level of attrition from recent recruits.

Q37 **Chair:** You have not with the compliance team. The investment in the people is hopefully going to come.

Jim Harra: Yes, we do not have a problem with that.

Chair: That is heartening. Hold the thought, Ms MacDonald, because I know that Mr Grant wants to talk to you in a lot more detail about customer service later.

Justin Holliday: Just to help on the continuity point, there was an increase in the compliance baseline resourcing in SR20, which was carried through to the three-year settlement in SR21. We have a higher degree of confidence about baseline compliance resourcing than perhaps we have had for a while.

Q38 **Chair:** Nevertheless, you have been having to model the 20%, 30% and 40% headcount reductions.

Justin Holliday: Yes, that is true.

Q39 **Chair:** We are probably not going to get much further with you on that, given that you are waiting for 31 October before anything is in the public domain.

Can I just touch on the IR35 reforms? We had the previous Chancellor announce that those IR35 reforms were going to be taken away. You have spent a lot of time and effort on that. I have quite strong views about the impact on tech businesses in my area, and there was a lot of discussion about this. What was your estimate of the reduction in tax that would have flowed from the IR35 reforms if they had remained cancelled, because they have been reinstated since?

Jim Harra: The estimate was about £2 billion a year. That would have been the cost of that measure. That has now been removed from the cost of the Government's growth plan as a result. What is that made up from? By and large, HMRC would say that would have been an increase in non-compliance with the underlying IR35 rules, back to the kinds of levels that we saw in the past. One of the concerns about the 2017 and 2021 reforms, I know, is the belief that some genuinely self-employed people will get caught up in the way that engagers assess their status. Some of that cost, you might argue, comes from that, but we would have said that would have been as a result of non-compliance and therefore tax gap growth.

Q40 **Chair:** Do you have any understanding of how many people in your organisation, within HMRC, have been working on the IR35 reforms? It has now been reinstated, but that was a lot of work that had gone into that. How many people are working on that?

Jim Harra: I do not know offhand what the resource is that is deployed on it. We would be changing now the nature of our work. We would have put quite a lot of resource up front in helping engagers to get to grips with their new obligations. That is different from the amount of resource we would put on it on an ongoing basis to police it. One of the advantages of the 2017 and 2021 response from HMRC's point of view is that it gives us a smaller number of people whose compliance we have to manage, because we can hit one to many when we go to an engager who might employ 20 or 30 or 50 contractors.

Q41 **Chair:** Has there been any impact on HMRC of the two-week period between when it was announced it was going and then it was announced it was being reinstated?

Jim Harra: Not from an operational point of view, no.

Q42 **Chair:** It was so fast it did not even hit you.

Jim Harra: My policy advisers and Treasury have been very busy, as you might expect, over the last couple of months. We had started some operational planning for what we would have done if the changes had come in, which is not now the case. Otherwise, given that those measures were not intended to come in until April next year, they had not changed anything straightaway.

Q43 **Chair:** Just going back to you, Mr Holliday, on the issue of compliance, when you are talking to the Treasury, what is the sweet spot in terms of resourcing that you would get in that would get to increase compliance and reduce the tax gap? Do you have those discussions with Treasury? What is the optimal level of resourcing you would need?

Justin Holliday: We think we are resourced at the moment to be able to hold the tax gap.

Chair: That is to hold it.

Justin Holliday: Yes.

Q44 **Chair:** What you have now, even in this current difficult climate, is optimal.

Justin Holliday: If optimal is holding the tax gap, yes.

Q45 **Chair:** That is your definition. Can you give us some figures of what extra money would deliver roughly a reduction of the tax gap? Can you give us any metrics on that?

Justin Holliday: Jim was mentioning the fact that, from time to time, through Budgets and other fiscal events we have particular investment for particular purposes. Typically, those investments give a return of between 10 to one and 20 to one. On that basis, to get £1 billion off the tax gap, you would need between a twentieth and a tenth of £1 billion to be able to deliver that.

Chair: That is a helpful pitch to the Treasury. I am sure the Chancellor is listening.

Jim Harra: On average, for every pound that we spend in our customer compliance group, we recover about £18 worth of additional tax revenues. That does not mean that the marginal benefit of an extra pound would be another £18, but it shows you that there is a very positive rate of return.

Q46 **Chair:** We dealt with some of those figures in detail last time, so I will not go into that too much again. We have a rocky period ahead with the economy. You were very clear there, Mr Harra, that some people might decide to prioritise other things. Clearly things like rent and food are absolutely basic. What strategies do you have in place? If you do not get the money in, that is less money to spend on public services. There are huge knock-on effects. Any underperformance by HMRC is immense. What strategies do you have in place to make sure that people pay their tax on time or, if they do not pay on time, that you have a very quick recovery process to make sure that they get back on track with repayments?

Jim Harra: A key risk for us is non-payment. We saw that after the 2008 financial crash. That was a part of the tax gap that grew. We have seen evidence that, as the economy has returned to pre-pandemic ways of working, we are not seeing a return to pre-pandemic payment compliance by taxpayers.

Q47 **Chair:** Is there any particular group? Some businesses are struggling very much with the energy prices and other things as well. Are there any sectors that are particularly problematic?

Jim Harra: We have seen an increase in the rate of non-payment of Pay As You Earn and VAT. That is in the business area rather than the personal tax area. For example, at the end of June the debt balance was £42 billion. That is not particularly a hangover of that big pandemic peak of debt. That is because of new debt arising at a rate that we did not see before. If you look at the peak of debt during the pandemic at the end of August 2020, debt stood at £72 billion. That was largely due to Government policies to allow people to defer payment. We have worked through and cleared the vast majority of that. About £60 billion of that has now been cleared and a further £1.2 billion of it has been put into a managed Time to Pay arrangement. There is roughly £12 billion of that still working with my debt management service.

Despite that, the debt balance at the end of June this year is significantly higher than going into the pandemic. The reason for that is that new debt post pandemic is rising at a significantly higher level than we saw before. Our strategy is to segment those debtors, to understand what it is that is driving their debt and therefore what kind of treatment we need to apply to it.

To some extent, it is caused by the prevailing economic conditions, the cost-of-living crisis and, as we said earlier, people unable to pay or feeling they have to prioritise other things. Some of it, I suspect, is down to a learned behaviour during the pandemic that we need people to unlearn, which is that they can treat the taxman as a bit of an overdraft facility. I am not a bank and that is not what I am here to do. We want to segment those debtors, understand the reasons why they are in debt and then apply the correct treatment to each segment. That is a departure for us, because in the past we have had a one-size-fits-all debt management process that we put all debts through.

Q48 **Chair:** Some of those new 4,000 compliance people will be trained with respect to this.

Jim Harra: We have increased our debt management service by 700 people. We have been given funding for that. In terms of their performance in clearing debts, they are achieving record levels of productivity.

Chair: There are record levels of debt.

Jim Harra: You are nevertheless seeing the debt balance increase because non-payment has increased significantly.

Q49 **Peter Grant:** Mr Harra, you mentioned that levels of tax debt are increasing. Do you have an up-to-date estimate for what level it is at now?

Jim Harra: At the end of June, which is the last published figure, it was £42 billion. At the end of August it was about £46 billion, so it has continued to grow since then. It fluctuates during the course of the year because there are certain payment points. That is when non-payment crystallises. Nevertheless, the trend continues to be upward rather than downward.

Q50 **Peter Grant:** There is a self-assessment payment point at the end of July.

Jim Harra: Yes, and that would have been reflected in that.

Q51 **Peter Grant:** That would mean that, if people missed that, it hits the figures for August. Are you able to get any feel for how much of that is people who are struggling to pay and how much of it is people who are trying not to pay?

Jim Harra: That is what our segmentation approach is looking at. We are trying to get as good as possible data, understanding what is driving the behaviour, including getting data from credit reference agencies. We are experimenting with that to see if that can give us accurate insights and an ability to identify which debtors are displaying which kinds of behaviours. If someone is genuinely financially distressed and unable to pay their tax, what we want them to do is engage with us so that we can put them into an affordable arrangement. If, on the other hand, they are making choices about what they spend their money on, we want to apply different techniques to make them treat us as a higher priority than some of them are currently treating us.

Q52 **Peter Grant:** The level of debt actually came down during 2021-22. It came down by £16 billion or £17 billion or thereabouts. You also reported the highest ever amount collected during that year, over £730 billion. Was any of that increase in collection due to people paying off their debts from previous years?

Jim Harra: First of all, to clarify, the £731 million is on an accruals basis. It is actually the liabilities that relate to the year. Looking at the debt balance, yes, people were allowed to defer payment of certain taxes during the pandemic as a means of helping them get through it, VAT and self-assessment in particular. That is what caused the peak. Of the VAT debt that was deferred, currently there is only £700 million of it still outstanding, which I know is a lot of money but proportionately is a very small amount of what was about £40 billion deferred. Yes, a lot of that reduction was businesses paying off the tax that they had been allowed to defer but that we had nevertheless treated as debt on our books.

Q53 **Peter Grant:** Since the date of the accounts, and in fact even since they were signed off in July of this year, clearly the financial pressures on individuals and businesses have increased significantly and are going to continue to increase. Have you been able to make an assessment as to what impact that is likely to have on the ability of individuals and businesses to pay their tax, especially if they are still paying tax based on the business profits for last year and they are now making a loss because they cannot afford to pay the bills? Have you been able to assess what the impact on your tax take has been?

Jim Harra: In the accounts, we assessed an impairment. In operational terms, we remit or write off debt once it has got through all of the debt recovery processes, if we conclude that it is irrecoverable. In the accounts, we have to make some assumption or estimate overall about how much of that debt balance we think we will be able to collect. There was an impairment in our accounts of about £14.4 billion on the debt at 31 March. That was our best estimate at the time when the accounts were compiled.

You are right: the situation keeps changing all the time. I go back to what I said before. We are currently carrying out work, including looking at sources of data, to try to give us the best possible insight, mainly at this stage from an operational point of view in terms of understanding what the best treatment is that we can apply to different types of debt.

Q54 **Peter Grant:** Between March 2020 and March 2022, there was an increase of nearly 1.5 million in the number of taxpayers who were in debt to some level with HMRC. How quickly do you expect that number to come down, or do you expect it to keep increasing?

Jim Harra: I have not really focused on the number of debtors, but we do not expect the amount of indebtedness to reduce in this financial year. We have not seen anything in the trends that would suggest that debt balance is going to be materially lower. We continue to work through all of the pandemic debt—as I say, there is still about £12 billion of it sitting with my debt management service that we have not cleared—to make sure that we meet our commitment that we were going to work through all of that unprecedented stock of debt.

In terms of what is happening here and now, we are constantly learning. I do not see anything in the external environment or in what we are going to be able to do that will significantly reduce that debt balance by the end of this financial year.

Q55 **Peter Grant:** It is quite likely that a lot of those additional 1.4 million people have never been in debt to HMRC before. Some of them will never have been in debt of any kind until quite recently. Do you have a different approach to them from the approach you have for people who are always tardy in paying their bills?

Jim Harra: Yes. You are right that there are a larger number of smaller debts than we have dealt with before. We do, in our debt management approaches, give people some earned autonomy in the sense that, if your track record has been that you have always paid and then suddenly you have not, we will ask why, because the chances are you are in financial distress as opposed to someone who is always late with their payments or always shows a propensity of not paying until we take enforcement action. We have changed our debt management processes. For example, where we know that a debtor is someone who only responds when we get serious, we short-circuit that.

Chair: It is quicker.

Jim Harra: We do not go through the nice letters, I am afraid, with those people before we get to the stronger ones. It is very important that we segment these customers and that we are careful about making assumptions about the correctness of the segmentation, because we have to treat every person on a case-by-case basis when we engage with them. Our aim is always, with anyone who is financially distressed, to help them out of debt in a manageable way and, if they are a business and their business is viable—in other words they can meet their ongoing liabilities—to allow them whatever time they need to do that.

Angela MacDonald: If I might add, part of that is about modernisation of things like Time to Pay. We had 851,000 customers, as of June 2022, on Time to Pay arrangements, which is a significant increase. You can also now go online and self-serve a Time to Pay arrangement if you are within certain parameters. We also have things like the Breathing Space initiative. We are doing everything we can to support customers who genuinely need our forbearance and our support, to try to help them. The average length of a Time to Pay has increased. At the minute it is up at 14 months, which in prior times would be at six.

By far the majority of Time to Pay arrangements do then pay off. We would rather that the customer was giving us regular payments and actually the money was eventually got than we pushed too hard and that customer did not end up paying through. We are doing everything we can to be firm with those that need it but supportive of those who need our support.

Q56 **Peter Grant:** The approach that you have indicated, where you are not just treating everybody the same, is likely to be a lot more time-consuming and to involve a greater input of staff time. Of course, you now have more people in debt than you had previously. Do you have sufficient capacity within your staff, first of all, to deal with such a big increase in the number of debtors, and also to deal with them in a way that is more time-consuming and more demanding on staff than simply the standard process?

Jim Harra: First of all, in some areas it is less time-consuming. We have automated a lot of Time to Pay. For example, people can go online and self-serve that, whereas in the past they had to speak to one of my advisers. That is something that we, over time, have felt is a safe thing to do.

Q57 **Chair:** Can I just chip in there? You say it is a safe thing to do, but if it is easy just to go on and register for Time to Pay, it makes it easier to do that even when you do not need Time to Pay. Do you think people could just be using you as a bit of credit?

Jim Harra: First of all, I should point out our Time to Pay arrangements are not interest-free; it is not a cost-free option for people.

Q58 **Chair:** There is less interest than on a credit card.

Jim Harra: Potentially, yes, it is certainly less than on a credit card. We will be monitoring who uses it and whether people are repeatedly using it, because it is supposed to be a one-off thing to help you out of a distressed period and you must pay your ongoing liabilities while you are clearing down your debt on Time to Pay.

It is important that we focus our resources where they really are needed. With Time to Pay, what we have seen is that people use it responsibly and there are quite high completion rates. We want to make sure that we use data sources effectively to segment customers in a way that does not involve a heavy operational input, which is why it is a little experimental at this stage.

Q59 **Peter Grant:** Are you able to work jointly with other agencies to make sure that you are supporting people who need to be supported? Do other issues about data confidentiality prevent you from working jointly with local authorities, for example, which are likely to know the people?

Jim Harra: Part of our process, if we meet a distressed debtor who has debts to other organisations as well, is to encourage them to go to agencies that can actually give them the right advice about their overall circumstances, which is not something that we are able to do. We do refer people to those agencies and we do, to some extent, fund the voluntary sector as well to help vulnerable taxpayers where they are better placed than us.

We also work across Government. We are probably the biggest debt collection function in Government, but there are others. We probably see ourselves as the most professional and we can help across Government. In addition, where there is distress in particular sectors, we will work with the relevant parts of Government that help that sector. For example, at the moment some rugby union clubs are feeling they are in financial distress and that is reflected in tax debts. We work closely with Sport England and with DCMS to make sure that there is an aligned and consistent approach to supporting people like that.

Q60 **Peter Grant:** Can you give us an update on the single customer record? Is that proceeding on target? When should we expect to see it significantly changing the ability, first of all, to collect debt from people who should be paying and to support people who are struggling?

Jim Harra: First of all, we have an extensive digital account presence now for customers. Over 31 million citizens have credentials that give them access to a personal tax account. About 18 million to 19 million people actively use their online account. We also have a mobile app and about 1.6 million customers use that as well. We were given funding in the 2021 spending review to reform our digital offering, to offer a single comprehensive online account for our customers. Customers will start to see the active benefits of that from summer next year as we build it.

Then we will incrementally build in more and more services to that, as well as improving the customer experience, because we get significantly higher customer satisfaction levels with our digital services than our analogue services. It is also key to us achieving the efficiencies that we signed up to in the spending review and to pushing those as far as we possibly can.

As well as building the account and populating it with what is already there, we have a programme of work to identify what are the highest-priority areas, particularly of income tax and national insurance work, to add to that account and to enable people to self-serve.

Q61 **Peter Grant:** HMRC issued a statement in August that it was taking on responsibility for administering the Government's new debt respite service. Can you tell us, first of all, what that is and why it was HMRC that was asked to take it on?

Jim Harra: There is a slight misunderstanding there. We are not taking on responsibility for managing the debt respite service. The debt respite rules apply to us as a creditor, in the same way as other creditors. We are investing to make sure that we can meet the standards required of us as a creditor in relation to that, for example giving people Breathing Space, which we have already implemented, but also picking up the more formal arrangements that people can put in place via the Insolvency Service, because we expect to be one of the biggest creditors affected by that policy.

Q62 **Peter Grant:** The way it was reported in Public Technology was that HMRC was seeking a commercial partner to support a multimillion-pound programme over the next three years to transform its debt management services and systems. Are you telling me that did not relate to the debt respite service?

Angela MacDonald: Forgive me; that is a slightly different thing. Our debt management systems more broadly are part of our more aged IT estate and therefore they require significant modernisation. We have been given funding to modernise the platforms that those sit on, thinking about things like core resilience and data analytics. You can imagine the sophistication we are talking about here for the targeting. That requires some quite significant investment to do that, as well as then enabling things that we have just launched in August: the ability for our field collectors to be able to collect debit card payments with a card reader that they will have in the field.

It is a broader and bigger investment in our debt management architecture to improve data security and then enable really great digital services to then build on the top of those. The capabilities that you talk about there are some of the capabilities that we build in as part of that.

Q63 **Peter Grant:** How does that relate to the single customer account? Is it part of the same project, or are the two of them running side by side?

Angela MacDonald: We have a variety of different transformation programmes, which all sit within one common architectural end design. We want one experience for the customer. At the minute, we have very high usage on our digital channels, but there are also many instances of how you can get into HMRC digitally. Our aim is to have one front end, into which all of those services go, and architect all of the variety of pieces at the back, so that they are all heading into that one piece of design. The transformation of debt supports the changes we need in order to support the changes we are doing for things like making tax digital. They will also support the things we need to do for single customer accounts. It is all one big, connected technology roadmap.

Q64 **Peter Grant:** A final question for me just now is based on the Committee's experience with a number of other Government IT projects. Can we be certain that, when all these new systems are switched on, they will talk to one another in the same language?

Jim Harra: There is nothing certain about my transformation programme. It runs at some risk. Yes, one of the key reasons for the single customer account is that at the moment we have separate digital services that are not integrated. That does not give a seamless service.

Underlying that—my digital colleagues will not thank me for saying this—is that it is relatively simple to build the digital front end. The real challenge is the data that underlies it and making sure that there is a single instance of each customer with a full record of all their tax affairs that can get presented to them in their account. We have a major programme of work, called a unique customer record, going on to make sure that all of that data is joined up and can be presented to a single customer in a single way.

Q65 **Peter Grant:** I said that was my last question, but I have one quick follow-up to what you said earlier. You mentioned that the Time to Pay arrangements, for example, are not free. They are not interest-free. What is the current rate of interest on it? How much would it compare to what someone is now having to pay on their mortgage, for example?

Jim Harra: I am not sure I know offhand what the answer to that is. Our interest rates are statutory. They are set by legislation.

Q66 **Chair:** Is it primary legislation? It must be able to change.

Jim Harra: I think it is secondary legislation. Our statutory interest rate is 2.5 percentage points above the Bank of England base rate for late payment.

Chair: You cannot change that without changing the legislation.

Jim Harra: No, not without changing the legislation.

Q67 **Chair:** How often do you try to change that?

Angela MacDonald: We have just done it, have we not?

Jim Harra: I am not aware.

Chair: I missed an SI; forgive me.

Angela MacDonald: I will write to you with the details but I think we have just updated it.

Q68 **Chair:** I just wonder about keeping pace with things, with the Bank base rate as it is. I wanted to pick up on the point you raised, Ms MacDonald, about all the investment you are putting into your various platforms. Forgive us if we have a bit of scepticism about how those will work, but you are also doing this all under the pressure of a huge inflation and resource constraint. Mr Harra talked earlier about the prioritisation. If you have to prioritise, what is the impact going to be on the customer trying to reach HMRC through the digital programmes. Will some of this go slower? Will some things not happen? Do you have a list of priorities if your funding is going to be tighter, for all the reasons that we know?

Angela MacDonald: That is a very fair question. Our transformation has four main thrusts to it. We have an amount of money that is for resilience, remediation, security—the core pieces that the customer does not see but without which we do not function.

Chair: They are top priorities.

Angela MacDonald: That is about risk, data and security, so there is an amount of money there. There is an amount of money that is about the delivery of UK transition, so Single Trade Window, which HMRC is doing on behalf of Government and things like freeports; there are a variety of things that are there. We then have things that are about ministerial and legal commitments, so the stuff we get in policy. Then we have an amount of money that is the transformation, so things that enable us to improve our services to increase our efficiency.

Q69 **Chair:** That is at the bottom of the pile.

Angela MacDonald: No, those were in no particular order of attention.

Q70 **Chair:** How do you prioritise them?

Angela MacDonald: All of these are choices that we have in the past offered, and will continue to offer, to Ministers. Across the variety of all those change programmes, some of the business cases will contain additional tax revenue. Some of them are about risk reduction. Some of them are about delivery of new policy. When asked in prior times, we will always lay out to Ministers, "Here are the choices. If you would like to prioritise the speed with which we digitalise, which would allow us to be efficient more quickly, this would be your list. If you take a different attitude on risk and security, it would be here. If you want to move policies at different paces, this would be the list".

Q71 **Chair:** That is one of the risky ones at the moment. With the turmoil we are going through, with a potential general election—within at least two years there will have to be a general election anyway—you could be quite busy on the policy priorities as we go through different iterations of Government.

Angela MacDonald: Absolutely, and it is definitely the case that every time we, in our close working with the Treasury, are impacting requests given to us by Ministers, we will be clear, "You can have this one and either we can absorb that, because it is relatively small and easy to do, or, if you need us to do that, here are some of the choices that you need to make".

It is definitely true to say that, looking at the portfolio, there are many versions of what that prioritisation list could look like, depending on what the Chancellor and Treasury Ministers decide are the things that they want to focus on. For us, we have a long-term strategy of the transformation that we wish to do in the tax system. That is publicly available. Often, in this situation, it will be that some of that will be able to go faster or more slowly, dependent upon ministerial choices. We will give fresh advice when requested.

Q72 **Chair:** Mr Harra was very upbeat about the efficiencies that you are driving through, sticking to the plan that you already had, despite all the buffeting that is going on at the moment. That is supposed to help reduce demand on your expensive bit, your staff, because you can automate those things. There is quite a risk that a lot of policy changes, for example, could impact on that transformational end for the customer.

Angela MacDonald: Yes, absolutely. There is a correlation, and we are very clear in our advice about the connection between the decisions made on transformation, the capacity to do change and then what that does, running through to our capital and operational budgets. Justin would probably be much more able to talk to that than me, but we are very clear on the causation and correlation between the two.

Q73 **Chair:** Even delays, Mr Holliday, to some of these big capital programmes on IT will be costly.

Justin Holliday: In terms of the impact on efficiencies, our efficiencies broadly fall into two buckets. There is a significant proportion that is continuous improvement and not that investment-heavy. Then there is a significant proportion that is dependent on the investment. As Angela has said, we are really clear, as we look at prioritisation, where there could be a knock-on and are clear about the level of customer service deterioration and where we believe that would get to a point where that is politically unacceptable.

Q74 **Chair:** Is there a point of no return when you have invested a certain amount in a next stage of an IT system? We have looked at this in the past, where the loss of spending would be so great that it would not be good value for money to not go ahead with it, even despite the pressures that may be coming from Ministers and others.

Justin Holliday: That is also a factor that would be in play. Broadly speaking, our investment approach and development approach is quite incremental at the moment, so the chances of half-building a bridge are much lower than with an incrementally built IT system.

Q75 **Chair:** It sounds like you have built in safeguards from the beginning.

Jim Harra: The way fiscal events build up, you have a lot of different measures. Some of them make it through the process. Some do not. We cost each measure as they go in terms of understanding how we can deliver them. When the overall shape of a fiscal event is clear, we give an amalgamated piece of advice on our capacity to deliver the whole thing and what impacts that might have on other things that we are trying to deliver. Obviously, I do not have resources sitting on the bench waiting to be deployed, so every new thing has some consequence.

Q76 **Chair:** At the beginning we talked a bit about the efficiency savings and you were saying in July you had modelled things. When is the cut-off point for making efficiencies that would start kicking in in the next financial year for you? Presumably you have modelled a lot of this already.

Jim Harra: We have workforce plans right up until the end of the 2024-25 financial year, which assume the efficiencies that we will be able to make on an ongoing basis.

Q77 **Chair:** If you had to make more, when would be the cut-off point? I know it is not a precise figure. I mean the range.

Jim Harra: There is a difference between efficiencies and cuts. I can make a cut as fast as I am told, in a way.

Q78 **Chair:** I am not sure you want to offer that up to the Treasury at the moment.

Jim Harra: That would then involve a cut in performance, which would either be reflected in the services that customers experience or in the compliance yield that we can recover.

Q79 **Chair:** I am asking because there is a lot of discussion. Suddenly, the rest of the world is talking like the PAC does about efficiencies and so on. There is a dawning recognition that you cannot just make an efficiency by clicking your fingers and saying it will happen in the next few months. It is helpful for the tax-paying public, who are hopefully tuning in to your every wise word, Mr Harra, to understand how long it would take for you to create more efficiencies. You are a Department that is slightly different from other Departments. How long would it take you to work up an efficiency plan for the next financial year?

Jim Harra: If we had to implement plans that materially increased our efficiencies by focusing on that as the priority, I would want to be looking at doing that in 2024-25 or beyond, rather than next year. It is very difficult to see how we could implement something as quickly as that, not least because it is not just us, usually, who have to implement things. Our customers have to as well. Almost invariably now, any change that we make involves change to payroll software, business accounting software or whatever. We have a whole set of people we need to take with us.

Q80 **Mr French:** Moving on to error and fraud, the Auditor General's qualified opinion clearly states that HMRC did not have adequate controls in place during 2020-21 for some of the Covid schemes. How confident are you in your assessment of error and fraud in the Covid-19 support schemes now?

Jim Harra: I would not agree that we did not have adequate controls. I know that the amount of losses to error and fraud was material in audit and accounting terms, which I believe was inevitable. We have recently come up with an updated estimate of error and fraud for the entire length of the Covid support schemes, which was that it was about 4.6%—that is our central estimate—over the 18 months that the schemes ran. That is a significantly lower rate of error and fraud than we had previously estimated for the first year of the schemes, so that is obviously a positive change.

That remains an interim assessment and there will be a further estimate in due course. Jane can talk about the detail of how we made that.

Q81 **Mr French:** It is certainly welcome news that the revised detail suggests that it was a lower amount of fraud than previously thought.

Jim Harra: It is a lower amount of error and fraud overall and, within it, a higher proportion of it is error than fraud than we previously thought, which is also positive.

Q82 **Mr French:** On the estimates that are in the report, it is quite clear that there is some uncertainty still. Can you touch on why there is that uncertainty?

Jane Whittaker: Let me say a little bit about why we are more certain about these estimates now than the ones that were published in the previous annual report and accounts. That is because we have a lot more data now to underpin these estimates.

There are three main data sources that we have that we did not have before. One is for the furlough scheme: we have a random inquiry programme that has been undertaken with customers by our compliance experts. Another is that of course we have, in the time between the two annual reports, undertaken quite a lot of compliance activity, so we have a lot of operational data and intelligence to build in. Then on SEISS, we have self-assessment returns for 2021 as well, which tell us a lot more about the circumstances of the people who claimed SEISS.

We have recognised that there is uncertainty in the estimates and we have presented ranges. Jim referred to them. The most uncertain element of the estimates is the extent of error and fraud that is around people undertaking some work while their employer was claiming CJRS for them. That is an inherently extremely difficult thing to measure, so there will always be some level of uncertainty around that.

We have been very transparent in what we have published, both in the accounts and in the supporting technical document, about the methodologies that we have used. As Jim says, we have further work in hand to make our final estimates of error and fraud for next year. That is mainly additional random inquiry programmes for the later phases of the furlough scheme and a random inquiry programme for the last phases of the self-employment income support scheme, where the rules around the size of grant that you could claim and the conditions you needed to meet gave incentives for people to make sure they ended up on one side of the fence rather than the other. That is the additional data that we will gather. We have significant additional data to underpin these estimates, so we are feeling much more confident about the estimates than we did at the point of the previous annual report and accounts.

Q83 **Mr French:** That is helpful. You touched on it there and there is obviously a big fairness issue about the job retention scheme and furlough. Looking at the figures, it is clearly the biggest chunk of the bill. It is about £3.5

billion on the CJRS itself. How do you go about measuring that and detecting it now, after the event? How do you measure whether someone's employer was claiming furlough while they were working? Is it realistic to be able to detect that now?

Jane Whittaker: There are two sorts of questions in there about what we do from a technical measurement point of view and how we actually run our compliance operations. You are right that, with working while claiming, to be absolutely certain on that we would need to know exactly the working patterns of all those nearly 11 million people who at some point were on the furlough scheme and exactly how that corresponded to the claims that the employer was putting on. Obviously, there were changes in how employers and employees were working as the NPI position on Covid developed over that time.

From a technical measurement point of view, we have brought together all the existing data that is available from our compliance activity, but also from established surveys, such as the ONS's labour force survey and others, and matched that to our statistical and operational data. We undertook a small survey during the middle of the pandemic to further test what people could tell us about their working hours and how they compared with the hours that they were furloughed, but it brought it home to us that you have to make a very timely assessment of that. Recall issues were something that people struggled with on that. Does that help?

Q84 **Mr French:** It does and it brings me quite nicely on to my next question. How much of this estimated £4.5 billion of error and fraud is it realistic that you can recover from this point?

Jim Harra: We were given about £100 million funding to have a temporary taskforce to tackle this and we have opened about 40,000 compliance investigations in this area so far. By the time that taskforce has wound down, we forecast that we will have recovered about £1.1 billion, so that is about 25% of the error and fraud. Beyond that, we will continue. There will be, I suspect, some of the more complex cases still open at that stage. We will also continue, within our business-as-usual resources, to try to identify and recover further amounts alongside tax compliance.

Q85 **Chair:** Can you give an example of one of those complex cases?

Jim Harra: We will obviously make sure they remain resourced, but some of the more complex investigations are unlikely to be completed and closed at that point.

Q86 **Chair:** Can you give an example, talk us through what sort of thing you are talking about?

Jim Harra: For example, there are some of the criminal investigations.

Q87 **Chair:** They are all criminal, just to be clear.

Jim Harra: No, not all of them. The vast majority of these investigations are using our civil powers, but we have made 35 arrests so far and we have criminal investigations.

Q88 **Chair:** I am sorry. I am cutting across your answers. To be clear, on the ones that are complex that are not criminal, what sorts of things are you looking at and how are you finding out that there is even any fraud there?

Jim Harra: It is those where we are having to gather evidence and challenge what we are being told. We know that, at the point when the funding expires, we will still have some of those cases on our books. They are likely to be the ones that are not as straightforward to have investigated and closed. Some of those will be criminal investigations. Some of them will be larger but more complex evidential investigations. The £1.1 billion will not be the end of the story, but it is when the bulk of the resources will no longer be—

Q89 **Chair:** When you are talking about these cases, what size of organisation? Presumably, you are not talking about some of the individuals that Mr French was hinting at in his questions.

Jim Harra: As I mentioned earlier, in our latest estimate we have found that a higher proportion of this than we had first thought is error by a large number of fairly small concerns. That affects the cost-effectiveness of recovering it, because we have to investigate a larger number of people. We have opened significantly more investigations than we originally expected to do as a result, but they tend to be the simpler ones. I would expect the bulk of those to be resolved at the point when the funding expires and the resources come off this on to tax work.

We have to get our priorities right here, because there are choices we can make. The rate of return that I can get for this resource, in financial terms, is higher on tax than it is on this already and certainly by the time you get to the end of this. I currently forecast that, at that point, we will have recovered about 25% of the overall amount.

Q90 **Mr French:** On my side of things, given what was happening and the speed at which people were working at, both within Government and in businesses trying to adjust, I think we can all appreciate that there would have been a degree of error made, fairly genuinely in some cases, in the way it was tapered off and so on. In terms of not just recovering but learning lessons from this period, what are those key takeaways about the upfront controls that can be put in place for these kinds of schemes for HMRC?

Jim Harra: We feel that we had very effective upfront controls that prevented organised crime from abusing these schemes and kept them out. Our operational work downstream is detecting very little evidence that that happened, so we get increasing confidence that we kept those people out. The big lesson is the better, more up-to-date data that we have, the more we can assess what people's entitlement is and the less reliant we are on them self-assessing. The inevitability when it comes to furloughing is that the information is in the hands of the employer and the employee and not in the hands of HMRC.

If, God forbid, we had to re-run such a thing again, I cannot immediately see how we could have access to all that data in-house. You would always be reliant on some self-assessment, downstream risk management and detection. A key lesson is the better, more up-to-date data we have, the more securely and accurately we can make these payments.

Q91 **Mr French:** That is fair and helpful. Given the scale of the national challenges for the economy and some of the difficult decisions that have to be made in this place, there is certainly a moral duty and a fairness issue to pursue fraud where it has happened. I think most of us in this room would agree with that. How do you go about doing that from an evidence point of view? This is why I am a bit unclear from some of the answers. How do you that? Some of the examples provided were a voluntary basis of providing hours and so on. How do you do that within the tax system?

Jim Harra: We cross-reference against different data sources, and you would not believe how blatant some people are. We have met cases of employers who have both claimed to have furloughed all of their staff and, at the same time, made Eat Out to Help Out claims on the basis that they had had a record month in August 2020.

We have ways of cross-referencing where, if there was not a downturn in your business performance that reflects the level of furloughing that you said you had, that is a factor that would cause us to go in and have a look at what went on. Inevitably, sometimes there is evidence of people working, because it is quite difficult to have someone working and not lay a trail that that is what they have been doing. Nevertheless, the key behaviour that we have found in this non-compliance is error rather than fraud.

Q92 **Mr French:** There is one last point from me before I hand over. This is not necessarily specific to the two schemes that we have been discussing today. I know we are going to have a further report on some of the other schemes that were put in place during Covid. My experience, as I said at the start of the session, of trying to roll out some of those business support schemes during the height of this pandemic was that so much pressure was being put on local councils, for example, to get money out the door to the businesses. That is understandable, to an extent. I also remember the criticisms that came alongside that for councils that did the right thing and tried to put upfront fraud checks in place. I was aware of certain councils in London that were literally just sending cheques out of the door to businesses. God forbid we are put in this situation again, where you have to quickly put the scheme out, but how do you stop that and that level of fraud, because that is huge?

Jim Harra: In our case, we undertook to pay people within six days after they claimed, which gave us a very short window to risk-assess what we were receiving and block any that we thought ought not to be paid, but did give us time. I think there was about 72 hours when our risk assessment service could do those validation checks. We blocked 67,000 claims and registrations pre-payment as a result of those checks. At the time, getting the support to businesses was time-critical, because people were going to be made redundant if the furlough payments did not arrive.

Mr French: I understand.

Jim Harra: That was a priority choice that we had to make. It was always inevitable that we were going to see some level of error and fraud. The amount of error and fraud that we were going to see was, to some extent, dependent on how much upfront checking we could do, versus how much time we had to do it. That was the balance. Treasury and HMRC together had to advise Ministers how to make that choice.

Q93 **Chair:** Mr French raises an important point. Notwithstanding that there is going to be a public inquiry, which is a bit of a circus really, we have touched on this in previous sessions. You and the DWP had at least an understanding of the risks you were taking and you could assess, when you dropped certain safeguards, what some of the impact would be. We still want you to recover it. There is no free thing from the PAC on that.

Are you trying to code this into a sort of handbook? There were a lot of other bodies giving out money, as Mr French said, some better and more capable than others. Are there lessons that you can crystallise and turn into something that is a sort of handbook if ever this happened again? It is not just this. Government are increasingly giving funds to local government, like the housing fund and household support fund and so on, that they have to disburse at pace.

Jim Harra: I will have a look at that. We have published an interim evaluation.

Q94 **Chair:** That may be a bit dry. That is your novel, is it not, Mr Harra?

Jim Harra: Some of my colleagues wrote it, but I would agree with you that it does not necessarily capture what we are talking about here. I will take that away and think about it.

Q95 **Chair:** I am sure the Comptroller and Auditor General and the NAO are doing good work on this, but it is worth thinking about. We are seeing a lot of councils with a lot of financial problems at the moment and some of us share the concern about training and support.

Jim Harra: In our case, first of all, we were dealing with a group of employers and a group of businesses that were known to us and already on our books. We had a significant amount of data, albeit on the business side, not necessarily very current because there is often an 18-month lag in us getting the data. It meant that, in particular, we were able to guard access to the schemes. We got challenged for, "Are these secure enough?", but also challenged for, "People have been excluded as a result of your unwillingness to tolerate fraud risk". That was the balancing act that we had to achieve.

Chair: Absolutely, as it was for so many parts of Government and the system.

Q96 **Olivia Blake:** Mr Harra, I would like to ask a couple of questions about R&D reliefs—research and development reliefs—and how concerned you are initially about the increase in the estimates around fraud and error in those reliefs.

Jim Harra: Our current estimate of the level of error and fraud in research and development reliefs is about 4.9%. That is an increase on our previous estimate, which is largely as a result of an improvement in our methodology of measuring it. We are making further improvements to the methodology, so we have already started a random enquiry programme into research and development reliefs to get further certainty around that.

4.9% compares with an overall tax gap of 5.1%, so it is not way out of step, but I appreciate that, in materiality terms, for auditing purposes, it requires a qualification to the accounts. This is a very important incentive for the Government—they want to achieve a target of 2.4% of GDP spent on research and development—but, at the same time, it is an attractive target for people who want to abuse it, whether they are out-and-out fraudsters who have not undertaken any research and development or the sorts of boutique advisers who encourage taxpayers to push at the boundaries. We also need to make sure that we police it effectively but, at the same time, give everybody making legitimate claims as quick access to it as possible. That is a balancing act.

In April this year, we detected a suspected organised criminal attack on the scheme. That caused us to stop making payments for about two weeks on the small and medium enterprise scheme and about one week on the Research and Development expenditure credit (RDEC) scheme while we investigated what was going on and made sure we understood what the badges of that attack were. That enabled us to identify and block the relevant claims. We then restarted payments, but I am afraid, as a result of the additional checks that we now have to make before payment, we are currently not offering the 28-day turnaround. We are offering a 40-day turnaround for SME tax credits, so there has been a deliberate but unfortunate temporary deterioration of the overall service level that we can offer in order to protect the scheme.

We also expect further measures to come in next April to strengthen our ability to manage compliance. For example, businesses will have to give us advance notification that they intend to make claims. They will have to make them online and provide additional data. They will have to identify for us the names of anyone who advised them in compiling their claim, because we know which advisers push the boundaries. A named person in the business will have to certify that they are accountable for the quality of the claim. We have found, when we have gone in to investigate some high-risk claims, firms that will say, "A boutique adviser came in, helped us to claim it and then has gone. I do not really know how this claim is made up". We want to make sure that there is personal accountability. We will continue looking at what we need to do to improve compliance.

Q97 **Olivia Blake:** I will come to the measures in a moment. On the estimate, I thought it was interesting that the ONS has estimated that companies carried out £25.9 billion of R&D activity, while the Treasury's analysis suggests that companies have claimed tax relief on £47.5 billion R&D expenditure. Do you not think this may suggest that the 4.9% estimate of error and fraud might be slightly understated?

Jim Harra: I will ask Jane in a moment to explain what we have done about that. Yes, that was a cause of concern for me: that there was such a disparity between the amount of R&D in the economy that the ONS could see and the amount that was being claimed for. There can be some legitimate reasons for that. ONS looks at research and development that is going on in the UK, whereas the tax relief can cover costs that are incurred outside the UK. We did some work with ONS last month and we have published a joint paper, which closes that gap significantly. Jane can give you more on that.

Q98 **Olivia Blake:** Before Ms Whittaker responds, do you think that is a legitimate use of this sort of tax relief—for it to go to companies that are doing the research external to the UK?

Jim Harra: Some changes have been made to target that, but, if you are a large business and undertaking an element of research and development, you might well contract with an overseas lab to do some work. That is part and parcel of business. The benefit of the R&D is still accruing to a UK business and that is where the intellectual property, for example, might well reside. It is not clear cut, but nevertheless some reforms have been made, for example particularly in the small business scheme, which do more to target research and development undertaken within the UK. Traditionally, the objective has been R&D that benefits the UK economy, as opposed to activity carried out within the UK boundaries. I will pass to Jane to give you more information.

Jane Whittaker: You have made most of the points that I would have made, Jim. We have been aware of the discrepancy between the survey data from ONS on research and development and the implied total amount of research and development through the tax administrative data. It is a discrepancy that has been broadening out.

The work referred to in the published document from ONS is something that we have been actively working with it on, in terms of data sharing and understanding what elements might perhaps be missing from the survey, as well as understanding those differences in definition of what counts for tax purposes versus for survey purposes. The document is out there. There are issues around whether the survey is picking up everything that it should, as well as questions about compliance. We are actively working with ONS to resolve the position.

Jim Harra: That published document from last month demonstrates that the gap is not as wide as was first thought. In fact, ONS has now increased its estimate of how much R&D was carried out. The Government have a target to achieve 2.4% of GDP spent on R&D. It looks like that may have been achieved in 2019, based on the revised ONS figures, partly as a result of R&D—

Olivia Blake: I am just curious with all these estimates.

Jim Harra: You are right. It was a key discrepancy. It was definitely cause for concern, which is why we did the work that we did.

Q99 **Olivia Blake:** "Discrepancy" is an interesting word when it is almost double. That is quite a big difference. I accept the points you are making, but how confident are you on the new estimate that the driver is this external spend to the UK?

Jim Harra: We want to increase our certainty in our estimate. In 2020-21, we estimated 3.6%. In 2021-22, we estimated 4.9%. We do not really think that is because non-compliance worsened. It is because we have a better measure, and we are now undertaking a random enquiry programme that will give us even more certainty and might well cause us to revise that number.

Q100 **Olivia Blake:** Focusing on some of the measures that you mentioned for the small business scheme, we have had some evidence from the Chartered Institute of Taxation. On the first measure you mentioned about pre-notification that people intend to claim this, they have concerns that this could be poorly targeted because it might prevent some dubious claims but also might rule out some genuine claims that fall out of that time. They are particularly worried about smaller and newer companies, because they may not get the right tax advice in the first part of the year and would then fall out of that six months. They were concerned about that pre-notification window being six months. I wondered if you had any comments on that and whether you share their concerns.

Jim Harra: I do not have any personal insight into the specific issue, other than this is typical of the challenge that we face in policing error and fraud risks in these incentives while, at the same time, making sure that legitimate claimants can genuinely access them. It is a balancing act and a choice based on your priorities. I am sure we will be looking at how that and the other measures work in practice.

The aim is not to exclude legitimate claimants. The aim is to improve levels of compliance. We would certainly keep it under review. I am sure my colleagues are picking up on the representations. It is typical of the kinds of trade-offs that you have to make in the design of these schemes between their security and them achieving their policy objectives.

Q101 **Olivia Blake:** The other question is a value-for-money one as much as a capacity one. There is concern that this will increase HMRC's workload if there has to be this added interaction with HMRC. Are you concerned about that? Given all the priorities we have just spoken about, do you think that this is a valuable use to make sure compliance is correct?

Jim Harra: Given the scale of R&D spend and the fact that, if you look over time, Governments have wanted to make this relief more and more generous and increase its scope, it is a priority for us to manage the error and fraud risk. No error and fraud is acceptable, but keeping it within reasonable bounds is a priority for us. We are content that it is a priority for us to focus on the successful delivery of R&D, because it is a key plank of the Government's growth plan and has been for many years, but also look at it from a revenue management point of view. Because this involves expenditure, in some cases people would regard the behaviour here as particularly egregious compared with perhaps carelessly under-declaring your tax liability.

Q102 **Olivia Blake:** Moving on to corporation tax research and development reliefs, how well do you think the more recent initiatives that you have had in tackling fraud and error in that area have worked or are developing?

Jim Harra: We have increasing clarity about where the risks lie. There are two key reliefs. There is one focused on large business, where we think that the level of error and fraud is around 1%, so probably teetering on the point where I suspect it is, from an auditor's point of view, not that material. The risk that large businesses pose is that they are more likely to push the boundaries in a technical sense of what amounts to R&D.

The level of error and fraud in the small business scheme is 7.3%. That is challenging for us, because we get about 76,000 claims from small businesses every year, so that is a lot to police. We are zoning in all the time on where the error and fraud is, what the nature of the behaviour is and what the kinds of responses that you can deploy to that are. We will assess how the new measures work and, if they are not working effectively, what we need to change, or, if more is needed, what more would be needed. As I say, it is an arms race, to some extent. There is no end to it.

Q103 **Olivia Blake:** Are you setting yourself a target on what reduction you would like to see in these schemes, in terms of level of fraud and error? Is there a time period in which you would like to see a reduction in that, or are you content that you are recognising this?

Jim Harra: I am generally reluctant to have micro targets. It is part of my overall target to keep the tax gap down. It is a particular area of focus, because we see the scheme growing in scale all the time. Therefore, as an area of risk, it grows all the time. We calculate how much we think the new measures will achieve, in terms of reduction of error and fraud, and we will want to assess that that is what they produce. I am happy to look at it, but I am generally reluctant to have lots of micro targets because it reduces our flexibility about how we deploy our resources.

Q104 **Olivia Blake:** I have two more points. Going back to the Chartered Institute of Taxation's evidence, it highlighted some issues. It was worried that some of changes to accessing the scheme might be confusing to SME R&D relief applicants, around the subcontracted and subsidised wording within that. On a broader point around that, do you think that the tightening up on the abuse of the system might make accessing the relief too burdensome for some honest taxpayers? Is that a price worth paying?

Jim Harra: It is not something we want to do. If we could perfectly target measures so that they only impacted on the people that we want impacted, that is what we would do. The reality is that we cannot do that, so we have to get the balance right between adding to everyone's burden and who that impacts on. That is something we will have to keep continuously under review. We will also listen to feedback and gauge what the relative priorities are.

Q105 **Olivia Blake:** In terms of the broader aim of these reliefs, obviously they are not anything new and they have been around for a long time. Do you think that they are contributing to productivity and growth in the UK, or is this just an opportunity for it to look like we are doing something in this area?

Chair: You are a cynic.

Olivia Blake: I am a cynic—I am sorry.

Jim Harra: We have published some research into the extent to which R&D tax reliefs stimulate additional R&D. That is available and I can send you a link to that. We can demonstrate that these two reliefs stimulate more R&D than there would otherwise be. The additionality is particularly in the large business scheme. The additionality—the pound-for-pound value for money—is much more marginal in the small business scheme, but there is definitely evidence that both positively increase R&D. The UK has traditionally been seen as not having enough R&D and the Government have had a long-standing target of getting to 2.4%, which the reliefs contribute to.

Q106 **Chair:** Ms Blake is picking away at a little sore of the PAC's, as you know, about our concern about tax reliefs and how you evaluate their effectiveness. There are rather a lot of them. Publishing the list and working out whether they are effective is something—

Jim Harra: For this one, which is obviously one of the larger non-structural reliefs, we definitely have published research. I do not think that research shows what the benefit is to the UK economy, but it demonstrates directly what the additionality in terms of R&D activity is.

Q107 **Chair:** We welcome the research, because it would be good to see that on some of the other tax reliefs. I will park that one because of the late hour. On this issue of the research and development tax credit, I have a constituent—I represent Shoreditch and lots of technical businesses—that is a digital start-up company trying to claim R&D tax credit. When calling your organisation, they get a message saying, "If you are ringing about R&D tax credits, please hang up now". You have said it is a 40-day turnaround, not 28 days. If you have to hang up now, where are you measuring the 40-day turnaround from?

Jim Harra: I apologise for that. I did not realise. We do not have a helpline for that. We have R&D teams who work on the claims.

Q108 **Chair:** They have gone through the Kafkaesque system, but then, if they are ringing about R&D, they are told to hang up now.

Jim Harra: I will take that away and look at it.

Chair: Who knows? It was a few days or weeks ago. It might be out of date by now, but that was the situation.

Jim Harra: I will look at it if you send me your constituency case. On the 40-day turnaround, there was a period in May where we had to stop all payments altogether while we tackled this attack. People who were awaiting payments at that time experienced more than 40 days. For claims that were received from August onwards, 40 days is the turnaround.

Q109 **Chair:** It is good to hear you say that, because my constituent tells me that there are a number of other start-ups, not just in Shoreditch but locally, that are on the brink of bankruptcy because of the backlog in cases. Do you have anything to say about that?

Jim Harra: By 31st October there will be no backlog, but there certainly was. We committed internally that this month we would get that up to date. Claims received from 1 August have been achieving the 40 days. For claims that were received before that that were held up, that has been recovered.

Chair: That is heartening to hear. Thank you very much.

Q110 **Peter Grant:** Staying on the R&D reliefs, the audit Report says, "In 2021, HMRC introduced a new claim checking approach, supported by standardised operating procedures to ensure consistent application by caseworkers". That reads as if you had not done that until 2021. Is that correct?

Jim Harra: I do not know the detail of the changes that we introduced, so I cannot say, I am afraid, what was there before. We have always had resource dedicated to R&D claims. They are in specific units. It sounds like it is the case that we definitely did more work internally to standardise those procedures, but we always had procedures before that.

Q111 **Peter Grant:** Could you possibly write and clarify?

Jim Harra: Whereabouts is this in the Report?

Q112 **Peter Grant:** It is in paragraph 346 of the C&AG's Report. It may simply be that the procedures were updated or improved, but one interpretation of it is that the R&D relief scheme ran for 20 years before HMRC had consistent operating procedures to handle it, which I do not think is the case.

Jim Harra: I do not believe that will be the case, but I will definitely write to you.

Q113 **Peter Grant:** Going back to some of the questions from Mr French earlier on furlough fraud, as well as the economic impact, clearly there is a moral issue if people are deliberately stealing from the public purse. It is a bad thing. I had some cases—I expect most MPs did—from honest businesses in my constituency that were doing the right thing. They discovered that, in one case, their only UK competitor was not only working illegally through lockdown, which they were not allowed to do, but, through conversations with shared customers, it became obvious that they were claiming furlough for the people who were working illegally. They contacted, and I think I contacted, HMRC about it at the time.

I can understand the reasons why you cannot tell either me or my constituent very much about it unless and until a case comes forward and is heard in open court. Do you understand the immense frustration that a lot of honest businesses still feel when they know that they were put at a significant competitive disadvantage by fraudsters that, in many cases, will get away scot-free, because either you do not have the resources to chase them all, or, if you go back two years later, it is impossible to get evidence that somebody was working at a particular time?

Jim Harra: I do indeed recognise the frustration. That is the case in relation to tax non-compliance as well. Part of the reason for us policing all this is not just to protect revenues but also to create a level playing field, because that promotes good compliance by people who are willing to comply.

We have an online and telephone hotline where people can report any frauds that they suspect. We look at every single one of those reports, triage them and identify those that we think are suitable for investigation. That is the kind of behaviour that we would prioritise, but we certainly wanted, and we have stated it publicly, to target that kind of fraudulent behaviour, as opposed to genuine innocent errors, when tackling error and fraud in the Covid schemes.

I get a lot of correspondence from MPs frustrated that we will not give people feedback on what we have done with the information that they have provided. I understand that frustration as well, but that is a pretty strict rule, I am afraid, that we have. I assure you that every single allegation of fraud is looked at.

Q114 **Peter Grant:** I want now to move on to the customer service performance in the year that we are looking at. Ms MacDonald, looking at figure 8 in the Comptroller and Auditor General's Report, there are eight performance measures listed there. Seven of them have been in pretty much constant decline since 2018. One of them declined last year after a couple of years of slight improvement. How do you explain that? Why is performance declining almost across the board in the delivery of service to customers?

Angela MacDonald: As I have said in my last two appearances here, the period that you describe would hardly be described as usual times for HMRC. Through that period, we dealt with Covid. I will not rehearse the discussion I gave to you, Mr Grant, when we were here last year. Obviously, there has also been the work that HMRC needed to do to leave the European Union. There have been a variety of things that have been on the go.

Also during that time, there have been some much bigger situational changes. If you go back five years, I had 25,500 colleagues in customer services and I now have 19,500 colleagues in customer services. A number of those have been efficiencies as we have improved and moved customers digitally. When we are significantly smaller, that means that our ability to manage shocks, fluctuations and things that we did not expect against plan becomes significantly less.

We have also made some shifts to some of our methodologies. For instance, it is actually very easy to control things like average speed to answer, if you really wanted to, by simply making ourselves engaged more often. You can control the number of people that you let into the queue and keep your average speed to answer down by saying, "We think it will take you longer than five minutes and therefore we will not let you in at all".

We understood from our customers' insight that actually they would prefer to come on and wait. We have reduced by more than 50% the number of busys—we call them busys—that we play to let more people into the queue. What we are focused on and what our customers tell us is important is they would rather wait, get through to a person, so the average number that we handle is then the important number. Then they want to be confident that the service that they get is done once and done, so we measure that also. I recognise that, if you simply look at the pure charts, you can see that that is what the numbers say. It perhaps does not take into account the full circumstances of HMRC's experience during that time to simply compare the numbers at the beginning of the chart with the numbers at the end.

Q115 **Peter Grant:** Can I make sure that I have understood that answer correctly? Are you saying that, as well as the measurement of the time of people who actually get through, sometimes you basically shut the door and do not even let anybody join the queue?

Angela MacDonald: This is not simply an HMRC approach. In any contact centre anywhere, you always have a choice when you are thinking about the service that you want to offer. You can simply leave your phone lines open and people sit in the queue for as long as the queue takes to be done. That is an easy thing to do.

Many organisations, us included, will take a view that says, "If you know before they even join the queue that they are going to be sat there for a long period of time, you say, 'We are not going to do that.'" If we think that it is going to be longer than however many minutes, we will say to the customer, "The lines are extremely busy at the minute. Please call back again at a different time". That is perfectly standard industry practice.

Q116 **Peter Grant:** Do you measure and report on the number of times that that happens?

Angela MacDonald: Yes, we do.

Q117 **Peter Grant:** Is that happening more or less often than it was previously?

Angela MacDonald: The latest number is that that is happening about 5% of the time. I think it is 5.5%. That is less than it would have been. In prior years we would have played busy messages about 11% or 12% of the time. The decision that we made, because of the feedback we had from customers, is that, rather than ringing and being told to ring back, they would rather come in and wait for longer. That is what we have done.

You can absolutely go back the other way and say, "I only want people to wait a maximum of five minutes and in that case, to do that, I am going to tell more people to ring back later". Ideally, you have enough colleagues to be able to answer all the calls in a timely fashion. That would be the absolute nirvana, but in any organisation there are busy periods and quieter periods and therefore you have to try to manage the customer's experience as fairly and consistently as you can.

Q118 **Peter Grant:** If you are putting on a busy message simply for the convenience of the person trying to call in, that is fair enough. If it is being done in order to reduce the measured waiting time, it is fiddling the figures.

Angela MacDonald: That is exactly right, which is why I do not do it.

Jim Harra: To be clear, we do not do it, but in previous years we did have a policy of playing a busy tone rather than let people join very long queues. That is why, when you compare waiting times year on year, you are not actually comparing like with like. Our current policy is that we let people into the queue and do not target ourselves on call waiting times. We target ourselves on the percentage of callers who want to speak to an agent who succeed in speaking to an agent. That is an indicator that cannot be manipulated by that kind of behaviour that Angela has described.

The service standard I would like us to hit is that 85% of customers who need to speak to an agent can get through to an agent the first time they call. We are not currently achieving that. We are currently achieving about 77%.

Angela MacDonald: Yes.

Jim Harra: That has improved over the course of the year but still falls short of the standard I would like to offer people.

Q119 **Peter Grant:** Is the decision to put on the busy message taken centrally? Are there only certain senior people who are authorised to do that, or can individual call handlers put on the busy?

Angela MacDonald: Oh gosh, no. We have a set of standards around the overall length of queues. Those are not more real time. Obviously if there is an emergency you may have to shutter the calls, but these are longer-term plans. They are based on an understanding of what customers are typically comfortable tolerating. There is a point at which, on some queues particularly, customers will be prepared to wait longer and on others you see that, after a while, the abandon rate goes up, because people have waited longer than they were comfortable with.

You are trying to find the balance of letting people into the queue and making sure that they can get to speak to somebody, but recognising that tipping point at which typically people will put the phone down. In that case, you may as well have known that in advance and not made them wait the 15 or 20 minutes to then decide that they were going to put the phone down. Does that make sense? It is a modelling question, not a, "I personally do not want to answer the phone" question, if that helps.

Q120 **Peter Grant:** I will go back to the comment Mr Harra made earlier on about when it is efficiency and when it is a cut. It is very clear from the answer that you gave particularly about a significant reduction in staff numbers and customer service that a big part of that can now be seen to be a cut in the quality of customer service, rather than an efficiency, can it not?

Angela MacDonald: I do not think that is fair. We have definitely, over the period that you talk about, put in significant digital changes to improve efficiency. During this period of time, there have been quite a lot of other things that we are doing. If I refer you back to when we were here last year, for the first half of 2021-22 we were still managing the Covid schemes. As I think I have shared with you when I was here last time, that was a material usage of HMRC resources.

I said at that point that our telephony situation was there or thereabouts back on an even keel but we had a large backlog of post, 3.3 million items. I said that we were going to successfully manage the self-assessment peak, which was January, and get ourselves back down to a standard head of work, which is about 2 million items, which is about four weeks' work. We were going to do that by March 2022 and that is exactly what we did.

It is always a tight balance in any large service organisation to manage the variety of different things that we have to manage, and we do that. Yes, I would always want more staff. I would always want it to be a little less tight than it is, but we still maintain all our services to as good a service level as we can. I know last year you asked Jim what he thought good service was. We are doing the best that we can, but we need to keep focusing on the fact that there are more opportunities to digitalise the customer experience.

We are already a largely digital organisation and the answer is not to put more people on phones and post. A lot of phones activity is people seeking reassurance, seeking information, chasing and following up with things. We do not want to answer the phone more often. We ideally want to take that away from that needing to be done in the first place by reducing demand.

Q121 **Peter Grant:** I mentioned the eight customer service performance measures, all of which have been declining. Seven of those eight declined between 2018-19 and 2019-20. Unless there was a massive fall in performance in the last couple of weeks of March 2020, at the very beginning of Covid, you cannot blame that decline on Covid. Between those two years, for example, the percentage of customers who waited more than 10 minutes to speak to an adviser increased from just under 20% to almost 30%. That was not caused by Covid. That can only have been caused by something that was already happening within HMRC.

At what point do we, on behalf of customers of HMRC, need to be knocking on the door of the Treasury and saying, "These efficiency savings are not efficiency savings. You are forcing Departments to cut service to our constituents"? Are those discussions that you have with Treasury? Do you make representations to say, "We can achieve this by efficiencies", which, in my book, means "The customers will not notice the difference"? If we have to reduce budgets by this amount, it will become a cut in customer service and the customers will notice the difference. Do you have those conversations with the Treasury?

Jim Harra: Yes, we do. For example, in our spending review settlement, in return for the funding that we get from Treasury, we set out what it is that we believe that we can deliver in performance levels, whether that be customer service or managing the tax gap.

A challenge with some of our customer service demand, as Angela mentioned, is that it is difficult to justify servicing that demand, because the answer is that we should not have it. We get a lot of phone calls from people that we have to deal with where the thing they want to do is available in their online personal tax account or available on the mobile app. Therefore, we have to channel people into that. We have work that we do or that can be dealt with by a digital assistant, and we have to keep developing our digital assistant to be able to handle more of those calls.

Similarly, on the correspondence side, a very large part of the correspondence increase that we are dealing with is claims that people are making for small expenses, which can be done online, but a lot of which come in in non-standard paper formats, which are inefficient for us to process. It is inevitable that Treasury will say, "We will fund you to modernise that, rather than fund you on an ongoing basis to manage that in a very inefficient way". The challenge for HMRC is actually to do that.

Q122 **Peter Grant:** It almost sounds as if you are blaming the customers for wanting to speak to a human being, rather than interacting online.

Jim Harra: No, I am not blaming anyone. I know that there will be customers who will always need to speak to someone, either because they are unable to deal with us digitally or because of the nature of their inquiry. A lot of the demand that we get that is what I would call low-value demand and is driven by our own processes, so it is for us to reform those processes, so that customers find it easier to self-serve or find that they do not need to do this at all. I do not intend to do that, but, I am afraid, when it comes to making the case for more funding, Treasury has to make choices across the whole of Government. For me to have more funding to answer phone calls, which I would admit are low-value very often, is very difficult to do.

Q123 **Chair:** There are a last couple of things from me. We talked earlier, at the beginning, about the tax compliance targets. I wanted to pin down that you are going to write to us with that. I think we discussed it at the beginning. Are you okay to write to us with the tax compliance target for 2023?

Jim Harra: Do you mean the £36 billion? Yes, of course.

Q124 **Chair:** It was right at the beginning. I was not quite sure I had nailed it down. It would be quite helpful, Ms MacDonald, if you could write to us with the long-term data sets or some information about that data that you measure on busy calls.

Angela MacDonald: Yes, I am happy to.

Q125 **Chair:** It has been quite a revelation. I have a quick one on that. Do you have a call-back system? I have not rung you for a long while—there you go—because the digital must be working to some extent. If someone wants to be called back, do you have that system?

Angela MacDonald: That is a really good question, which has evaded my brain right now. I will write to you with that one as well. I will include more details for you on that.

Chair: It has been a hot, long session, but calmer than what is going on in the rest of Westminster.

We will be producing a short report on this in the next few weeks, depending on whether we have an election. I am only half-joking. Can I thank our witnesses very much indeed? The transcript will be up on the website uncorrected in the next couple of days. Thank you to our colleagues at Hansard for that.