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The COVID-19 pandemic has added to HMRC's workload, at a time when it already faced extreme challenges dealing with the impact of the UK's exit from the EU and the strain of modernising the tax system. HMRC performed well in setting up and operating the COVID-19 support schemes in response to the pandemic. But responding to COVID-19 and the other pressures HMRC faced, along with a workforce which is much smaller than when the department was established in 2005, has led to poor performance, delays and backlogs in key aspects of tax administration. In 2020–21 customer service declined, as did compliance activity, with compliance yield falling by almost a fifth to £30 billion. Total tax revenue in 2020–21 was also 4% lower at £609 billion, reflecting the impact of COVID-19 on the economy. The pandemic contributed to HMRC delaying an extension of Making Tax Digital, which is a key part of its long-term transformation plans. HMRC claims that the Making Tax Digital initiative is intended to make tax easier for individual and business taxpayers but it is not clear that is how it is turning out in practice. COVID-19 has also led to changed working patterns, leaving HMRC with much more new office space than it needs.

HMRC is keen to return to business as usual as quickly as possible but this is not the reality it faces. In autumn 2021, aspects of customer service remained poor and HMRC told us it was only just starting to examine compliance cases it had deferred in 2020–21. We are therefore extremely concerned about its capacity to clear backlogs while tackling the avalanche of error and fraud it now faces on the COVID-19 schemes, Personal Tax Credits and research & development tax reliefs, delivering its long-term transformation ambitions and responding adequately to tax avoidance schemes. Error and fraud in COVID-19 support payments cost HMRC around £6 billion in 2020–21. Taxpayers view the loss of this money differently to the theoretical losses which HMRC assesses arise from the tax gap. HMRC is not doing enough to get back the money lost through error and fraud in COVID-19 support payments. Even if successful, its current plan would see it fail to recover £4 billion of COVID-19 support payments made incorrectly in 2020–21. Such inaction risks rewarding the unscrupulous and sending a message that HMRC is soft on fraud.

Introduction

HMRC is responsible for administering the UK's tax system. For 2020–21, HMRC was responsible for: collecting revenue and managing compliance; improving customer experience; delivering coronavirus (COVID-19) support schemes; supporting the UK's international trade; transforming how it works; and supporting wider government aims. In 2020–21, HMRC raised £608.8 billion of tax revenues, a reduction of £27.9 billion (4.4%) compared to 2019–20. HMRC estimates the yield from its tax compliance activities in 2020–21 was £30.4 billion, 18% below the yield in 2019–20 (£36.9 billion). As well as its traditional responsibilities for tax collection and administering Personal Tax Credits, HMRC played a major role in implementing the government's response to the COVID-19 pandemic. In particular, it administered the Coronavirus Job Retention Scheme (CJRS) providing £61 billion in 2020–21 to help firms continue to keep people in employment. And, through the Self-Employment Income Support Scheme (SEISS), it paid £20 billion of grants in 2020–21 to self-employed individuals whose businesses had been 'adversely affected' by the pandemic. HMRC was also responsible for key customs and border-related programmes and preparing for the end of the transition period on 31 December 2020.

Conclusions and recommendations

1. **HMRC's unambitious plans for recovering overpayments of COVID-19 support could lead to government writing off at least £4 billion.** HMRC currently estimates that error and fraud across its main COVID-19 grant schemes totalled nearly £6 billion in 2020–21. HMRC is focusing on egregious abuse and it is currently planning that most recovery action will stop at the end of 2022–23. It only expects to recover around £2 billion of the £6 billion it currently estimates has been lost to error and fraud in 2020–21. Losses are likely to be even greater as it has not yet published estimates of error and fraud in 2021–22. HMRC will have a better understanding in 2022 of the level of error and fraud once it has investigated a sample of furlough payments and examined 2020–21 self-assessment tax returns. HMRC's approach to recovering fraudulent payments sends the wrong signals and risks encouraging abuse of tax and grant systems in the future.

   Recommendation: ***HMRC needs to take a number of actions to reassure parliament and the public that it is serious about tackling error and fraud from the COVID-19 support schemes and is taking all recovery action where it is cost effective to do so. Alongside its Treasury Minute response to this report, HMRC should write to the Committee setting out:***

   - ***the analysis it has undertaken, including the costs and benefits, in determining the amount it plans to spend on recovering error and fraud;***
   - ***whether its plans mean that it will have pursued all error and fraud where money recovered should exceed the cost which HMRC would incur in doing so;***
   - ***where further action would be cost-effective, commit to recovering more of the support payments lost through error and fraud and set out how this will be done;***
   - ***commit to reassessing whether its plans are sufficiently ambitious, once it has improved its estimates of error and fraud in 2022.***

2. **HMRC does not understand the reasons for the growth in the cost of research and development tax reliefs including how much is due to abuse.** The cost of research and development (R&D) tax reliefs has grown by 240% over the last four years, with claims exceeding forecasts. Over this period R&D expenditure used to claim reliefs has grown at a much faster rate than UK R&D expenditure reported by the Office for National Statistics. HMRC does not know why the cost of R&D tax reliefs has grown so much. Research and development reliefs are complex and open up opportunities for abuse. HMRC estimates error and fraud was £336 million in 2020–21, up £25 million from 2019–20. The C&AG considered the level of error and fraud estimated by HMRC to be material and qualified his regularity opinion in 2020–21 for the second year in a row. However, the actual level of error and fraud could be much bigger as HMRC's estimates involve a considerable amount of judgement. HMRC needs a better understanding of the nature of error and fraud in R&D tax reliefs. It is planning to examine a random sample of claims to improve its

estimates of error and fraud and has increased the compliance resources it uses to check R&D relief claims. The government is planning to make changes to the reliefs with the aim of improving how they are targeted and protected from abuse.

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

- ***how it will improve its understanding of the cost of research and development tax reliefs; and***
- ***the reduction in the level of error and fraud it is seeking together with how and when that will happen. This should include clear milestones for this Committee to monitor.***

3. **HMRC does not have a convincing plan for restoring compliance activity back to pre-pandemic levels.** In response to the pandemic, HMRC suspended some of its compliance work in 2020–21 where taxpayers could not cope with inquiries, and because it needed to redeploy staff. The number of compliance investigations which HMRC opened and closed in the year fell, which has led to a backlog of deferred cases. The Committee expects HMRC to fully investigate this backlog of cases and not leave them unchecked. HMRC told us that the action it took in 2020–21 would lead to a deferral rather than a loss of tax as tax legislation allows it to go back to earlier years where it finds non-compliance. HMRC expects compliance activity to get back to normal levels and timelines in 2022–23, but did not explain how this would be possible if it was clearing the backlog of cases at the same time. HMRC tracks compliance yield to measure the effectiveness of its compliance and enforcement activities. It considers yield will get back on "even keel" in 2022–23. It will need to identify and separate out the yield from deferred cases and new investigations if it is to fully understand and explain its performance.

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

- ***how and by when it will have eliminated the backlog of compliance cases; and***
- ***how it will report its performance on deferred cases and new cases, so fair comparisons can be made with its pre-pandemic performance levels.***

4. **Resource constraints are limiting HMRC's ability to get the optimum level of compliance yield.** Compliance yield represents the additional revenues that HMRC considers it has generated and the revenue losses it has prevented through its enforcement and compliance activities. HMRC spent around £1.5 billion on such activities in 2020–21 and generated a yield of £30.4 billion. HMRC's data indicate that it would increase this yield if it spent more on compliance, particularly if it increased its activities to ensure large business complied with their tax obligations. On average HMRC generates £17 of compliance yield for each £1 it spends, with returns from its large business activity at £60 to £1. HMRC told us that marginal rates of return from additional compliance resources would be lower than average rates. It also said it constantly adjusts the resource it applies to different areas of its business, based on both expected yield and risks that need to be managed. We understand from HMRC's evidence that the 2021 Spending Review gave it an

additional £180 million over three years for "spend to raise", of which £90 million is to come in 2024–25. The additional funding in 2024–25 is equivalent to 2% of HMRC's total running costs in 2020–21.

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

- ***its analysis, including the costs and benefits, in determining the overall size of its compliance programme; and***
- ***an assessment of the extent to which additional spending would lead to any further increase in tax revenue.***

5. **It is too easy for taxpayers to be unwittingly lured into tax avoidance schemes.** HMRC introduced the loan charge in 2019 to recoup tax from people who used 'disguised remuneration' schemes to avoid tax. The imposition of the loan charge on taxpayers who were unknowingly sold an unlawful scheme by unscrupulous tax agents has led to some being financially damaged. HMRC's strategy for tackling tax avoidance is two-pronged. It wants to reduce the supply of, and demand for, avoidance schemes. It said there are now 20 to 30 unscrupulous promoters of tax avoidance schemes, most of which relate to employment taxes. These promoters are mainly based outside the UK and have complex organisational structures which make them more difficult to investigate. However, HMRC considers it has sufficient powers to tackle promoters of avoidance schemes. On the demand side, HMRC is trying a new approach to identify and alert users of avoidance schemes and offer them help to get out. We welcome this change in approach, and HMRC should develop it by helping taxpayers not to enter into the schemes in the first place.

Recommendation: ***To reduce the risk of taxpayers getting involved in tax avoidance schemes, HMRC should, in its Treasury Minute response, set down how it will make it easier for taxpayers to identify illegal schemes and the unscrupulous tax agents who promote them.***

6. **Yet again customer service has collapsed and HMRC's recovery plans are not clear.** For over a decade this Committee has repeatedly reported on HMRC's inadequate levels of customer service. Following an examination by this Committee in 2016, HMRC's customer service improved, but since 2017–18 it has been declining. The decline in performance accelerated in 2020–21 as HMRC diverted resources to its COVID-19 response and UK's transition from the EU. HMRC told us that its call handling performance had improved in 2021–22, but there were still long delays in responding to correspondence. Since HMRC was established in 2005, its staffing levels have reduced by around 40%. HMRC told us that its customer service resources had been reducing over time and that it was resourced to give a "decent" rather than a "brilliant" service. HMRC's strategy for customer service is to discourage the type of calls that do not change people's tax outcomes or move such calls online. We are concerned whether this strategy is deliverable. As the Committee reported in 2016, HMRC tried a similar approach before, but it was overly optimistic about reductions in calls, with service levels collapsing when it cut staffing. HMRC is not publicly reporting call handling speeds for 2021–22 and has not a set a target for its correspondence response time measure. We will continue to scrutinise HMRC's response times until confident that HMRC is sustaining acceptable service levels.

Recommendation: ***HMRC should, in its Treasury Minute response, explain:***

- ***the service levels it is aiming to provide and by when, including for the time taken to answer calls and respond to post, and commit to publishing outturn against these measures;***
- ***how it has tested the realism of its customer service plans; and***
- ***its contingency plans if the numbers of taxpayers writing and calling exceed forecast levels.***

7. **The benefits of Making Tax Digital to those with simple tax affairs are not clear.** The requirement for taxpayers to keep tax records and submit quarterly returns to HMRC digitally is a key part of its 10-year modernisation strategy. From April 2024, HMRC will extend Making Tax Digital to 4.2 million taxpayers with business and/or property income over £10,000, including small landlords and sole traders, to meet their income tax obligations. HMRC considers Making Tax Digital is making tax easier, keeping tax in line with the digital age, making business more productive and will provide better data if it needs to introduce further support schemes like SEISS. However, it is far from clear how those taxpayers with the most straightforward tax affairs, such as a retired person with rental income, will benefit from completing quarterly digital self-assessment returns. There is also no guarantee that the software they will need to submit returns digitally on will be readily available or easy to use, although HMRC is confident this will be the case. We question the value of asking the large number of taxpayers with simple tax affairs to take on additional costs and reporting.

Recommendation: ***HMRC should, in its Treasury Minute response, explain how the introduction of Making Tax Digital will be made easier, and less costly, for taxpayers with the simplest and most straightforward tax affairs.***

8. **Changed working practices have left HMRC with more office space than it needs.** We have long standing concerns about the flexibility of HMRC's estates strategy which is seeing it move to 13 regional centres with long-term non-breakable property leases. The shift to hybrid working caused by the pandemic has reduced the office space HMRC needs. HMRC is already renting out some spare capacity to other government departments in its regional centres. HMRC relies on the Cabinet Office to identify suitable alternative users of its spare space and encourage them to use it. HMRC told us the system is working well and there is a queue of organisations wanting to use the spare capacity in its offices. We remain concerned that changes in the commercial property market could leave HMRC with unused spare space in the future.

Recommendation: ***HMRC should:***

- ***work with Cabinet Office to draw up a plan for how they intend to make sure that spare HMRC office space is not left vacant, and write to the Committee explaining the plan within 6 months of this report; and***
- ***each quarter, report the amount and cost of empty space in its estate.***

1 Managing error and fraud, compliance and tax avoidance

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 2020–21.[1]

2. HMRC is responsible for administering the UK's tax system, reporting total tax revenue of £608.8 billion in 2020–21, a reduction of £27.9 billion (4.4%) compared to 2019–20, reflecting the impact of coronavirus (COVID-19) on the economy. For 2020–21, HMRC was responsible for: collecting revenue and managing compliance; improving customer experience; delivering COVID-19 support schemes; supporting the UK's international trade; transforming it how works; and supporting wider government aims. While most tax revenue is paid to HMRC without the need for intervention, some is only received because of specific compliance and enforcement activities. Compliance yield measures the effectiveness of these activities. For 2020–21, HMRC did not set a target for compliance yield due to the uncertainty around the COVID-19 pandemic and the need to respond quickly to urgent government priorities. HMRC estimates the yield from its tax compliance activities in 2020–21 was £30.4 billion, compared to £36.9 billion in 2019–20. HMRC did not set targets either for its eight key customer service measures in 2020–21. HMRC's performance against five of these measures declined in 2020–21, improved for two and was unchanged for the other. As part of administering the tax system HMRC is responsible for managing tax reliefs, including Research & Development (R&D) reliefs.[2]

3. HMRC faced a number of strategic challenges, specifically: its implementation of elements of the government's response to the COVID-19 pandemic including important measures to support employment and businesses; managing the impact of COVID-19 on its operations; managing UK transition and the ending of staged customs controls; and delivering its plans to build a trusted and modern tax administration system.[3] It needed to meet these challenges with a workforce which is much smaller than when it was established. Both TaxWatch and Unchecked UK submitted evidence to us which highlighted reductions in HMRC's workforce. In 2003–04 Inland Revenue and HM Customs and Excise had in total the equivalent of around 100,000 full time staff.[4] In 2020–21, HMRC's headcount had reduced to around 58,000 in the core department and around 4,000 more in its arm's length bodies.[5]

Error and fraud in the COVID-19 support schemes

4. As part of the government's response to the COVID-19 pandemic, HMRC administered three major grant schemes in 2020–21.

1 Report by the Comptroller and Auditor General, *HM Revenue & Customs Annual Report and Accounts 2020–21*, 4 November 2021

2 C&AG's Report, para 1, 4, 7–8, 18, 1.25, 1.28–1.29, 4.28, and Figure 8

3 C&AG's Report, para 2.1

4 Inland Revenue and HM Customs and Excise merged in 2005 to become HM Revenue & Customs

5 Written Evidence HMP0004-Tax Watch, para 53; Written Evidence HMP0003- Unchecked UK, para 17; HM Revenue & Customs Annual Report and Accounts 2020–21, page 164

- The Coronavirus Job Retention Scheme (CJRS), which paid grants to employers of up to £2,500 a month per employee to help continue to keep people in employment. CJRS cost £61 billion in 2020–21.[6]
- The Self-Employment Income Support Scheme (SEISS), which paid grants to self-employed people and members of partnerships. SEISS cost £20 billion in 2020–21.[7]
- Eat Out to Help Out – to encourage people to return to eating out, HMRC funded a discount of 50% (capped at £10 per diner) on food and non-alcoholic drinks every Monday, Tuesday and Wednesday in August 2020. Eat Out to Help Out cost £840 million.[8]

5. HMRC's most likely estimate of total error and fraud on payments made through these three schemes in 2020–21 was £5.8 billion. This comprised £5.3 billion for CJRS (equivalent to 8.7% of spending), £0.5 billion for SEISS (2.5%) and less than £0.1 billion for Eat Out to Help Out (8.5%).[9] In March 2021 the government announced that it would establish a Taxpayer Protection Taskforce of 1,265 HMRC staff to tackle fraud within the COVID-19 support schemes, at a cost of more than £100 million.[10] The Financial Times reported in November 2021 that HMRC's accounting officer had told it that HMRC was currently planning to finish its recovery action at the end of 2022–23.[11] HMRC subsequently told us that it expects to settle some of the more complex cases after 2022–23.[12]

6. We asked HMRC what it expected the levels of error and fraud to be on the later SEISS grants, as these had tighter eligibility conditions. HMRC explained that it had kept broadly the same assumptions about levels of error and fraud. It said it would need firm evidence to the contrary before changing its estimates. However, it said there was early evidence that as both CJRS and SEISS "went on" error and fraud did reduce, partly because HMRC had better intelligence. It also said that it was too early to know how tightening eligibility rules for SEISS had altered people's behaviour and thus the level of error and fraud.[13]

7. HMRC is planning to improve its estimates of error and fraud in 2022 for the two main support schemes. By early 2022, it plans to have examined a random sample of CJRS claims to assess error and fraud. For SEISS, HMRC expects to be able to refine its estimates using the full year of 2020–21 self-assessment tax return data which becomes available in early 2022. HMRC is not expecting to obtain significant new data or information on error and fraud for Eat Out to Help Out.[14]

8. We questioned HMRC about its plans to recover the almost £6 billion lost through errors and fraudulent payments made in 2020–21. It told us it had already recovered £850 million.[15] It said it also expected to recover a further £1 billon through the Taxpayer

6 C&AG's report, para 2.4–2.5
7 C&AG's report, para 2.6–2.7
8 C&AG's report, para 2.11
9 C&AG's report, Figure 16
10 C&AG's report, para 3.23
11 Financial Times, HMRC expects to recover less than half £5.8bn lost in Covid fraud and errors, November 2021
12 Note from the HM Revenue & Customs, received 22 December 2021.
13 Qq 80, 85
14 C&AG's report, para 3.27–3.28
15 Qq 69–70, 76–77

Protection Taskforce which was announced in Budget 2021.[16] We asked what it would do to get the remaining £4 billion back. HMRC told us it would try to recover it all, but £1 billon was its estimate of what it considers it will succeed in getting back. HMRC outlined the challenges it faced in recovering some of this money. It told us, for example, that for some aspects of the furlough scheme it was in practice difficult to establish fraud, such as cases where there was collusion between an employer and employee who was working whilst being claimed for under the furlough scheme.[17] HMRC also told us that the increasing number of business insolvencies may affect its ability to collect overpayments from businesses facing genuine financial hardship.[18] HMRC said that it would be targeting the most egregious behaviours and cases but it was not going to argue with people about fine judgements or try to find genuine mistakes that people made.[19]

9. In its evidence to us, TaxWatch said the legacy of the employment support schemes risks being damaged if more is not done to recover the billions of pounds stolen from them.[20] The Association of Accounting Technicians submitted evidence to us in which it said HMRC's current target for recoveries somewhat lacks ambition and HMRC needs do more to recover losses from errors and fraudulent payments.[21] We asked HMRC how much extra money it would need to get the remaining £4 billion back. HMRC told us that it was not sure whether further spending on recovering employment support schemes payments would provide it with the greatest payback, although it recognised such action might be important for other reasons. We told HMRC that its answer reinforced the impression that it had written off chasing fraudulent payments and errors as too difficult and too resource intensive. It responded that it had made a realistic assessment of what it thought it could recover.[22]

Error and fraud on research and development tax reliefs

10. HMRC is responsible for administering Corporation Tax research and development (R&D) reliefs, which support companies that work on innovative projects. There is a scheme for small and medium-sized enterprises, and a research and development expenditure credit scheme, mainly for larger companies. Both schemes are complex and open up opportunities for abuse.[23]

11. The cost of R&D tax reliefs has grown by 241% over the last four years to reach £9.3 billion in 2020–21 (**Figure 1**). In 2019, UK companies claimed tax relief on £47.5 billion of R&D spending; 83% more than the Office for National Statistics' (ONS) estimate of privately financed business R&D spending in the UK. HM Treasury has said that while this gap is partly explained by companies being able to claim tax relief for activity taking

16 Q 70, HM Treasury, Budget 2021, Protecting the jobs and livelihoods of the British people, 3 March 2021, HC 1226, para 2.61
17 Qq 72, 78–79
18 Note from the HM Revenue & Customs, received 22 December 2021.
19 Qq 100, 144, 149
20 Written Evidence HMP0004-Tax Watch, para 63
21 Written Evidence HMP0002- Association of Accounting Technicians, para 2.3, 3.34
22 Qq 140–142
23 C&AG's Report, para 18, 4.28

place overseas, this does not account for the full difference. The difference was also much smaller in 2015, when spending claimed for R&D reliefs had been 35% higher than ONS's estimate.[24]

Figure 1

Cost of R&D tax reliefs

Year	Expenditure £m (Note 1)	% change since 2016–17
2016–17	2,737	–
2017–18	2,879	5%
2018–19	4,866	78%
2019–20	8,770	220%
2020–21	9,325	241%

NOTES

Expenditure is the total for the two R&D schemes.

Source: HMRC, Annual Report & Accounts, 2016–17, 2017–18, 2018–19, 2019–20 and 2020–21

13. HMRC estimates that error and fraud in R&D tax reliefs was £336 million in 2020–21, or 3.6% of related expenditure (2019–20 – £311 million or 3.6% of related expenditure). The C&AG considers the level of error and fraud estimated by HMRC to be material and qualified his regularity opinion in 2020–21 as he had first done in 2019–20. The actual level of error and fraud could be much higher as HMRC's estimates involve judgements and assumptions.[25]

14. We asked HMRC how much of the increase in the cost of R&D tax reliefs was down to abuse. HMRC said monitoring was difficult because over time R&D tax reliefs had become increasingly generous and thus an increase in claims would be expected. It also said that claims have consistently exceeded forecasts, and it had therefore tried to understand the reasons why. We asked HMRC about the nature of fraud it had identified and whether there were trends in particular types. In response, HMRC focused on the role of advisers who, it said, approach businesses and suggest, incorrectly, that some expenditure can be recharacterised as R&D to get tax relief. HMRC explained that when it challenges a claim, it can find the adviser has gone and the business does not know a great deal about the rationale for the claim. HMRC confirmed that it had a watchlist of advisers that it was worried about. It said the list would be of great benefit to it when claimants are required to disclose who helped them with their claim.[26]

15. Given the uncertainties in HMRC's current estimates of error and fraud in R&D relief claims, we asked HMRC what it was doing to improve its estimates. It told us that it was planning a random enquiry programme for R&D claims which will inform its estimate. We expressed our concerns that HMRC was not on top of the abuse problem. HMRC said that it had increased the resources it deployed on R&D compliance. Referring to Budget 2021 and a November 2021 HM Treasury report on R&D tax reliefs published

24 HMRC, National statistics, Research and Development Tax Credits Statistics: Updated 30 September 2021, section 10 and HM Treasury, R&D Tax Reliefs – Report, November 2021, para 1.6

25 C&AG's Report, 4.32, 4.34–4.35, 4.37

26 Qq 133–135

the day before our evidence session, HMRC said that it had been advising Ministers about the extent to which it could control abuse operationally through its compliance response, and whether policy changes may be required to R&D reliefs. HM Treasury's report set out the government's plans to target abuse of R&D reliefs and improve compliance.[27]

Tax compliance

16. HMRC estimated that compliance yield from its tax compliance activities in 2020–21 was £30.4 billion. Yield was down 18% from the £36.9 billion HMRC generated in 2019–20. HMRC has reported the reduction reflected higher than usual performance in 2019–20 and lower than usual performance in 2020–21. In 2019–20, HMRC's performance was boosted by a small number of large, one-off successful litigations cases. In 2020–21, HMRC's compliance activity and yield were affected by pandemic restrictions and HMRC redeploying an average of 6% of its compliance staff to its COVID-19 response. HMRC also took a sympathetic approach to those struggling to pay their tax in 2020–21, only opening an enquiry into those affected by the pandemic if it thought the customer could engage. HMRC opened 29% fewer civil compliance cases in 2020–21 than in 2019–20 (256,000 compared with 361,000) and closed 26% fewer cases (250,000 compared with 338,000).[28]

17. We asked HMRC whether it was going to return to the cases it had not taken forward during 2020–21. It told us that, by and large, the action it took in 2020–21 would defer its ability to correct any non-compliance and recover tax, and it would not involve a significant loss of revenue as tax legislation enables it to go back to earlier years if HMRC finds non-compliance. HMRC said it was now picking up new cases and restarting the cases that it had put on hold. HMRC said compliance yield will continue to be depressed in 2021–22, but by 2022–23 it hoped that it would have normal volumes of work, would be pursuing normal timelines for clearing cases, and compliance yield would be back on "an even keel".[29]

18. We raised our concerns with HMRC that the impact of COVID-19 will make it difficult to make like for like comparisons of its performance. HMRC agreed that there will be distortions but said it would do its best to be transparent. It also said it will look at how it can present as clear a picture as possible and it would consider how to identify its performance on deferred cases.[30]

19. HMRC's annual report shows that it spent over £1.5 billion on compliance activities in 2020–21.[31] The rate of return from those activities varied across HMRC's five customer groups in 2020–21 (**Figure 2**). Returns were highest from large businesses, with average yield of £60 for each £1 HMRC spent on compliance, and wealthy individuals (£16 to £1). Returns were much lower for compliance spending on individual customers (not included in the wealthy group) and small businesses.

27 Qq 136–138, HM Treasury, R&D Tax Reliefs Report, November 2021
28 C&AG's Report, para 7, 1.22–1.23
29 Qq 18, 44–45
30 Qq 45, 50
31 HMRC, *Annual Report & Accounts 2020–21*, pages 42 and 43

Figure 2

HMRC's compliance yield and spend by customer group 2020–21

Customer group	Estimated compliance yield from HMRC activities (to nearest £0.1 billion)	Estimated spend on compliance activities (to nearest £10 million)	Average rate of return (ratio of yield to spend)
Individual customers	2.6£bn	410£m	6.3:1
Wealthy individuals	3.0£bn	190£m	15.8:1
Small businesses	5.3£bn	480£m	11.0:1
Mid-sized businesses, charities and public bodies	3.1£bn	260£m	11.9:1
Large businesses	13.2£bn	220£m	60:1
Total	**£27.2bn**	**£1,560m**	**17.4:1**

Source: HMRC, Annual Report & Accounts 2020–21, pages 42 and 43

20. We asked HMRC whether it would generate more revenue if it concentrated more of its compliance activities on large companies and less on small businesses and individuals. It told us that payback was a key factor when deciding how to deploy its resources, but not the only one. HMRC added that the marginal yield from additional compliance spending would not necessarily be as high as average yield. It also told us that its compliance work had to cover all aspects of the tax gap and that small businesses account for a large proportion of that gap. It explained that tackling non-compliance in small businesses was quite expensive and thus the rate of return is lower. It also said it constantly adjusted the amount of resource that it put into the directorates that cover its different customer groups.[32]

21. In its evidence to us TaxWatch argued for a substantial investment in tax compliance to ensure that public confidence in the tax system is maintained and enhanced.[33] In its evidence, the Association of Accounting Technicians (AAT) argued that HMRC should undertake more audits of taxpayers, and, in its evidence, Unchecked UK called for targeted audits of large businesses.[34] Both TaxWatch and AAT referred to research published by Warwick University in April 2021 into the effects of tax audits. AAT said the research suggests that undertaking more audits of taxpayers reduces evasion, avoidance, and error, and thus increases tax revenue.[35] Given this evidence, and the high returns across HMRC's compliance activities, we asked HMRC about its plans to expand its compliance activity. In response, HMRC explained why it had deferred compliance activity in 2020–21 while protecting revenue. It did not outline any plans to invest more in its compliance activities or whether it had made a case to HM Treasury to do so.[36] HMRC did however tell us that in spending review 2021, it had "been given some money for spend to raise. I think it's £30

32 Q39
33 Written Evidence HMP0004-Tax Watch, para 66
34 An audit involves a tax official undertaking a review of a tax return to ensure that the information that has been entered is correct.
35 Written Evidence HMP0002- Association of Accounting Technicians, paras 3.14–3.16 and Written Evidence HMP0003- Unchecked UK, para 29
36 Q 43

million, £60 million, £90 million over the three years." HMRC said it would be working with HM Treasury to determine the best thing to spend that money on.[37] £90 million is the equivalent of around 2% of the £4.3 billion cost of running HMRC in 2020–21.[38]

Tax avoidance

22. HMRC told us the nature of tax avoidance has changed. It said the bulk of avoidance schemes now relate to employment taxes and are not targeted at affluent people but middle-income earners, some of whom knowingly enter avoidance schemes and others who unwittingly get involved.[39] In 2019, HMRC introduced the loan charge to recoup tax from people who had used 'disguised remuneration' schemes to avoid income tax.[40]

23. We are concerned about how taxpayers are protected from those who promote avoidance schemes, and the financial damage that can follow if taxpayers unknowingly enter unlawful schemes. We therefore asked HMRC what progress it had made in pursuing the promoters of illegal schemes. It told us its strategy for tackling tax avoidance was two-pronged. It wants to reduce both the supply of schemes from tax advisers and the demand for them from taxpayers. HMRC considers it has been successful in driving the respectable end of the tax profession out of offering tax avoidance. It said what remains is a core of about 20 or 30 promoters many of whom are based offshore and hide behind complex corporate structures. HMRC told us that it had extensive powers for tackling promoters, and the government has recently announced further powers to enable HMRC to act more quickly against providers. It said it was using its full range of powers, from criminal investigation and prosecution through to using insolvency law and the Advertising Standards Authority to try and drive promoters out of the market. It also said that the location of promoters offshore did not deter it from bearing down on them.[41]

24. We asked HMRC whether it could do more to publicise its successes, including the naming and shaming promoters of avoidance schemes. HMRC explained how it was seeking to reduce demand through transparency. It said it published annual reviews of the tax avoidance market and it was more quickly disclosing information on promoters and their schemes, to warn off potential users as early as possible. HMRC also said it litigated if promoters did not comply with rules requiring the disclosure of tax avoidance schemes to the Department. HMRC told us that it was trying to identify as quickly as possible the people who have entered into avoidance schemes. It then tells these people they are in a tax avoidance scheme and offers them help to get out. HMRC told us this was a change in its operational approach. In the past HMRC would have opened an inquiry, picked a lead case to pursue to go through the tribunals and courts, with other cases left open which could lead to tax bills building up. We welcome this change in HMRC's approach and would like to see it do more to protect taxpayers.[42]

37 Q 142
38 C&AG's Report, page R4
39 Q 2
40 HMRC, Policy paper, Tax avoidance loan schemes and the loan charge, Updated 28 July 2021
41 Qq 2–5
42 Qq 2, 4–5

2 Customer service and transformation

Customer service

25. This Committee has regularly examined HMRC's customer service performance. In 2010, this Committee concluded HMRC's performance in responding to calls had been poor.[43] In 2016, the Committee found that customer service levels had collapsed as a result of HMRC assuming two new services, automated telephony and paperless self-assessment, would reduce the number of calls it received. HMRC released 5,600 staff, but phone demand did not fall and consequently its service levels collapsed.[44] HMRC's performance subsequently improved and in 2017–18 it achieved six of its eight customer service targets.[45] Since then, HMRC's performance has declined. In particular, its performance in answering calls and responding to post in 2020–21 was well below the levels in each of the three previous years. By the last quarter of 2020–21, the average time callers spent queuing to speak to an adviser was over 15 minutes (compared to less than 5 in 2017–18) and just 43% of post was responded to in 15 days (81% in 2017–18).[46]

26. We asked HMRC why response times were very poor at the end of 2020–21. HMRC said in the first half of 2020–21 it had diverted 5,000 customer service staff to work on COVID-19 support schemes. HMRC also said that during this period it did not have backlogs. It told us that in the second half of 2020–21, its customer services team had to continue to support the COVID-19 support schemes and 3,000 additional customer service staff were diverted to work related to the UK leaving the EU. It also told us that it "stayed strong on the fundamentals of the tax system", and it successfully managed the annual peaks in self-assessment and tax credits. It said that because of the priorities of paying money to vulnerable people, COVID-19 and customs, given the UK's exit from the EU, it had to put other parts of tax activity to one side, and it started to build-up a "bit of a backlog".[47]

27. HMRC told us that its performance was improving in 2021–22. It said it had got helpline performance up to what it regarded as a "decent service", and had thus diverted resources to handling post, as this was the area with most backlogs.[48] HMRC's latest published quarterly performance update, shows that in the first half of 2021–22, its performance in responding to post was worse than in 2020–21, with less than 40% of post responded to within 15 days.[49]

28. We asked HMRC why call handling performance had been declining before COVID-19. HMRC told us that it was resourced to give a "decent" rather than "brilliant" service and it had efficiencies that it had to deliver. It said that although some phone contact was very important to HMRC and to the taxpayer, some of it was "low value", in the sense that it did not change tax outcomes. HMRC's strategy is to reduce this type of

43 HC Committee of Public Accounts, *HM Revenue & Customs: Handling telephone enquiries*, Twenty-fourth Report of Session 2009–10, HC 389, March 2010, page 3
44 HC Committee of Public Accounts, *Quality of service to personal taxpayers and replacing the Aspire contract*, Thirteenth Report of Session 2016–17, HC 78, Incorporating HC 79, July 2016, pages 3 and 4
45 HC Committee of Public Accounts, *HMRC's performance in 2017–18*, Sixty-Sixth Report of Session 2017–19, HC 1526, November 2018, para 20
46 C&AG's Report, para 1.28–1.29, Figure 7, Figure 8
47 Q 117
48 Q 119
49 HMRC, HMRC quarterly performance report: July to September 2021, November 2021

contact or to get people to self-serve online if they can.[50] HMRC believes that its spending review settlement for the next three years is sufficient to enable it to do a good job, but the settlement requires it to make efficiencies. If it does not achieve these efficiencies, customers were likely to experience a poorer service.[51]

29. For 2021–22, HMRC has replaced most of its response time measures with metrics of whether it is easy for customers to access and deal with HMRC.[52] Rather than call handling times, it now publicly reports the percentage of callers wishing to speak to an adviser who are able to get through. It continues to report publicly on its postal response times but has not set a target for the number it responds to in 15 days.[53]

Making Tax Digital

30. HMRC's Making Tax Digital initiative is central to its 10-year modernisation strategy. It requires taxpayers to keep tax records and submit returns digitally. HMRC introduced Making Tax Digital for VAT first. The largest VAT traders provided digital returns in 2019, and the smaller ones are being required to do so by April 2022.[54] HMRC now plans to extend Making Tax Digital to income tax self assessment. From April 2024, 4.2 million taxpayers with business and/or property income over £10,000, including small landlords and sole traders, will be required to submit digital returns each quarter. HMRC had intended to introduce this extension to Making Tax Digital from April 2023 but decided to delay by a year because of the impact of the pandemic and stakeholder feedback.[55]

31. We asked HMRC what Making Tax Digital was for. HMRC told us Making Tax Digital was about making tax easier, keeping tax in line with the digital age and making business more productive.[56] HMRC also told us that, by providing real time or up-to-date data on taxpayers, Making Tax Digital would help it if it ever needed to introduce a support scheme like the Self-Employment Income Support Scheme again, although such a benefit was not one of the original reasons for introducing Making Tax Digital.[57]

32. We were concerned about the impact of Making Tax Digital on the smaller taxpayer, such as a retired person with rental income from one property. We noted that other administrative tax changes, such as on-line self-assessment, have not provided expected benefits to taxpayers because of problems with software.[58] We pointed out that it felt like Making Tax Digital might lead to small taxpayers serving HMRC rather that HMRC serving them.[59] We asked HMRC how Making Tax Digital would benefit small taxpayers. HMRC noted that its evaluation suggested that VAT traders found that Making Tax

50 Qq 120, 125–126
51 Q 131
52 C&AG's Report, para 1.32
53 HMRC, HMRC quarterly performance report: July to September 2021, November 2021 and HMRC, HM Revenue and Customs Outcome Delivery Plan: 2021 to 2022, July 2021
54 C&AG's Report, paras 2.28, 2.31
55 HMRC, Policy paper Extension of Making Tax Digital for Income Tax Self-Assessment to Businesses and Landlords, 23 September 2021 and HMRC, Guidance Using Making Tax Digital for Income Tax, October 2021
56 Q 54
57 Qq 61–62
58 Qq 56–57, 65
59 Q 62

Digital had made dealing with their tax affairs easier. HMRC also pointed out that self-employed taxpayers with income under £10,000 a year would not be mandated to be part of Making Tax Digital.[60]

33. We asked about the support and software that would be available to small taxpayers. HMRC said it was gearing up to support customers but that it would not be delivering software itself. Nevertheless it had received pledges from industry that they would, as they did for VAT, provide free-at-point-of-service software for those taxpayers with the most simple needs.[61] HMRC said the software industry had plenty of time to act on user research and get software right by 2024.[62]

HMRC's estates strategy

34. We have long-standing concerns about HMRC's estates strategy. In April 2017, long before COVID-19, this Committee raised concerns about HMRC locking government into holding larger properties for longer than needed. The Committee raised similar concerns again in January and April 2018. In January 2021, we concluded that HMRC's estate strategy risks becoming woefully out of date. We recommended that HMRC review its estate strategy in light of the impact of COVID-19 on the demand for commercial properties.[63] Since January 2021, HMRC has revisited its assumptions on attendance rates following changes in working patterns as a result of the pandemic. It now considers that attendance rate at its regional centres will reduce from its original estimate of around 67% of working days to around 50%.[64] HMRC confirmed during the evidence session that it was planning for hybrid working to be permanent.[65]

35. Given the change in HMRC's need for office space, and wider changes in the commercial property market, we asked HMRC whether its estate strategy was right for the future. HMRC told us its strategy was the right one and was part of making HMRC fit for the future by providing a high-quality estate. It also told us that the quality and location of the estate made it easy to offer to other government departments, as part of the broader move of civil service roles from London into other parts of the UK. HMRC said it had already let space, and there was currently a queue of organisations also wishing to let space.[66] It said it has leased 583,000 meters squared of space of which 107,000 meters squared (18%) has been "signed up to" by Other Government Departments. HMRC expects the amount of space it sublets in 2023–24 to increase to 117,000 meters squared (23% of the total space it expects to lease).[67]

36. We asked about the Cabinet Office's role in co-ordinating government office space. HMRC said it relies on the controls operated by the Cabinet Office, who look at all new property deals and lease extensions, and make sure those needing space are pointed at HMRC's buildings. HMRC said space would be let to central government organisations

60 Qq 55–58
61 Q 59
62 Q 65
63 HC Committee of Public Accounts, *HMRC performance 2019–20*, Thirty-Sixth Report of Session 2019–21, HC 690, January 2021, page 6
64 C&AG's Report, para 2.19
65 Q 47
66 Qq 46, 48, 51
67 Note from the HM Revenue & Customs, received 22 December 2021.

first, other public sector organisations next and then the private sector. It considered that Cabinet Office's controls were currently working well, and it said the Cabinet Office needed to continue to make them work.[68]

68 Qq 51–53

Formal minutes

Wednesday 2 February 2022

Members present:

Dame Meg Hillier, in the Chair

Dan Carden

Sir Geoffrey Clifton-Brown

Peter Grant

Sarah Olney

Kate Osamor

Nick Smith

HMRC Performance in 2020–21

Draft Report (*HMRC Performance in 2020–21*), proposed by the Chair, brought up and read.

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

Paragraphs 1 to 36 read and agreed to.

Summary agreed to.

Introduction agreed to.

Conclusions and recommendations agreed to.

Resolved, That the Report be the Thirty-seventh 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.

Adjournment

Adjourned till Monday 7 February at 3:30pm

Witnesses

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

Wednesday 1 December 2021

Jim Harra, Chief Executive and First Permanent Secretary, HMRC; **Angela MacDonald**, Second Permanent Secretary, HMRC; **Joanna Rowland**, Director General Transformation Business Group, HMRC; **Justin Holliday**, Chief Finance Officer, HMRC Q1–149

Published written evidence

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

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

1 Association of Accounting Technicians (AAT) (HMP0002)

2 TaxWatch (HMP0004)

3 TaxWatch (HMP0005)

4 Unchecked UK (HMP0003)

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.

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2nd	BBC strategic financial management	HC 187
3rd	COVID-19: Support for children's education	HC 240
4th	COVID-19: Local government finance	HC 239
5th	COVID-19: Government Support for Charities	HC 250
6th	Public Sector Pensions	HC 289
7th	Adult Social Care Markets	HC 252
8th	COVID 19: Culture Recovery Fund	HC 340
9th	Fraud and Error	HC 253
10th	Overview of the English rail system	HC 170
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13th	Initial lessons from the government's response to the COVID-19 pandemic	HC 175
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17th	High Speed 2: Progress at Summer 2021	HC 329
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23rd	Test and Trace update	HC 182
24th	Crossrail: A progress update	HC 184
25th	The Department for Work and Pensions' Accounts 2020–21 – Fraud and error in the benefits system	HC 633
26th	Lessons from Greensill Capital: accreditation to business support schemes	HC 169
27th	Green Homes Grant Voucher Scheme	HC 635

Number	Title	Reference
28th	Efficiency in government	HC 636
29th	The National Law Enforcement Data Programme	HC 638
30th	Challenges in implementing digital change	HC 637
31st	Environmental Land Management Scheme	HC 639
32nd	Delivering gigabitcapable broadband	HC 743
33rd	Underpayments of the State Pension	HC 654
34th	Local Government Finance System: Overview and Challenges	HC 646
35th	The pharmacy early payment and salary advance schemes in the NHS	HC 745
36th	EU Exit: UK Border post transition	HC 746
1st Special Report	Fifth Annual Report of the Chair of the Committee of Public Accounts	HC 222

Session 2019–21

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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
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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

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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
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35th	Improving Broadband	HC 688
36th	HMRC performance 2019–20	HC 690
37th	Whole of Government Accounts 2018–19	HC 655
38th	Managing colleges' financial sustainability	HC 692
39th	Lessons from major projects and programmes	HC 694
40th	Achieving government's long-term environmental goals	HC 927
41st	COVID 19: the free school meals voucher scheme	HC 689
42nd	COVID-19: Government procurement and supply of Personal Protective Equipment	HC 928
43rd	COVID-19: Planning for a vaccine Part 1	HC 930
44th	Excess Votes 2019–20	HC 1205
45th	Managing flood risk	HC 931
46th	Achieving Net Zero	HC 935
47th	COVID-19: Test, track and trace (part 1)	HC 932
48th	Digital Services at the Border	HC 936
49th	COVID-19: housing people sleeping rough	HC 934
50th	Defence Equipment Plan 2020–2030	HC 693
51st	Managing the expiry of PFI contracts	HC 1114
52nd	Key challenges facing the Ministry of Justice	HC 1190
53rd	Covid 19: supporting the vulnerable during lockdown	HC 938
54th	Improving single living accommodation for service personnel	HC 940

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55th	Environmental tax measures	HC 937
56th	Industrial Strategy Challenge Fund	HC 941