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Summary

Since March 2020, HM Revenue & Customs (HMRC) has had to implement a vital part of the government response to the COVID-19 pandemic, to help as many people as possible as fast as possible. We recognise the hard work and dedication of HMRC staff in rising to the challenge under difficult circumstances. The Department has already provided more than £80 billion as part of a wider package in support to businesses and individuals, including through the employment support schemes. However, despite HMRC's efforts, some groups have not received from financial support offered to other taxpayers.

The demands created by the pandemic have put a huge strain on HMRC's day to day operations and the pandemic has had a significant impact on HMRC's performance, in terms of, for example, falling tax revenues, poorer customer service, reduced compliance activity and increased debt balances. HMRC has yet to establish the full impact of COVID-19 and the support schemes on tax receipts. On top of the constant need for maintaining and improving its administration of the tax system, HMRC already faced a number of strategic challenges: its progress and plans to transform the tax system and its preparations for the end of the transition period following the UK's exit from the EU. The pandemic has significantly increased HMRC's workload and its complexity. The Department will need to review whether it has the resources and capacity to deliver on all of its commitments.

Introduction

HMRC is responsible for administering the UK's tax system. HMRC's objectives are to: collect revenues due and bear down on avoidance and evasion; transform tax and payments for its customers; and design and deliver a professional, efficient and engaged organisation. In 2019–20, HMRC raised £636.7 billion of tax revenues, an increase of £8.8 billion (1.4%) since 2018–19. It estimates the yield from its tax compliance activities in 2019–20 was £36.9 billion, 7.0% above its target (£34.5 billion). As well as its traditional objectives, the Department is playing a significant role in implementing the government's response to the COVID-19 pandemic. The primary support measures for individuals and businesses administered by HMRC include: grant-paying measures, such as the Coronavirus Job Retention Scheme and the Self-Employment Income Support Scheme; measures to defer payment of tax liabilities, such as deferring VAT payments; and other tax measures, such as a VAT cut from 20% to 5% on food, accommodation and attractions. HMRC is also responsible for administering Personal Tax Credits to support families with children and to help ensure that work pays more than welfare. In 2019–20, HMRC spent £18.3 billion on tax credits. Tax credits supported around 2.3 million families and around 4.4 million children. The government, as part of its COVID-19 support measures, increased the working tax credits from 6 April 2020 until 5 April 2021; which could mean up to an extra £20 each week for claimants or households.

Conclusions and recommendations

1. **Quirks in the tax system have left some groups of taxpayers excluded from financial support that other taxpayers received throughout the COVID-19 pandemic.** We are concerned that some self-employed taxpayers may have moved onto payrolls because of HMRC's IR35 rules, but were not employed at the relevant time, and so lost eligibility to COVID-19 support schemes. Some of those who moved onto payrolls, because of the pre-emptive actions of employers, could have benefited through the Self-Employment Income Support Scheme had they remained self-employed. Similarly, some other freelancers, with verifiable employment and tax records visible to HMRC, may also have been excluded from the Coronavirus Job Retention Scheme (CJRS). In some sectors, such as the creative industries, it is common for freelancers to work on a series of short-term employment contracts with gaps in between. HMRC maintains that it has been as flexible as possible, for example, by allowing, for the purpose of eligibility to the COVID-19 support schemes, the extension of short-term contracts and rehiring of employees who were made redundant. Meanwhile, some large companies that have received support from government during the COVID-19 crisis have continued to pay out dividends and high executive salaries.

   Recommendation: ***HMRC should, within six weeks of this report:***

   - ***publish an explanation for the reasons why it cannot help those freelancers and other groups that have been excluded from receiving any support and what would be required to determine eligibility for financial support for that group of taxpayers; and***
   - ***consider the support it can provide for those taxpayers that have, due to the IR35 rules, moved onto payrolls and missed out on support from the COVID schemes, for example, by reviewing whether it can use an average of wages in the past three years to determine grants.***

2. **A lack of certainty about the COVID-19 support schemes has undermined businesses' ability to plan effectively.** We recognise that it is not easy to provide support to everyone considering the unique circumstances of each individual and business. However, the uncertainties around the timings and details of schemes have made a difficult situation more uncertain for those in need of urgent support. For example, HMRC could not provide clarity on whether the Job Retention Bonus scheme had been delayed or scrapped. Such lack of clarity may lead to unnecessary hardships for some businesses, who in good faith were relying on the payments from the scheme to meet some of their needs. HMRC's lack of timely evaluation of schemes, such as the Eat Out to Help Out (EOTHO) scheme, to inform possible future iterations of the initiatives may also result in delays to their reintroduction and hinder their effectiveness.

   Recommendation: ***HMRC should, within six weeks of publication of this report, write to us to set out what lessons have been learned from the timing and content of its communications, such as about the future of the Job Retention Bonus scheme, and how those lessons might have improved the outcomes of the support schemes.***

3. **HMRC's estate strategy risks becoming woefully out of date.** Our long-standing concerns about HMRC's non-breakable long-term property leases have become all the more relevant, and prescient, given the COVID-19 pandemic. In April 2017, long before COVID-19, we raised our concerns about HMRC locking government into holding larger properties for longer than needed. We raised similar concerns again in January and April 2018. Yet HMRC persevered. HMRC's view is that its regional centres are located in prime sites and it can, therefore, lease them out to the private sector and other government departments if they have spare capacity. We strongly believe this is an out of date assumption that needs urgent revision in light of changing economic conditions. It is commonly accepted that some significant changes in working practices, with more staff working flexibly and less need for traditional office space, are likely to be here to stay.

   Recommendation: ***In its Treasury Minute response, we expect HMRC to set out its future plans on how it will review its estate strategy in light of the impact of COVID-19 on the demand for commercial properties, to ensure it can demonstrate value for money from its considerable investment should demand remain suppressed.***

4. **The pandemic has significantly increased HMRC's workload and made the organisation more complex.** HMRC has had to reallocate a significant number of its staff to work in COVID-19-related roles. At its peak, in May 2020, HMRC reallocated more than 9,000 (16%) of its staff. HMRC is facing a huge operational challenge. It is responsible for tackling a growing debt balance (while being sensitive to the hardships faced by taxpayers due to COVID-19), error and fraud in the COVID-19 employment support schemes, restoring its usual level of enforcement and compliance activities and pursuing its transformation plans. This is on top of dealing with the demands of EU Exit, on which more than 6,000 HMRC staff worked in 2019–20. HMRC also has to maintain and improve its customer services performance while facing increasing demand for its limited resources from other parts of its business. To achieve its objectives HMRC has published a 10-year strategy for modernising the tax administration system. However, short-term Spending Reviews, like the one in November 2020, may not provide HMRC with the opportunity to achieve a financial settlement commensurate with its long-term responsibilities, needs and ambitions.

   Recommendation: ***HMRC should review its priorities and work with HM Treasury to ensure it has sufficient capacity and resources to effectively manage its workload. HMRC should, following the November 2020 Spending Review, write to us, setting out the findings of its review and explaining what it might need to deprioritise if it has not secured sufficient additional resources.***

5. **HMRC has spent too much of its IT budget on patching up legacy systems rather than modernising them.** The COVID-19 pandemic has shown the importance of an effective tax administration system. There is a strong case for investment in a modern IT system. Of the additional costs incurred by HMRC as a consequence of the pandemic, the largest element, as of 11 September 2020, was the cost of IT at £53.2 million (80%). HMRC says that it has made some progress in its ambitious digital transformation but is looking for opportunities to reduce the risks facing its IT systems so that they are kept up to date and safe from cyber-attacks and

catastrophic losses. The Department accepts it should redress the balance between spending too much on legacy systems and not enough on investing for the future. Since we took evidence, HMRC secured £268 million in the November 2020 Spending Review to fix its outdated IT, to ensure its core systems are secure and support better administration. It remains to be seen whether this is sufficient to urgently address the long-standing issues the Department has identified.

Recommendation: ***HMRC should write to us, by the end of March 2021, setting out what it is doing, and has planned, to refocus IT investment on modernisation for the future, while retaining resilience, so it can move on from the need to simply keep patching up legacy systems.***

6. **HMRC too often struggles to provide reliable and timely financial estimates upon which good financial and operational planning depends.** HMRC is responsible for dealing with vast sums of public money, both revenue and expenditure. Reliable and timely financial estimates are vital if it is to manage and allocate resources effectively, assess and report on its progress, judge how much it can afford to do, and consider where it needs to adjust its focus and interventions. Yet we have seen numerous examples where it has struggled: for example, its estimates of Corporation Tax revenues needed to be retrospectively amended by £6.6 billion in 2019–20; it exceeded its cash requirement control total by more than £700 million because of basic errors in financial forecasting; it is uncertain what its estimate of fraud and error from tax credits should be; and there has been a delay in producing a more rigorous estimate of the level of fraud and error associated with the Research & Development relief. On understanding the impact of COVID-19, HMRC is falling behind where it needs to be. For example, it is some way off being in a position to better assess the actual level of error and fraud from the employment support schemes, with planning estimates ranging from 5% to 10% on the Coronavirus Job Retention Scheme; and it has no estimates of error and fraud from the Eat Out To Help Out scheme, despite the scheme having ended in August.

Recommendation: ***HMRC should, in its Treasury Minute response, set out:***

- ***the steps it is taking to ensure its financial estimates are sufficiently timely and rigorous; and***
- ***when it will have an estimate of the actual amount of error and fraud in the COVID-19 grant schemes it administers, rather than a planning estimate, and its plans for recovering those losses.***

1 COVID-19 support schemes administered by HM Revenue & Customs

1. On the basis of a Report by the Comptroller and Auditor General, we took evidence from HM Revenue & Customs (HMRC) on its performance in 2019–20.[1]

2. HMRC is responsible for administering the UK's tax system, reporting total tax revenue of £636.7 billion in 2019–20, an increase of £8.8 billion (1.4%) since 2018–19. HMRC's objectives are to: collect revenues due and bear down on avoidance and evasion; transform tax and payments for its customers; and design and deliver a professional, efficient and engaged organisation.[2] While most tax revenue is paid to HMRC without the need for further intervention, some is only received as a result of specific compliance and enforcement activities. Compliance yield measures the effectiveness of these activities. HMRC estimates the yield from its tax compliance activities in 2019–20 was £36.9 billion, against a target of £34.5 billion. HMRC is also responsible for administering Personal Tax Credits. In 2019–20, HMRC spent £18.3 billion on tax credits.[3] The most recent available estimates suggest that overpayments by HMRC decreased from 5.5% (£1.41 billion) of expenditure on tax credits in 2017–18 to 4.9% (£1.11 billion) in 2018–19, meeting HMRC's target for error and fraud overpayments to be below 5%.[4] In 2019–20, HMRC met three of its eight customer service performance targets.[5] HMRC missed its two targets for speed of answering telephone calls, its two targets for speed of response to tax correspondence and its target for speed of response to i-forms and secure emails. From March 2020, because of the COVID-19 pandemic, there was an increase in the average time HMRC took to answer telephone calls, peaking at 14:59 minutes in May and improving to 9:15 minutes in June 2020.[6]

3. HMRC faces a number of strategic challenges, specifically: its implementation of the government's response to the COVID-19 pandemic and the impact of COVID-19 on its operations; its plans to transform the tax system; and its preparations for the end of the transition period following the UK's exit from the EU. HMRC is responsible for administering significant aspects of the government's response to COVID-19, incurring an estimated cost of over £80 billion to support businesses and individuals.[7] In 2015, HMRC set the ambition of transforming itself to become one of the most digitally advanced tax administrations in the world. HMRC aims to move to a fully digital tax system where all individuals and businesses can see their tax affairs in one place and carry out transactions digitally.[8]

1 Report by the Comptroller and Auditor General, *HM Revenue & Customs Annual Report and Accounts 2019–20*, HC 891, 5 November 2020
2 C&AG's Report, para 1, 3 & 4
3 C&AG's Report, para 6, 3.1 & 3.2
4 Q 83; C&AG's Report, para 16
5 C&AG's Report, para 7 & 2.28
6 C&AG's Report, para 2.28
7 C&AG's Report, para 3 & 9
8 C&AG's Report, para 2.33

COVID-19 support schemes and the exclusion of some taxpayers

4. HMRC is playing a significant role in implementing the government's response to the COVID-19 pandemic. For example, as of 20 September, the Coronavirus Job Retention Scheme (CJRS), which HMRC administers, had allowed employers to furlough 9.6 million employees at a cost of £39.3 billion. The Self-Employment Income Support Scheme (SEISS), as at 20 September, had seen 4.8 million claims totalling £13.4 billion to support the self-employed.[9] We asked HMRC about firms that have received large amounts of support though the CJRS scheme but continued to pay dividends or high executive salaries. HMRC told us that while it expects companies to claim support only if they need it, there is no fixed rule about their arrangements for paying executive salaries or dividends.[10] HMRC confirmed to us that it is possible to attach eligibility conditions to the support schemes but that it is difficult to define conditions that prevent undesirable practices without also affecting aspects of the support schemes that are considered necessary.[11]

5. We questioned the Department about taxpayers who had not been able to receive any help from the COVID-19 support schemes because they were complying with HMRC's 'IR35 rules', which govern off-payroll working. If they had been able to continue to be self-employed, they might have had the opportunity to claim support under the SEISS measure.[12] HMRC explained to us that the 'IR35 rules' only apply to people for whom the nature of their work engagement is employment.[13] HMRC stressed the point that the 'IR35 rules' do not apply to anyone who is self-employed.[14] In 2018, the NAO had examined the nature of, and associated issues related to, individuals the BBC hires on a freelance basis and highlighted some of the uncertainties and difficulties around the interpretation and application of the 'IR35 rules'.[15] We pointed out that such excluded taxpayers have tax and employment records visible to HMRC.[16]

6. We also questioned HMRC about the exclusion of some other freelancers, particularly from the creative industries, who, for similar reasons to those "forced" onto payrolls by the 'IR35 rules', had not been able to receive any help. Some freelancers, due to the nature of their job, often move from one job to another on relatively short-term employment contracts and due to the bad luck of not having the "right dates" on their contracts had missed out on support that their colleagues in the same industry had received.[17] The Department acknowledged it had not been able to help everyone through the support schemes.[18] It did, however, explain to us that it took a number of steps in the design of the CJRS measure to allow as many people as possible to be eligible for support. For example, if someone who worked on a series of short-term contracts had a contract in place when the furlough scheme started, their employer could extend that contract and furlough the

9 C&AG's Report, para 9 & 2.2
10 Qq 1–2
11 Q 3
12 Qq 5–6
13 Qq 5–6; Guidance on understanding off-payroll working (IR35) available at: www.gov.uk/guidance/understanding-off-payroll-working-ir35#who-the-rules-apply-to
14 Qq 5–6
15 C&AG's Report, *Investigation into the BBC's engagement with personal service companies*, Session 2017–2019, HC 1677, 15 November 2018
16 Q 9
17 Qq 8, 10–11
18 Qq 8, 13

person during the period of COVID-19, even though in normal circumstances the contract would have ended. HMRC had also allowed employers to rehire those made redundant and then furlough them.[19]

7. Following our evidence session HMRC added that people with more than one employment can be furloughed simultaneously by different employers and that eligible employees can be on any type of employment contract, including "IR35, umbrella company and agency working". With the CJRS extension, the cut-off date has moved from 19 March to 30 October and the requirement to have been previously furloughed has been removed. Some people are ineligible for CJRS or SEISS because of policy choices, for example, it was decided that self-employed people with profits over £50,000 would not qualify for SEISS. HMRC added that, in other instances, the design of the tax system and operational constraints have meant that it had been unable to deliver help at speed and with manageable error and fraud risks. For example, the most recent complete set of self-employment data held by HMRC is for the 2018/19 tax year, meaning that the Department did not have up to date data which it could have used to determine SEISS entitlement for everyone who started self-employment more recently.[20] HMRC confirmed to us that it has no plans to do further work on new schemes for people who have not been able to benefit either from the CJRS or the SEISS measures.[21]

Lack of certainty about the support schemes

8. HMRC is responsible for administering several government interventions in response to COVID-19. These include: grant-paying measures, such as the Coronavirus Job Retention Scheme and Eat Out to Help Out; measures to defer payments of tax liabilities, such as deferring VAT and self-assessment payments; and other tax measures, such as a VAT cut from 20% to 5% on food, accommodation and attractions. The Office for Budget Responsibility (OBR) has published estimates for the costs of COVID-19 measures. It estimates the costs of measures administered by HMRC, apart from the extra cost of the extension to the CJRS measure, at more than £80 billion.[22]

9. We asked HMRC whether it had carried out any evaluation of the Eat Out to Help Out scheme to inform its possible reintroduction.[23] The scheme allowed customers, at participating establishments, to get a 50% discount on food or non-alcoholic drinks to eat or drink in (up to a maximum of £10 discount per diner) every Monday, Tuesday and Wednesday between 3 and 31 August 2020.[24] HMRC told us that HM Treasury will announce in due course its plans for evaluating the Eat Out to Help Out and other COVID-19 support schemes. The Department explained the purpose of the Eat Out to Help Out scheme was to increase demand in the restaurant sector. HMRC told us that, while there is some evidence to show this had been achieved, there will need to be a fuller evaluation of how well the scheme worked, the error and fraud risk and whether the scheme had achieved value for money.[25]

19 Qq 5–6, 8
20 Letter dated 3 December from HMRC Permanent Secretary to Chair
21 Qq 9, 11
22 C&AG's Report, para 2.2 & Figure 10
23 Qq 29, 35–36
24 Q 31; C&AG's Report, Figure 10
25 Qq 29, 31–33

10. We asked HMRC whether the Coronavirus Job Retention Bonus scheme had been cancelled or just delayed.[26] The scheme would have granted a one-off payment to employers of £1,000 for every employee who they previously claimed for under the Coronavirus Job Retention Scheme and who remained continuously employed through to 31 January 2021. The OBR had estimated the scheme would cost £6.1 billion. This was lower than HM Treasury's estimated cost of up to £9.4 billion because the latter estimate represented a maximum rather than a central estimate, so the figures are not directly comparable.[27] HMRC told us that, as the CJRS measure was originally planned to stop at the end of October, the bonus scheme was meant to have then provided an incentive for employers to keep people on their payrolls. But because the CJRS measure had now been extended to 31 March, the Chancellor announced there was no need for the incentive of a bonus payment in January.[28] HMRC recognised our concerns about businesses' ability to meet their tax liabilities without any payment from the bonus scheme but reiterated the reasons the scheme was no longer proceeding. HMRC explained that there has been no announcement about the arrangements that will be in place once the CJRS measure has expired.[29] HMRC subsequently told us that, as the original purpose of the Job Retention Bonus had fallen away with the extension of the CJRS scheme, the Government had announced on 5 November 2020 that the Job Retention Bonus would not be paid in February 2021 and that it would redeploy a retention incentive at the appropriate time.[30]

26 Qq 38–39
27 Letter dated 3 December from HMRC Permanent Secretary to Chair; C&AG's Report, Figure 10
28 Q 38
29 Qq 38–40
30 Letter dated 3 December from HMRC Permanent Secretary to Chair

2 The impact of COVID-19 on HMRC's operations

HMRC's estate strategy

11. "Building Our Future Locations" is one of the major programmes in HMRC's transformation portfolio. It consists of creating 13 regional centres, redeploying staff and disposing of buildings.[31] In terms of the impact of the COVID-19 pandemic on HMRC's plans for these regional centres, the Department told us that it remains committed to reforming its office estate and its overall strategy has not changed. HMRC explained that its legacy of a large number of small offices no longer fits what it needs as a modern tax authority. There have been some delays to the programme because of the impact of the pandemic on the construction industry but the Department continues to make progress.[32] Its Annual Report notes that 12 sites for its new regional offices have been secured, nine centres are being built and fitted out, and three are already open (in Croydon, Bristol and Belfast).[33]

12. We questioned the Department on its policy of entering into non-breakable 25-year lease agreements, which we had criticised in the past. We wanted to know whether the impact of the pandemic on the commercial property market, such as falling rents as a result of reduced demand for space, had made its policy even more unwise. We stressed that it was strange for it not to be looking at taking shorter leases.[34] In April 2017, long before COVID-19, we raised our concerns about HMRC locking government into holding larger properties for longer than needed. We raised similar concerns again in January and April 2018.[35]

13. We asked the Department if it had taken on any more leases on a 25-year non-breakable basis in the last year. HMRC said its estate strategy had not changed in the last year and it did not think it had taken on any more 25-year leases but it would need to check.[36] It subsequently confirmed that the only new 25-year lease with no break since the April 2018 evidence session was for the regional centre in Nottingham, signed in November 2018. The only other new leases since April 2018 have been for specialist sites in Worthing and Ipswich. Worthing will be a 17-year lease and Ipswich (which is a refurbishment of part of an existing building) is three leases for different floors, each for 15 years with breaks after ten years.[37]

14. Following our April 2018 session we had questioned whether the regional office deals HMRC had struck would offer sufficient flexibility to cope if plans did not work out as intended.[38] In our 2020 evidence session HMRC told us that it expects to have more

31 C&AG's Report, Figure 18
32 Qq 66, 69
33 HMRC, Annual Report and Accounts 2019 to 2020, HC 891, November 2020
34 Qq 68, 70–71
35 Committee of Public Accounts, *The HMRC Estate*, Fifty-third Report of Session 2016–17, HC 891 ,29 April 2017; Committee of Public Accounts, *HMRC's Performance in 2016–17*, Twelfth Report of Session 2017–19, HC 456, 12 January 2018; Committee concerns raised in the April 2018 evidence session summarised in letter dated 6 June 2018 from Chair to HMRC Permanent Secretary
36 Q69
37 Letter dated 3 December from HMRC Permanent Secretary to Chair
38 Committee concerns raised in the April 2018 evidence session summarised in Letter dated 6 June 2018 from Chair to HMRC Permanent Secretary

flexible working arrangements for its staff in the future, which will reduce its need for office space. It acknowledged that many more of its staff are likely to spend, say, two or three days a week working at home if they want to, and that this would affect the amount of office space it needed. However, the Department explained that in general its regional centres are "government hubs" that provide a great deal of flexibility in terms of who occupies them. For example, HMRC told us that it currently lends some of its estate in Croydon to the Department for Work & Pensions.[39]

15. HMRC told us it still believed the most cost-effective way of getting good deals in the property market is to enter into long-term leases. The Department explained to us that its regional centres are in "attractive locations" and if it transpired that it needed less space because of the COVID-19 pandemic, it believed that space would be "readily lettable" to other government departments or the private sector.[40] HMRC assured us subsequently that, where possible and in keeping with commercial reality, it has negotiated flexibility, such as subletting and sharing of occupation arrangements, into its leases. The Department told us that all of its transactions had been scrutinised and endorsed by qualified Chartered Surveyors, external to government, to demonstrate that, on the terms negotiated, HMRC had achieved value for money over the full term of the leases.[41] We asked the Department to agree to take the impact of the pandemic on the commercial property market into account before taking on any more long-term leases and HMRC confirmed that it would.[42]

16. We asked the Department to write to us about how its recruitment and location policy would reflect the 'levelling-up agenda'.[43] HMRC subsequently wrote to us to explain that it was supporting the government's levelling-up agenda by helping ensure the Civil Service was spread more widely across the UK. HMRC told us that, in future, its staff would be based in a network of large regional centres, specialist sites and transitional sites across every region and nation of the UK and that it would concentrate recruitment in these locations. Eleven of HMRC's regional centres (Manchester, Birmingham, Leeds, Newcastle, Bristol, Nottingham, Liverpool, Cardiff, Edinburgh, Glasgow and Belfast) are identified as Places for Growth.[44]

HMRC's workload

17. COVID-19, and HMRC's role in the government's response, has had a significant impact on the Department's operations. Most of HMRC's staff are working from home and it has reallocated many of them to support the COVID-19 measures. HMRC told us that customer service performance levels suffered as soon as it had to divert resources to deal with the implications of COVID-19.[45] At the peak, in May 2020, 9,097 staff (16% of its total workforce of 58,592) were reallocated to COVID-19-related roles.[46] When we asked HMRC why it had struggled to provide a good level of customer service even before the

39 Qq 66–68, 71
40 Q68
41 Letter dated 3 December from HMRC Permanent Secretary to Chair
42 Q 70–71
43 Q73
44 Letter dated 3 December from HMRC Permanent Secretary to Chair; Further detail on Places for Growth can be found on the Office of Government Property website available at: www.gov.uk/government/groups/office-of-government-property-ogp
45 Qq 20, 52–53; C&AG's Report, para 13
46 Q 53; C&AG's Report, para 2.22

emergence of COVID-19, the Department told us about problems in its recruitment in the first half of 2019–20, which meant headcount was approximately 8% below where it should have been.[47]

18. In terms of its compliance work, restrictions on travel and social distancing have affected HMRC's ability to visit taxpayers and many businesses have not been operating. HMRC told us that while it has restarted some of its criminal investigations, it has put its more routine compliance work that involves visits to taxpayers' premises on hold. The Department did point out, however, that the vast majority of its compliance work is done remotely and does not require visiting premises.[48] Nevertheless, HMRC confirmed that it will collect less compliance through its compliance activity in 2020–21 than in did in 2019–20.[49] We asked HMRC about the impact of the pandemic on tax receipts and the effect of this on its compliance activities. HMRC told us that the economic impact of COVID-19, in reducing incomes, and government measures to defer payment of certain taxes, will lower tax receipts in 2020–21. The Department told us that the Office for Budget Responsibility expects a reduction in receipts in both this year and future years.[50] While COVID-19 is an unprecedented event, HMRC told us its experience of the 2007 financial crisis suggests that, in a period of economic downturn, the tax gap is not necessarily affected significantly, with the exception of one element. That one element being 'non-payment' mainly where people or businesses become insolvent without paying their taxes.[51]

19. HMRC told us that it has a significant debt balance, about £27 billion, which is not in any payment arrangement and has increased mainly as a result of policy decisions to allow taxpayers to defer their tax payments. HMRC aims to get as much of the balance as it can into "managed payment arrangements" and to minimise its exposure to losses through insolvencies. HMRC said its intention was to allow taxpayers as much time as they need to pay their tax, and to try to avoid bankruptcy or insolvency except "as a very last resort on non-viable taxpayers". HMRC highlighted the very high compliance rates, about 90%, of its 'time-to-pay' instalment arrangements to recover tax debts, which allow it to collect the vast bulk of outstanding taxes and to minimise the number of insolvencies.[52] In the early stages of the COVID-19 lockdown, HMRC had suspended all of its debt recovery actions to recognise the struggles faced by taxpayers as a result of the pandemic. The Department told us that more recently it has restarted it debt recovery operations, targeting businesses that its data suggest ought to be able to pay their tax liabilities.[53]

20. We asked HMRC about it plans to tackle fraud and error in the COVID-19 support schemes while ensuring the timely payments of support to those in need. HMRC explained that it has to strike a balance between helping as many people as it could, as fast as possible, while also managing the risks of fraud and error. HMRC mitigated some of the risks at the design stage of the schemes by making any support contingent on the data it already held about employers, employees and the self-employed. It was also able to identify very high-risk claims in the period of approximately 72 hours between a claim being made and payments being processed. HMRC told us it had stopped about £63 million-worth of payments during that period. However, it will have to manage the remainder of any

47 Qq 59–60
48 Q 58; C&AG's Report, para 13
49 Qq 102–103
50 Qq 20–21; C&AG's Report, para 2.16
51 Qq 21, 57
52 Qq 21–23
53 Q 26

fraud and error after payments have been made, over a period of time.[54] We asked the Department about what it considered was an acceptable level of fraud in the schemes it administers. HMRC told us that no fraud is tolerable. However, in the case of the CJRS it had made a planning assumption that the level of fraud and error in the scheme could be between 5% to 10%. The lower end of the estimated level of fraud and error would be in line with the estimated levels of fraud and error in tax credits and the tax system (HMRC's latest available estimate of the tax gap in 2018–19 was 4.7%). The upper level of HMRC's estimate of fraud and error in CJRS, however, was significantly higher than comparable estimates and it would be "very unwelcome" to HMRC.[55] HMRC explained to us that it faces a "multi-dimensional" challenge, in terms of administering COVID-19 support schemes, dealing with the end of the UK's EU Exit transition period and modernising the tax system whilst still maintaining business as usual performance.[56] To help achieve its objectives HMRC has published a 10-year strategy for modernising the tax administration system.[57]

54 Q 42; C&AG's Report, para 2.13

55 Q 43; HMRC's statistics and methodological annexes relating to measuring tax gaps available at: www.gov.uk/government/statistics/measuring-tax-gaps

56 Qq 62, 65

57 The government's 10-year strategy to build a modern tax administration system available at: www.gov.uk/government/publications/tax-administration-strategy

3 IT modernisation and financial estimates

HMRC's IT infrastructure

21. As HMRC moves towards a fully digital tax system, the capability of its IT systems, including in terms of cyber security, will become increasingly important to HMRC's ability to operate effectively. HMRC has recognised that, due to the need in the past to forgo operational maintenance and upgrades to its systems to secure cost savings, its IT systems now constitute a significant risk to the Department.[58] We asked HMRC about the impact of the relatively poor state of its IT infrastructure on the cost-effectiveness of its administration of the tax system. HMRC told us that it is important that it has sufficient investment to modernise its IT estate as well as continue to maintain its legacy systems to ensure they are kept up to date and are safe from cyber-attacks and catastrophic losses. In the case of its legacy systems, 'patching' is a never-ending process.[59]

22. HMRC told us that it spends too much of its IT budget on maintaining its legacy estate and not enough on investment for the future and modernisation. The Department will seek funding opportunities, such as Spending Reviews, to modernise its systems. HMRC's experience of implementing the COVID-19 schemes showed the importance of having up-to-date technology and data in overcoming any constraints in supporting those in need.[60] Of the extra costs incurred by HMRC on COVID-19-related work, as of 11 September 2020, the largest element was the cost of IT at £53.2 million (80%).[61] HMRC highlighted self-employed taxes as an area where data and technology infrastructures had not kept pace with developments since they were put in place in the mid-1990s.[62]

23. We asked about the success of the Department's transformation plans following the ambition it set itself in 2015 to "become one of the most digitally advanced tax administrations in the world". HMRC considers that, although it is not the most digitally advanced tax administration in the world, it has made significant digital advances since 2015. For example, 22 million people have an online personal tax account.[63] HMRC, in July 2020, published a 10-year strategy for modernising its tax administration. The Department told us that the government has already agreed to provide HMRC with about half a billion pounds of funding for its plans to modernise income taxes through the Making Tax Digital initiative.[64] HMRC, in dialogue with HM Treasury, will continue to present the case for further investments to achieve the vision set out in its strategy while acknowledging that for the foreseeable future it will have to continue maintaining its legacy systems, for example in its administration of tax credits.[65] HMRC believes its strategy will ensure that it has more resilient and agile technology and database platforms to support its administration of the tax system and enable it to better support society

58 C&AG's Report, para 2.40
59 Q 73
60 Q 73
61 C&AG Report, para 2.19 & 2.20
62 Q 73
63 Q 75; C&AG's Report, para 2.33
64 Q 74; The government's 10-year strategy to build a modern tax administration system available at: www.gov.uk/government/publications/tax-administration-strategy
65 Qq 74, 82, 85

at times of crisis, such as the COVID-19 pandemic.[66] Since we took evidence, HMRC secured £268 million in the November 2020 Spending Review to bring its technology up to date.[67]

HMRC's financial estimates

24. HMRC handles large sums of money, both collecting and paying out.[68] It relies on financial estimates in various different contexts to help achieve its objectives. Yet we have recently seen several examples where there have been mistakes in those estimates. We asked the Department about the circumstances of its breach by £726 million, in 2019–20, of its net cash requirement total, an important parliamentary control over public spending. The Comptroller and Auditor General had to qualify his opinion on HMRC's accounts because of this breach. HMRC recognised the seriousness of its breach. It explained that it had made an error in calculating its cash requirement which meant that it used more cash than it had predicted. The Department noted that it had not exceeded its budget and that in its view "there was no real-world impact from this error". As a result of the breach, HMRC commissioned a review by its internal audit function to understand what had gone wrong and identify improvements to its processes for estimating its cash requirements.[69] In a separate example, HMRC, as explained in its own Annual Report and Accounts, also had to correct its estimates of Corporation Tax revenues by some £6.6 billion in 2019–20, as a result of errors it made in its estimates in previous years.[70]

25. HMRC's latest estimate of the level of error and fraud in tax credits indicates that overpayments by HMRC decreased from 5.5% (£1.41 billion) of expenditure on tax credits in 2017–18 to 4.9% (£1.11 billion) in 2018–19. The estimated 2018–19 overpayment rate of 4.9% is lower than HMRC's forecast of 6.2%.[71] HMRC told us that fraud and error will continue to be a feature of tax credits and that getting the fraud and error level significantly below 5%, its ministerial target, will be "extremely challenging".[72] We asked the Department whether it is able to provide us with more rigorous estimates of the level of fraud and error in tax reliefs, particularly the Research & Development (R&D) tax relief, which cost £8.8 billion in 2019–20. HMRC told us that for some reliefs, such as the R&D relief, it is able to quantify the level of non-compliance because taxpayers have to claim the relief. In contrast, for tax reliefs that are not claimed but simply granted to those eligible, HMRC needs to make estimates based on indirect data. HMRC estimates the level of fraud and error associated with the R&D tax reliefs to be 3.6% (£311 million in 2019–20) of the tax relief expenditure. However, as highlighted by the Comptroller and Auditor General, HMRC's current estimate of error and fraud in R&D reliefs is based upon a series of judgements about how likely it is that cases of detected error and fraud are likely to occur within the larger population of unreviewed cases. HMRC does not yet have

66 Qq 75–76

67 HM Treasury, *Spending Review* 2020, CP 330, November 2020.

68 Q 51

69 Qq 15–17; HM Revenue & Customs Annual Report and Accounts 2019–20, The Resource Accounts: Certificate and Report of the Comptroller and Auditor General to the House of Commons, HC 891, 5 November 2020

70 HM Revenue & Customs Annual Report and Accounts 2019–20, Trust Statement, note 6.3

71 C&AG's Report, para 16 & 17

72 Qq 83, 85

a sufficiently developed understanding of the error and fraud risks arising from the R&D schemes.[73] Next year, HMRC plans to publish a list of all reliefs, with significant detail on each one, including the objectives of those reliefs that are aimed at changing behaviours.[74]

26. Regarding the COVID-19 support schemes, we asked HMRC whether it had estimated the level of fraud and error in the Eat Out to Help Out scheme considering the scheme had ended at the end of August. HMRC confirmed to us that it did not yet have an estimate of the level of fraud and error.[75] It explained to us that, while it had made three arrests so far for fraud, its compliance work had been affected by the fact that restaurants had to go back into a lockdown. It has identified high-risk cases, for investigation, where the amounts of the received claims have not been in proportion to the information the Department holds on the businesses.[76] In the case of the CJRS measure, HMRC has made a planning assumption for its compliance work that there could be 5% to 10% of fraud and error. It has yet to determine the actual level of fraud and error.[77]

73 Qq 97, 99; HM Revenue & Customs Annual Report and Accounts 2019–20, The Resource Accounts: Certificate and Report of the Comptroller and Auditor General to the House of Commons, HC 891, 5 November 2020

74 Qq 92–93

75 Qq 31, 33

76 Qq 28, 34

77 Q 43; C&AG's Report, *Implementing employment support schemes in response to the COVID-19 pandemic*, Session 2019–2021, HC 862, 23 October 2020, paragraph 19

Formal minutes

Thursday 14 January 2021

Virtual meeting

Members present:

Meg Hillier, in the Chair

Shaun Bailey
Sir Geoffrey Clifton-Brown
Barry Gardiner
Peter Grant
James Wild

Draft Report (*HMRC performance 2019–20*), proposed by the Chair, brought up and read.

Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 26 read and agreed to.

Summary agreed to.

Introduction agreed to.

Conclusions and recommendations agreed to.

Resolved, That the Report be the Thirty-Sixth of the Committee to the House.

Ordered, That the Chair make the Report to the House.
Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

[Adjourned till Monday 18 January at 1:45pm

Witnesses

The following witnesses gave evidence. Transcripts can be viewed on the inquiry publications page of the Committee's website.

Monday 16 November 2020

Jim Harra, First Permanent Secretary and Chief Executive, HM Revenue & Customs, **Justin Holliday**, Chief Finance Officer, HMRC and **Angela MacDonald**, Director General, Customer Services, HMRC Q1–108

Published written evidence

The following written evidence was received and can be viewed on the inquiry publications page of the Committee's website.

HMR numbers are generated by the evidence processing system and so may not be complete.

1 Hodgson, Mr David (Retired) (HMR0001)

List of Reports from the Committee during the current Parliament

All publications from the Committee are available on the publications page of the Committee's website.

Session 2019–21

Number	Title	Reference
1st	Support for children with special educational needs and disabilities	HC 85
2nd	Defence Nuclear Infrastructure	HC 86
3rd	High Speed 2: Spring 2020 Update	HC 84
4th	EU Exit: Get ready for Brexit Campaign	HC 131
5th	University technical colleges	HC 87
6th	Excess votes 2018–19	HC 243
7th	Gambling regulation: problem gambling and protecting vulnerable people	HC 134
8th	NHS capital expenditure and financial management	HC 344
9th	Water supply and demand management	HC 378
10th	Defence capability and the Equipment Plan	HC 247
11th	Local authority investment in commercial property	HC 312
12th	Management of tax reliefs	HC 379
13th	Whole of Government Response to COVID-19	HC 404
14th	Readying the NHS and social care for the COVID-19 peak	HC 405
15th	Improving the prison estate	HC 244
16th	Progress in remediating dangerous cladding	HC 406
17th	Immigration enforcement	HC 407
18th	NHS nursing workforce	HC 408
19th	Restoration and renewal of the Palace of Westminster	HC 549
20th	Tackling the tax gap	HC 650
21st	Government support for UK exporters	HC 679
22nd	Digital transformation in the NHS	HC 680
23rd	Delivering carrier strike	HC 684
24th	Selecting towns for the Towns Fund	HC 651
25th	Asylum accommodation and support transformation programme	HC 683
26th	Department of Work and Pensions Accounts 2019–20	HC 681
27th	Covid-19: Supply of ventilators	HC 685
28th	The Nuclear Decommissioning Authority's management of the Magnox contract	HC 653

Number	Title	Reference
29th	Whitehall preparations for EU Exit	HC 682
30th	The production and distribution of cash	HC 654
31st	Starter Homes	HC 88
32nd	Specialist Skills in the civil service	HC 686
33rd	Covid-19: Bounce Back Loan Scheme	HC 687
34th	Covid-19: Support for jobs	HC 920
35th	Improving Broadband	HC 688