Eightieth report of Session 2022-23

HM Revenue & Customs

Making Tax Digital

Introduction from the Committee

His Majesty's Revenue & Customs (HMRC) is responsible for administering the UK's tax system. In 2015 the government announced its ambition to make tax digital by 2020 and in 2015–16 HMRC launched its flagship transformation programme Making Tax Digital. The objectives of the programme are to maximise tax revenue, make sustainable cost savings and improve customer service by modernising the tax system for three taxes, VAT, Income Tax Self Assessment (Self Assessment) and Corporation Tax. The programme aims to move HMRC's existing tax system and records to a new modern tax management platform. HMRC will require taxpayers to keep and submit digital tax records quarterly through third party software. HMRC expects that the programme will reduce the amount of tax revenue lost to errors and carelessness (currently estimated at £9 billion) and help taxpayers understand their tax affairs better.

HMRC introduced digital tax record keeping for larger VAT businesses as initially planned in 2019, and for smaller VAT businesses three years later than planned in 2022. The Self Assessment part of the programme was originally due to be introduced in 2018 but by December 2022 the timetable had been delayed on four occasions. In December the government announced that the introduction of Making Tax Digital for Self Assessment would be delayed again, and the number of taxpayers affected would be reduced. Those businesses and landlords with Self Assessment incomes above £50,000 will be required to use the new system first in 2026, then those with incomes between £30,000 and £50,000 in 2027. The programme for those with incomes between £10,000 to £30,000 has been put on hold until further notice. HMRC has not announced when it will introduce digital record keeping for general partnerships or Making Tax Digital for Corporation Tax. The programme has so far cost £642 million. HMRC expects introducing Making Tax Digital for VAT and Self Assessment will now cost a total of £1.3 billion, a 400% increase in real terms compared to its original estimate of £222 million in 2016 for all three taxes in the programme.

Based on a report by the National Audit Office, the Committee took evidence on 19 June 2023 from HM Revenue & Customs. The Committee published its report on 24 November 2023. This is the government's response to the Committee's report.

Relevant reports

- NAO report: Progress with Making Tax Digital – Session 2022-23 (HC 1319)
- PAC report: Progress with Making Tax Digital – Session 2022-23 (HC 1333)

Government response to the Committee

> *1. PAC conclusion: Widespread and repeated failures in HMRC's planning, design and delivery of Making Tax Digital have led to increased costs and several delays to the Making Tax Digital programme.*

> *1a. PAC recommendation: HMRC should urgently test that its existing plans are sufficiently detailed and rigorous to ensure the successful delivery of the remainder of the programme, and report to the Committee on its findings for Making Tax Digital for Self Assessment as part of its Treasury Minute.*

1.1   The government agrees with the Committee's recommendation.

Recommendation implemented

1.2   His Majesty's Revenue & Customs (HMRC) has developed a detailed plan to enable the delivery of Making Tax Digital for Income Tax Self-Assessment (MTD for ITSA).

1.3   In 2023, HMRC took steps to strengthen and further assure its plans. All aspects of MTD's design, alongside work to build the required IT changes, is now subject to a consistent methodology to assess the cost and work required to implement each change. This provides assurance that the overall plan is deliverable, enabling HMRC to effectively monitor progress against it.

1.4   HMRC has used this methodology to design a set of products for stakeholders. These include:

- a high-level delivery roadmap;
- customer journeys covering the beta testing period in 2024-2026 and the period after the new mandated requirements are introduced in April 2026;
- a revised Application Programming Interface (API) roadmap for software developers; and
- updated eligibility criteria for the private beta testing phase through to April 2025.

1.5   HMRC made these products available to key external stakeholders in November 2023.

1.6   MTD is also part of the Government Major Projects Portfolio (GMPP) and is subject to regular assurance reviews by the Infrastructure and Project Authority (IPA). The most recent was in March 2023, when the IPA assessed delivery confidence for MTD as "amber" (increased from the previous "red" rating) and noted substantial progress since their last review in August 2022. A further review is expected in February 2024.

1.7   The government recognises that delivery of the MTD for ITSA programme remains challenging but considers that HMRC's plans demonstrate a realistic timetable.

> *1b. PAC recommendation: HMRC should, as part of its Treasury Minute response, specify in detail how it will hold senior leaders accountable for delivering against the programme's timetable and budget, and what consequence there will be for any further timetable and budget overruns.*

1.8.   The government agrees with the Committee's recommendation.

Recommendation implemented

1.9   As a part of the GMPP, MTD is subject to robust governance processes with clear accountabilities for all aspects of delivery.

1.10   In line with GMPP governance, people in key roles, such as MTD's Senior Responsible Owner (SRO), sign letters setting out their responsibilities and accountabilities for delivery of the programme and its intended outcomes. These letters are updated as people change roles.

1.11   MTD's SRO also completes a quarterly report to the IPA, covering the programme's activity.

1.12   The delivery of MTD is reflected in the performance objectives of the Programme Director, SRO and other senior HMRC officials. Performance against these objectives is appraised through the formalised Senior Civil Servant (SCS) performance management process, which include manager assessments at mid-year and end-of-year points to track progress against performance objectives.

1.13   There are also significant internal governance and scrutiny processes in place, including internal audit processes and an Executive Oversight Group, enabling HMRC's Executive Committee to scrutinise all aspects of the programme's delivery. The Programme also reports to HMRC's Transformation Board including Executive Committee members and HMRC Non-Executive Directors.

1.14   MTD's business case is updated regularly and scrutinised through Treasury Approval Point hearings, ahead of the Chief Secretary to the Treasury's sign-off.

1.15   The business case includes HMRC's analysis of costs and benefits of the programme, alongside planned expenditure. The programme has continuously delivered within its annual allocated budgets and financial forecasts, in accordance with conditions set at Treasury Approval Points.

> **2. PAC conclusion: It is unacceptable that seven years in, with £640 million of taxpayer's money spent on the programme as a whole, so many questions remain about how Making Tax Digital for Self-Assessment will work.**

> **2a. PAC recommendation: HMRC should, in partnership with its programme stakeholders including customers, tax agents and software providers, resolve design issues and write to the Committee by April 2024 to explain how each of the significant outstanding design issues have been resolved. As part of this, HMRC should consider what steps it can take to simplify arrangements for Self Assessment taxpayers.**

2.1   The government agrees with the Committee's recommendation.

Recommendation implemented

2.2   The government has provided its full response in the following paragraphs, together with the announced changes to the design of MTD for ITSA made at the 2023 Autumn Statement.

2.3   This announcement addressed the most significant outstanding design issues. It resulted from consultation and collaboration with external stakeholders, undertaken as part of a review into MTD and the needs of smaller business in 2023. In particular, the announcement included:

- a revised customer journey for landlords with jointly-held property;
- amendments to the design of quarterly updates;
- confirmation that the requirement to complete an End of Period Statement within MTD will be removed; and
- a commitment to develop a solution allowing multiple agents to act for customers, by April 2026.

2.4   HMRC also updated its eligibility criteria to support MTD's beta testing phase, clarifying who can participate.

2.5   HMRC will continue work with external stakeholders on other more detailed policy design elements ahead of mandation in 2026, alongside continuing a private beta testing programme in 2024-25 and a public beta in 2025-26 to ensure that service design meets users' needs.

> **2b. PAC recommendation: HMRC should, by Summer 2024, undertake and publish a robust assessment of how much difference to tax revenue is made by (i) more frequent submissions of Self Assessment data and (ii) by digital submissions.**

2.6   The government disagrees with the Committee's recommendation.

2.7   MTD software is designed to ensure records are kept accurately and in a timely manner. It is not possible to estimate robustly the effects of the separate components in isolation, since quarterly digital updates help to ensure software is used timeously. While initial assumptions were made, these have been overtaken by evidence from MTD for VAT which does not allow for disaggregation of the source of the additional tax revenue.

2.8   A 2022 evaluation estimated additional tax revenue from MTD for VAT in 2019-20 of at least £185 million, providing strong evidence that MTD reduces the tax gap. This provides confidence that the approach will also yield benefits in ITSA.

2.9   HMRC has now applied the MTD for VAT evaluation findings to MTD for ITSA and expects a reduction of around 15% in the tax gap from error and failure to take reasonable care. This methodology has been approved by the independent Office for Budget Responsibility (OBR).

2.10   Based on the Autumn Statement 2023 forecast, OBR-certified MTD for ITSA benefits (including digital prompts) are:

- £25 million in 2025-26;
- £120 million in 2026-27;
- £465 million in 2027-28;
- £780 million in 2028-29.

2.11   These estimates assume quarterly updates and software together encourage higher-quality and timely record keeping. HMRC will evaluate benefits of MTD for ITSA as new evidence is available.

2.12   Research with customers shows around one-third currently wait to the year end to update records, indicating that MTD would increase the frequency of record keeping. Evidence of behaviour and estimates will improve as MTD for ITSA is implemented.

> **3. PAC conclusion: HMRC's design of Making Tax Digital has not taken sufficient account of the realities facing business taxpayers and agents.**

> **3a. PAC recommendation: In addition to Making Tax Digital, HMRC should research what services customers would find most helpful, drawing on customer views as well as international research, and publish its findings by Autumn 2024.**

3.1   The government disagrees with the Committee's recommendation.

3.2   The government disagrees with the Committee's recommendation to produce a standalone publication by Autumn 2024. However, the government agrees with the need for research and customer insight to inform the development of a modern digital tax administration system. As part of the government's 10-year strategy to build a trusted, modern tax administration system, HMRC has undertaken a range of external consultations and research activities to understand the needs and views of its customers.

3.3   Some of these explore how ITSA could be more straightforward and easier for customers to understand, including:

- a Call for Evidence on reforming ITSA registration for individuals with income from self-employment or property, with the Summary of Responses published in July 2022;
- a Discussion Document on Simplifying and Modernising Income Tax Services, published in March 2023, as part of the Tax Administration Framework Review;

- external research on the views and experiences of individuals who have recently become required to register for ITSA, published in June 2023; and
- analysis, to support the MTD small business review, looking at the experience of self-employed customers and landlords with income below £30,000. This will be published in 2024.

3.4   HMRC has recently launched a full review of the circumstances in which a taxpayer should submit a self-assessment tax return; improved its online tools; and added to or improved customer guidance.

3.5   HMRC shares its research and approach to customer understanding with international tax authorities and will continue to evaluate how international research can inform its approach.

> ***3b. PAC recommendation: HMRC should ensure that all its future proposals for digitalising the tax system: start with what taxpayers need; are demonstrably better for them than existing arrangements; and the plans are supported and therefore can be championed by taxpayer representatives, including its own Administrative Burdens Advisory Board.***

3.6   The government disagrees with the Committee's recommendation.

3.7   A priority for government is to make it easy for taxpayers to get tax right. However, it needs to balance several objectives for the tax system, including raising revenue and tackling the tax gap. While these often align, there can be trade-offs to consider.

3.8   HMRC regularly engages a range of taxpayer representatives, including the Administrative Burdens Advisory Board (ABAB), as new services are developed and to better understand issues faced by taxpayers. ABAB provides valuable insight, including on MTD for ITSA, where its views were important in informing the announcements made in the 2023 Autumn Statement.

3.9   HMRC has also established an expert panel to consult on digital improvement ideas which provides insight into how to implement changes and provide the right support for vulnerable or digitally excluded customers.

3.10   As part of HMRC's governance, the Customer Experience Committee, which includes independent expert advisers, provides advice on customer-experience issues. HMRC shares plans for digital improvements with this committee.

3.11   The government has recently enhanced existing processes which support policy and service delivery, ensuring these consider improving taxpayers' experience. This includes improving training and internal guidance for policy officials; introducing checkpoints in the policy making process where senior officials review measures from a simplification and customer experience perspective; and ensuring advice to ministers sets out how a measure contributes to making the tax system simpler, fairer or supports growth.

3.12   HMRC also runs research programmes to build understanding of customer needs, publishing analyses of impacts on individuals and businesses in Tax Information and Impact Notes (TIINs).

> ***4. PAC conclusion: In seeking further investment in the programme, HMRC has not been open enough about the substantial costs that Making Tax Digital will impose on many taxpayers.***

> **4. PAC recommendation: Before finalising its proposals to extend Making Tax Digital to lower income taxpayers, HMRC should:**
>
> - **fully reassess the costs for customers to comply with Making Tax Digital for Self Assessment, taking account for inflation and any significant design changes made when finalising its plans; and**
> - **Use this to prepare a robust updated business case for Making Tax Digital for Self Assessment.**

4.1   The government agrees with the Committee's recommendation.

Target implementation date: Spring 2025

4.2   At the 2023 Autumn Statement, the government announced changes to simplify and improve the design of MTD for ITSA. These changes followed extensive collaboration with accountancy, business and landlord representative bodies, and software developers; and they were informed by research with landlords and self-employed customers.

4.3   HMRC has reassessed costs to customers as a result of these changes as well as the government's decision to retain the income threshold for mandating customers into MTD for ITSA at £30,000. This has been developed with the input of stakeholders in business and the accountancy professions as well as the Administrative Burdens Advisory Board.

4.4   HMRC has also conducted a comprehensive review of the evidence feeding into estimates, bringing in the latest internal and external data available. These estimates will be published in a Tax Information and Impact Note alongside amendment regulations in the fourth quarter of 2023-24. The current MTD business case has spend approval until 31 March 2025, and the next iteration will provide a full update on costs (HMRC and customer) and the benefits of the programme in line with approvals timelines.

4.5   HMRC continues to ensure that these estimates are kept under review, updated as necessary and included within ministerial advice. HMRC will also ensure that all estimates on customer costs are included in the net present value (NPV) calculation within business cases, and separate narrative and annexes, in line with National Audit Office (NAO) recommendations.

> **5. PAC conclusion: HMRC's poor track record of repeated delays to the Making Tax Digital programme and its lack of conviction in its latest timetable gives us little confidence that it will deliver the rest of the programme on time.**

> **5a. PAC recommendation: HMRC should, as part of its Treasury Minute response, explain how it will assure itself that the timetable and budget for Making Tax Digital for Self-Assessment is realistic and how it will use independent technical assurance and other sources of evidence to provide this assurance.**

5.1   The government agrees with the Committee's recommendation.

Recommendation implemented

5.2   HMRC has undertaken detailed work to assure its delivery plan for MTD. HMRC is confident its budget for the next two years reflects the resourcing and funding requirements needed to achieve the deliverables within this plan.

5.3   A programme of MTD's scale and complexity carries inherent risk. Its delivery roadmap to mandation presents an ambitious but realistic timetable. Successful delivery remains contingent on external software developers building MTD products, and engagement from the

agent community to support customer readiness; it also assumes stability in HMRC's resource and internal capacity to deliver MTD.

5.4   HMRC will continue to monitor progress against its plans and key performance indicators – alongside its approach to risk management – through internal governance and independent technical and other assurance. This includes work to develop contingency plans to respond swiftly to any potential delays, minimising impacts on customers and stakeholders.

5.5   MTD was reviewed independently by the IPA in March 2023 and will be reviewed again in February 2024. MTD's delivery and budget receives additional scrutiny through HM Treasury checkpoints, HMRC's internal audit function, internal governance and investment boards.

5.6   For further technical assurance of moving taxpayer records, HMRC has commissioned a data quality assessment of the Self-Assessment data held on legacy systems. This assessment is being undertaken by a number of suppliers including a specialist data company.

> **5b. PAC recommendation: If further changes to the delivery timetable are necessary, HMRC should communicate this clearly, early and definitively, to provide certainty to its delivery partners and customers.**

5.7   The government agrees with the Committee's recommendation.

Target implementation date: April 2026

5.8   Making Tax Digital is central to the delivery of a digital and modernised tax administration system. The government recognises that HMRC's customers and delivery partners need certainty and assurance over the delivery plan for MTD.

5.9   The government announced the phased mandation timeframe of MTD for ITSA in December 2022. This announcement recognised the significance of these changes to HMRC, taxpayers and delivery partners - alongside the challenging economic environment facing small businesses. It was also informed by HMRC's detailed internal planning.

5.10   Following the announcement of the outcome of the small business review in November 2023, HMRC has also shared detailed plans and a delivery roadmap with key external partners involved in the delivery of MTD.

5.11   HMRC has also sought feedback on its communications plans from agent representative bodies, software developers and tax agents and will continue to do so alongside sharing key messages and assets where available. Short-term plans are focussed on supporting software developers, agents, self-employed people, and landlords to take part in beta testing.

5.12   As April 2026 approaches, additional messaging will be introduced to encourage those outside of testing to prepare for the new requirements.

5.13   The government will ensure that any future decisions that affect customers or delivery partners – such as any future decision to amend the income threshold for mandation into MTD – provides adequate time for all parties to prepare.

> **6. PAC conclusion: We are concerned that the repeated delays and poor design of the Self-Assessment phase of the programme is deterring software providers from developing quality progress with Making Tax Digital products and will ultimately put customers at risk.**

> **6a. PAC recommendation: HMRC should, within three months, write to the Committee and set out how it will ensure that it strikes the right balance between ensuring competition, quality and access to software for its Making Tax Digital VAT and Self Assessment customers.**

6.1   The government agrees with the Committee's recommendation.

Recommendation implemented

6.2   The government has provided its full response in the following paragraphs, together with HMRC's end-to-end service guides for both MTD for ITSA and VAT.

6.3   These guides set out in detail how developers should produce software for MTD, including:

- how to integrate software with HMRC's systems;
- how software aligns with various end-to-end users; and
- HMRC's criteria for allowing an MTD product to be listed on its software choices page.

6.4   These guides are continuously reviewed, with the most recent revision in December 2023.

6.5   HMRC manages the quality of software through its production approvals process which is outlined in these guides. This includes a section on "Minimum Functionality Standards" which sets out the minimum required functionality expected of MTD products. HMRC is currently reviewing these standards, with the aim of ensuring they support innovation in the software market and incentivise the development of the best possible software products.

6.6   HMRC works closely with stakeholders to balance the burden on software developers entering the market, the benefits of innovation, and the quality of the MTD customer journeys.

6.7   For example, HMRC has adapted its approach in response to feedback, enabling software developers to build MTD products iteratively and to be granted production approval for specific elements of the required functionality. From a taxpayer perspective, however, an MTD for ITSA product will only be listed on the HMRC Software Choices webpage once it satisfies all the requirements listed under the 'Minimum Functionality Standards'.

> **6b. PAC recommendation: HMRC should, within three months, write to the Committee explaining what assurance customers can take from its accreditation of software and how it will protect taxpayers if the software (rather than the taxpayer) makes mistakes in tax submissions or does not safeguard taxpayer data sufficiently.**

6.8   The government agrees with the Committee's recommendation.

Recommendation implemented

6.9   The government has provided a full response to the Committee in the following paragraphs.

6.10   Following the Committee's June 2023 hearing, HMRC corrected oral evidence in a letter dated 29 June 2023, including confirmation that it does not accredit software.

6.11   Instead, HMRC operates a recognition or "production approvals process" to assure users that software meets its requirements. Approval depends on software meeting API specifications and undergoing testing.

6.12   Developers are also required to accept HMRC's software terms of use, covering data security requirements, encryption policies, and data-access controls.

6.13   Before introducing MTD for ITSA, HMRC will list approved software which meets minimum functionality standards on a Software Choices webpage, helping customers to choose the most suitable product for them.

6.14   HMRC has a proven software integration model, which ensures commercial products meet with HMRC's technical specifications and can integrate seamlessly with its systems. MTD for VAT has an ecosystem of over 500 commercially available products, catering to diverse customer needs and budgets.

6.15   Calculation of tax liabilities and the application of penalties remain a function of HMRC, using its own systems. However, HMRC has robust processes to protect taxpayers if, for example, they believe a software error has resulted in a penalty. This includes review and appeals processes.

6.16   HMRC would also investigate any such cases, ensuring any detrimental customer impacts are addressed. Should a major problem affect MTD software, HMRC can ultimately remove the ability of that product to upload updates to HMRC's systems, safeguarding customers and developers until problems are resolved.