National Audit Office

Report by the Comptroller and Auditor General

HM Revenue & Customs 2022-23 Accounts

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Issued under Section 2 of the Exchequer and Audit Departments Act 1921

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This report provides the findings and overall conclusion of work conducted under section 2 of the Exchequer and Audit Departments Act 1921, by which the Comptroller and Auditor General must consider the adequacy of the systems to assess, collect and allocate tax revenues.

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Contents

Coverage of this report

HMRC corporate document	Coverage of this report
Trust Statement	HM Revenue & Customs (HMRC) reported £814.0 billion of tax revenue for 2022-23. Under the Exchequer and Audit Departments Act 1921, the Comptroller and Auditor General (C&AG) must certify whether the Trust Statement is true and fair, and whether HMRC has used the income and expenditure for the purposes Parliament intended. The C&AG has concluded that: • the figures in the Trust Statement are true and fair; and • HMRC has used income and expenditure for the purposes Parliament intended. The 1921 Act also requires the C&AG to consider whether HMRC's systems to collect tax are adequate. We found that HMRC's systems to collect taxes are adequate, subject to the observations in this report and other reports to Parliament.
Resource Accounts	The cost of running HMRC in 2022-23 was £6.9 billion. HMRC paid out £34 billion, including £8.8 billion of Personal Tax Credits and £11.6 billion of Child Benefit. Under the Government Resources and Accounts Act 2000, the C&AG must certify whether HMRC's Resource Accounts are true and fair, and whether HMRC has used the income and expenditure for the purposes Parliament intended. The C&AG has concluded that: • the Resource Accounts are true and fair; but • there remains a material level of error and fraud in Corporation Tax research and development reliefs (Part Two); and • there remains a material level of error and fraud in Personal Tax Credits expenditure (Part Three)
Annual Report	We reviewed HMRC's performance against its main objective of collecting tax revenues and considered the main components of the £814.0 billion raised during 2022-23 (Part One). We reviewed whether HMRC is delivering value for money and report our findings to Parliament under section 6 and section 9 of the National Audit Act 1983.

Summary

HM Revenue & Customs' performance, 2022-23

1 HM Revenue & Customs (HMRC) is responsible for administering the UK's tax system. HMRC's strategic objectives are to:

- collect the right tax and pay out the right financial support;
- make it easy to get tax right and hard to bend or break the rules;
- maintain taxpayers' consent through fair treatment and protect society from harm;
- make HMRC a great place to work; and
- support wider government economic aims through a resilient, agile tax administration system.

2 This report sets out our factual commentary on HMRC's performance in 2022-23, together with the reasons and context for the Comptroller and Auditor General's (C&AG's) qualification of his opinion on the regularity of HMRC's 2022-23 Resource Accounts. It draws on the findings from our statutory audit work in respect of HMRC during the period, including the audits of HMRC's financial statements; the adequacy of its systems for collecting revenue; and the value for money it achieved from its spending (see Appendix One). This report does not reach a separate conclusion on the value for money of HMRC's expenditure.

3 In this report we cover:

- HMRC's performance against its 2022-23 objective of collecting revenues and managing compliance, the main components of the £814.0 billion raised in 2022-23 and HMRC's customer service and debt management performance (Part One);
- the basis of the C&AG's qualification of his opinion on the regularity of HMRC's Resource Accounts in relation to error and fraud in Corporation Tax research and development reliefs (Part Two); and
- the basis of the C&AG's qualification of his opinion on the regularity of HMRC's Resource Accounts in relation to error and fraud in Personal Tax Credits (Part Three).

Summary findings

Total revenues

4 **HMRC reported total revenues of £814.0 billion for 2022-23, the highest on record, representing an 11.3% increase on 2021-22.** Total revenues increased by £82.9 billion compared with 2021-22 (£731.1 billion). HMRC reported increases in most revenue streams, reflecting the impact of inflation on taxable goods, services and profits, and the freezing of tax bands and thresholds. This increased the size of the taxpayer population and moved some taxpayers into higher tax brackets. Since 2019-20, the year before the COVID-19 pandemic, total revenues have increased by £177.3 billion (27.8%). The four largest components of revenue in 2022-23 were Income Tax, National Insurance Contributions, Value Added Tax (VAT) and Corporation Tax, which together accounted for 83.7% (£681.2 billion) of the total (paragraph 1.2 and Figure 1).

5 **HMRC estimates that the tax gap – the difference between the amount of tax that should, in theory be paid to HMRC, and what was actually paid – has remained at 4.8% of all tax liabilities, equivalent to £35.8 billion in 2021-22.** HMRC's estimate of the tax gap for 2020-21 was 4.8% and £30.8 billion; HMRC revised it down from the 5.1% and £32.2 billion previously reported due to updated data on consumer spending. The tax gap arises for several reasons including mistakes, failure to take reasonable care, avoidance and evasion of tax, and insolvency, and can be affected by factors such as changes in the economy and demographics. In monetary terms, HMRC estimates that the tax gap for personal income taxes, particularly Self Assessment, increased the most. The tax revenue HMRC generated from its tax compliance work declined as a percentage of theoretical tax liabilities in 2020-21 and 2021-22, but HMRC's estimates do not indicate any increase in the size of the tax gap as a result. The pandemic has made reconciling movements in the tax gap to changes in revenue more complex. HMRC defines theoretical tax liabilities as the tax gap plus the amount of tax it actually receives. Its estimate of total theoretical liabilities of £739.3 billion for 2021-22 is just £8.2 billion more than total revenues in that year (paragraphs 1.19 to 1.23 and Figure 4 and Figure 5).

6 **HMRC estimates that the yield from its tax compliance activities in 2022-23 was £34 billion, up 10% compared with 2021-22 but £2 billion below its target.** Compliance yield measures the effectiveness of HMRC's compliance and enforcement activities. It is one of HMRC's main performance measures. The yield reported in 2022-23 is lower than HMRC's target for the year of £36 billion. Compliance yield is affected by interventions in previous years. HMRC explained it is still seeing the effects of reduced compliance activity during the COVID-19 pandemic in its 2022-23 performance. HMRC set its target at a level to maintain the tax gap. HMRC's compliance yield in 2022-23 represents 4.2% of total revenues, the same as in 2021-22 and below the five-year average of 5.2% achieved between 2015-16 and 2019-20 before the pandemic (paragraphs 1.24 to 1.31 and Figure 6 and Figure 7).

7 **Tax debt was £43.9 billion at 31 March 2023, £4.7 billion (11.9%) more than the debt reported at 31 March 2022.** As a proportion of annual revenues, it has remained at 5.4%. The tax debt balance is lower than the £68.5 billion reported at the height of the pandemic but remains significantly higher than the pre-pandemic level. In the five years between 2015-16 and 2019-20, tax debt was typically around £14 billion. The increase in tax debt reported reflects the impact of the current economic conditions on taxpayer finances, meaning more taxpayers are in debt and debts are getting older as taxpayers struggle to pay them. HMRC's research suggests taxpayers may be prioritising other debts before paying their debts to HMRC. There were over one-fifth more new tax debts in 2022-23 than the number of tax debts HMRC was able to clear, while the number of tax debts older than 12 months increased by 25%. HMRC has increased the number of staff to help taxpayers manage their debt and is purchasing data from credit reference agencies to better tailor its debt collection. HMRC has a new strategy to bring down tax debt in the long term but accepts that it will remain at the current higher level throughout 2023-24 (paragraphs 1.10 to 1.15 and Figure 3).

Customer service performance

8 **HMRC's customer service performance remained well below its expected service standards in 2022-23, with particular problems faced by taxpayers wanting to speak to an adviser.** Taxpayers' satisfaction with HMRC's customer services fell further in 2022-23, continuing the trend seen during the pandemic. The performance of HMRC's telephone services was particularly low, with HMRC reporting higher demand than in 2021-22. The average speed of answering calls to HMRC helplines was 16:24 minutes (2021-22: 12:22 minutes), with three-fifths of callers (62.7%) waiting more than 10 minutes to speak to an adviser, up from 46.3% in 2021-22. HMRC's digital services performance was relatively stable. Performance on customer correspondence improved, with 72.7% cleared within 15 working days, but from a low base in 2021-22 of 45.5% and still below HMRC's expected standard of 80%. HMRC says that its existing resources are insufficient to meet forecast demand for phone and post services at the standard it expects. It is instead encouraging taxpayers to self-serve using digital services where they can, although it accepts this transition will take some time. It is employing an average of 1,630 additional temporary staff each month between April and September 2023 to meet some of the additional demand on phone and post services. This follows a reduction of 834 (5%) customer service staff in 2022-23. In recent months it has closed two of its customer helplines: its Self Assessment helpline on a temporary three-month basis, and its VAT registration helpline indefinitely (paragraphs 1.37 to 1.47 and Figure 9 and Figure 10).

Error and fraud in Corporation Tax research and development reliefs and Personal Tax Credits

9 **The C&AG has qualified his opinion on the regularity of HMRC's 2022-23 Resource Accounts due to the material level of error and fraud in Corporation Tax research and development reliefs.** The research and development relief schemes are complex and have proved attractive to those seeking to abuse them, opening up opportunities for fraud. HMRC used the results of a random enquiry programme for the first time to produce an estimate of error and fraud for 2020-21 and in turn an illustrative estimate for 2022-23 of £1.1 billion or 13.3% of related expenditure. This is more than double HMRC's 2021-22 estimate of £469 million (4.9%), which it calculated using its previous methodology, and now provides a more realistic assessment of the rate of error and fraud present in the schemes. HMRC's estimate for 2022-23 includes an assumption that recent compliance interventions will have reduced error and fraud by £250 million. It will not know the actual impact of these interventions until it has completed and evaluated its random enquiries on 2022-23 returns from claimants for that year (paragraphs 2.2 to 2.21 and Figure 11).

10 **HMRC's revised estimate of error and fraud in Corporation Tax research and development reliefs for 2020-21 is £1.1 billion (16.7% of related expenditure).** There is a two-year lag between claimants incurring qualifying expenditure and submitting a return to HMRC. Taken together with the time HMRC needs to open and close its random enquiries, this means that the claims it has currently tested date back as far as 2018-19. HMRC considers that applying the results from its random enquiry programme to 2020-21 expenditure produces the most statistically robust estimate of error and fraud. HMRC estimates that in 2020-21, error and fraud in Corporation Tax research and development reliefs could have been as high as £1.6 billion (23.2%) or as low as £0.9 billion (13.0%) (paragraph 2.13).

11 **HMRC's random enquiry programme found that for the Small- and Medium-sized Enterprise (SME) scheme one-quarter of the value of claims were non-compliant.** Of the £1.1 billion of error and fraud HMRC has estimated for research and development reliefs in 2020-21 as a whole, £1.0 billion relates to the SME scheme. This represents an error and fraud rate of 24.4%, which is among the highest reported across all government spending programmes, including those administered in response to the pandemic. HMRC's random enquiry programme found that 50% of claims filed in 2020-21 that it inspected were non-compliant where some or all of the claim was for expenditure that did not meet the qualifying criteria (paragraphs 2.13 and 2.16 and Figure 11).

12 The C&AG has also qualified his opinion on the regularity of HMRC's 2022-23 Resource Accounts due to the material level of error and fraud in Personal Tax Credits. HMRC's estimate for 2021-22, the most recent available, indicates that error and fraud resulted in overpayments of 4.5% of tax credits expenditure. This is lower than HMRC's revised estimate for the 2020-21 overpayment rate of 4.7%, which it initially reported as 5.0% (note 5.1.3 to the HMRC Resource Accounts). Errors in tax credits resulting in underpayments amounted to 0.4% of expenditure, which is lower than 0.8% in 2020-21. These rates equate to overpayments of £510 million from an estimated 280,000 claims, or on average, £1,821 per claim (a reduction of £220 million compared with finalised 2020-21 estimates) and underpayments of £40 million from an estimated 70,000 claims, or on average £571 per claim (a reduction of £80 million compared with the finalised figures for 2020-21) (paragraphs 3.5 to 3.14 and Figure 12).

Conclusion

13 In fulfilling our statutory duties under the Exchequer and Audit Departments Act 1921, while recognising that no tax collection system can ensure that everyone meets their tax obligations, we conclude that, in 2022-23, HMRC framed adequate regulations and procedures to secure an effective check on the assessment, collection and proper allocation of revenue, and that they are duly carried out. This assurance is subject to the observations on specific aspects of the administration of taxes in this report and our other reports to Parliament.

14 HMRC reported record tax revenues for 2022-23, reflecting the impact of inflation on taxable goods, profits and services and the freezing of tax bands and thresholds. This has increased demand for HMRC's services at a time when it is facing its own spending pressures, both of which have affected its performance during the year.

15 HMRC missed its compliance yield target, with yield reported still lower than the average it achieved before the pandemic. This will need to improve if HMRC is to continue to maintain the tax gap. Tax debt remains high as the current economic conditions push more taxpayers into debt and for a longer period of time. HMRC will need to ensure its debt management strategy delivers on its aims of supporting those taxpayers who most need it and collecting tax from those who can afford to pay more quickly.

16 Taxpayers and their agents are still not receiving the support they expect, with customer service performance remaining considerably below HMRC's own targets and historical performance levels. HMRC's plans to move more customer enquiries onto digital channels may address this in the longer term, but it will need to improve how it services current demand while those plans are being implemented and have a contingency should they take longer than anticipated.

17 HMRC now has a more realistic picture of the extent to which Corporation Tax research and development reliefs are being abused. It needs to carefully consider the adequacy of its current compliance approach and the case for inspecting more claims from the period before the point at which the scale of abuse became clear.

Recommendations

18 HMRC should:

a consider whether the scale and focus of its current compliance arrangements for Corporation Tax research and development reliefs are adequate, now that it has a better understanding of the extent to which these schemes are being abused; and

b assess whether it should inspect more Corporation Tax research and development relief claims made prior to the period covered by its latest estimate. This assessment should balance the costs of carrying out further reviews and the expected rate of return on any error and fraud these reviews may identify.

Part One

Performance in 2022-23

1.1 This part of the report sets out HM Revenue & Customs' (HMRC's) performance in 2022-23 in collecting revenues due and managing compliance. Performance is measured by the revenues reported in HMRC's Trust Statement, and the tax gap and compliance yield, which are disclosed in its Annual Report. This part also considers customer service and debt management performance reported by HMRC in 2022-23.

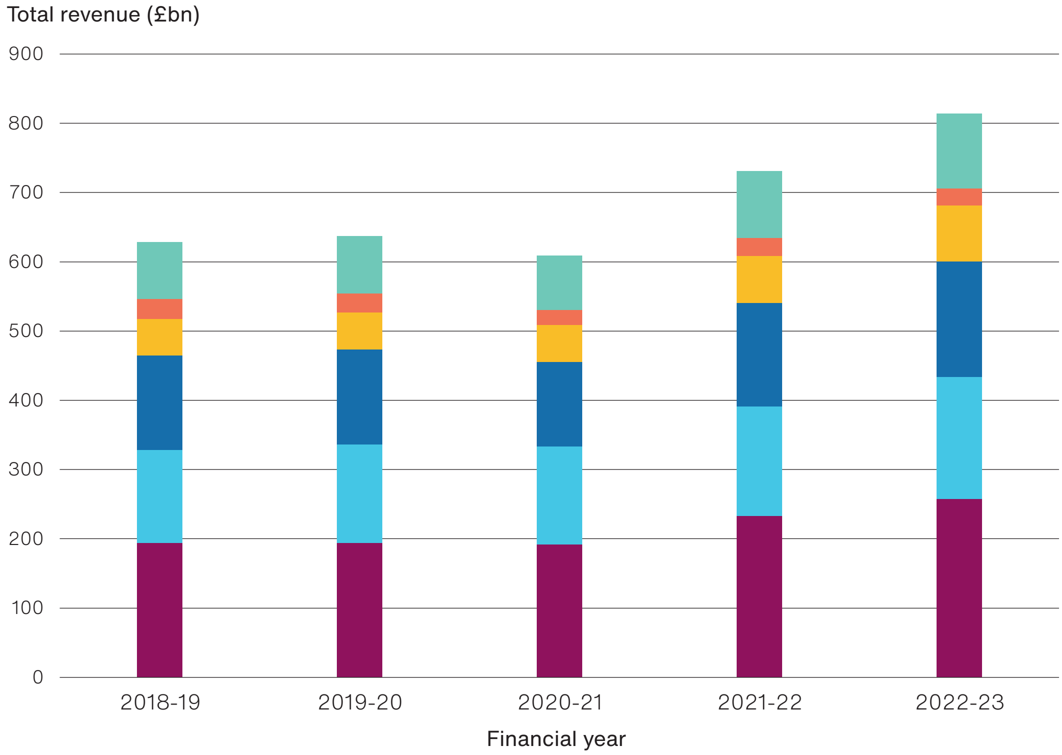
Total revenue in 2022-23

1.2 The total revenue HMRC reported in its Trust Statement for 2022-23 was £814.0 billion (£731.1 billion in 2021-22) (**Figure 1** overleaf).[1] Total revenues increased by £82.9 billion (11.3%), driven by large percentage increases in most taxes. Tax bands and thresholds remained largely unchanged in 2022-23, meaning wage rises increased the size of the taxpayer population and moved some taxpayers into higher tax brackets. Inflationary increases in the prices of taxable goods and services and on companies' profits also contributed to the increase in tax revenues. The following four taxes accounted for 87.3% of the increase: Income Tax (an increase of £24.6 billion (10.5%) from 2021-22), Value Added Tax (VAT) (£18.1 billion, 12.2%), National Insurance Contributions (NICs) (£17.5 billion, 11.1%) and Corporation Tax (£12.2 billion, 17.9%). Total revenues in 2022-23 are the highest ever reported by HMRC and have increased by £177.3 billion (27.8%) since 2019-20, before the COVID-19 pandemic.

1 HMRC records revenue in the Trust Statement on an accruals basis, other than for those taxes disclosed in Note 1.2 of the Trust Statement accounts. Accounting for tax on an accruals basis means that the revenue figures reported relate to tax due on earned income or activities during the financial year, regardless of when HMRC receives the cash. Values throughout the report are in nominal terms to maintain consistency with HMRC's Trust Statement and its wider Annual Report and Accounts.

Figure 1
Total revenues reported by HM Revenue & Customs (HMRC), 2018-19 to 2022-23

In 2022-23 total revenues increased by 11.3% to their highest reported level



	2018-19	2019-20	2020-21	2021-22	2022-23
Income Tax (£bn)	194.0	194.2	192.0	233.4	258.0
National Insurance Contributions (£bn)	135.0	141.9	141.5	158.3	175.8
Value Added Tax (£bn)	135.6	137.4	122.1	148.8	166.9
Corporation Tax (£bn)	53.5	53.0	53.7	68.3	80.5
Hydrocarbon oils duty (£bn)	28.0	27.4	21.3	25.8	25.0
Other (£bn)	81.8	82.8	78.2	96.5	107.8
Total revenue (£bn)	**627.9**	**636.7**	**608.8**	**731.1**	**814.0**
Change in total revenue from previous year (£bn)	–	8.8	-27.9	122.3	82.9
Change in total revenue from previous year (%)	–	1.4	-4.4	20.1	11.3

Notes

1 'Other' includes, for example, Stamp Taxes, Inheritance Tax, alcohol and tobacco duties, Insurance Premium Tax, Capital Gains Tax, student loan recoveries, environmental taxes, customs duties and fines and penalties.

2 Values are in nominal terms to maintain consistency with HMRC's Annual Report and Accounts.

3 Income Tax, National Insurance Contributions, Value Added Tax and Corporation Tax together accounted for 83.7% (£681.2 billion) of total revenue in 2022-23.

Source: National Audit Office analysis of HM Revenue & Customs Trust Statements 2018-19 to 2022-23

1.3 In March 2023, the Office for Budget Responsibility (OBR) forecast that public sector receipts in 2022-23 would increase by £102 billion (11.1%) compared with 2021-22, outperforming growth in the nominal gross domestic product (GDP), which was expected to rise by 7.1%.[2] The OBR's assessment highlighted particularly strong growth in:

- Pay As You Earn (PAYE) and NICs, where most thresholds have been frozen since April 2021. Nominal pay rises since then have both generated new taxpayers, where those individuals now earn more than the tax-free allowance, and moved others into higher tax brackets;
- VAT receipts, which reflects strong growth in nominal consumer spending and the end of some temporary tax cuts that were introduced during the COVID-19 pandemic. VAT cuts for the hospitality industry were in place between 15 July 2020 and 31 March 2022;
- Corporation Tax, with companies' underlying profits in 2022-23 being better than expected, as well as strong growth in sectors such as financial services, retail and professional services that are typically large payers of Corporation Tax; and
- Capital Gains Tax, which has shown stronger-than-expected Self Assessment receipts on liabilities in 2021-22, and higher payments on property disposals.

Repayments

1.4 The total revenue figure of £814.0 billion is net of £130.3 billion of repayments to taxpayers (£126.6 billion in 2021-22) (**Figure 2** overleaf). Repayments are a necessary part of tax administration and can arise for a variety of reasons. For instance, HMRC may demand payments on account from taxpayers before it has assessed their full liability, which can lead to repayments.

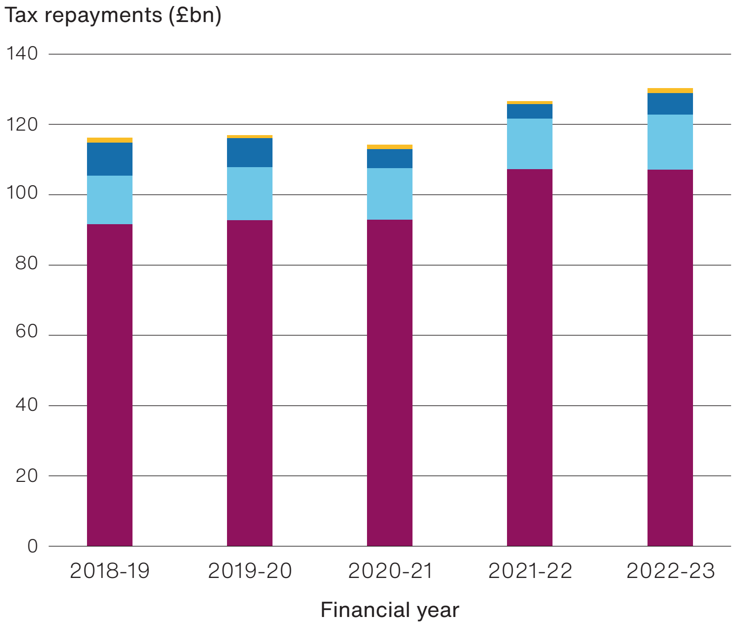
1.5 Most repayments relate to VAT (£107.2 billion in 2022-23, which compares with total VAT revenue in 2022-23 of £166.9 billion). VAT-registered taxpayers can claim back VAT on certain purchases they have made where they relate to the sale of goods and services. This is repaid to taxpayers net of the VAT due to HMRC on the sale of those goods and services.

2 Office for Budget Responsibility, *Economic and fiscal outlook,* March 2023, paragraph 4.6. The large majority of public sector receipts comes from taxes administered by HMRC. Other public sector receipts include Council Tax and Business Rates.

Figure 2

Repayments made by HM Revenue & Customs to taxpayers by tax type, 2018-19 to 2022-23

Total repayments in 2022-23 increased by 2.9%, with most repayments relating to Value Added Tax



	2018-19	2019-20	2020-21	2021-22	2022-23
Value Added Tax (£bn)	91.7	92.9	93.0	107.4	107.2
Income Tax and National Insurance Contributions (£bn)	13.8	15.0	14.6	14.3	15.7
Corporation Tax (£bn)	9.4	8.2	5.5	4.1	6.1
Other (£bn)	1.3	0.9	1.2	0.8	1.3
Total repayments (£bn)	**116.2**	**117.0**	**114.2**	**126.6**	**130.3**

Notes

1 ‘Other’ includes alcohol duties, Capital Gains Tax, hydrocarbon oils duties and stamp duties.

2 Total for 2020-21 does not sum due to rounding.

3 The values presented in this figure are in nominal terms.

Source: National Audit Office analysis of HM Revenue & Customs Trust Statements 2018-19 to 2022-23

Receivables, impairment and revenue losses

Receivables and accrued revenue receivables

1.6 Receivables represent taxpayer liabilities to HMRC that have been established, irrespective of whether they are due or overdue. They can include taxes, duties, recovery of tax credits, penalties and interest charges owed by individuals and businesses.

1.7 As at 31 March 2023, total HMRC receivables amounted to £192.6 billion – 23.7% of revenue (March 2022: £173.8 billion, 23.8%). This balance consisted of:

- **receivables** – £60.0 billion (31.2%) due from taxpayers but not yet received. This is an increase in the value and proportion outstanding since 31 March 2022 (£51.2 billion, 29.5%). HMRC's analysis indicates there were large increases in the volume of new debt, primarily caused by compliant taxpayers struggling to meet their payment obligations, together with an increase in the aged profile of older debt; and
- **accrued revenue receivables** – an estimated £132.6 billion (68.8%) (31 March 2022: £122.6 billion, 70.5%) of taxes not yet due from taxpayers but related to 2022-23 revenues where a tax return has not been received from the taxpayer by the end of the reporting period.[3] Two-thirds (£6.8 billion) of the £10.0 billion increase in the accrued revenue receivables was attributable to Income Tax, mainly from Self Assessment, due to the growth in income from self-employment and dividends.

1.8 Of the £132.6 billion accrued revenue receivable balance, 92% comprises taxpayer liabilities for Income Tax (£48.7 billion), VAT (£46.2 billion), NICs (£17.4 billion) and Corporation Tax (£10.1 billion). For Income Tax (Self Assessment) and Corporation Tax in particular, HMRC's estimates of the amount of tax that will be due, once the relevant tax returns have been received and the tax liabilities assessed, are subject to an inherent degree of estimation, as explained in Note 4.2 of the Trust Statement.

1.9 We review HMRC's models and assumptions used to calculate the accrued revenue receivables estimates as part of our financial audit of HMRC. As a result of that work, we are satisfied that HMRC's estimates are reasonable based on the data available to HMRC at the time.

3 As HMRC explains in the Trust Statement, accrued revenue receivable represents amounts of taxes and duties where the taxable event has occurred but the return has not been received from the taxpayer by the end of the reporting period. For taxes where HMRC has received returns since the end of the reporting period, it used this information to support its valuation of accrued revenue receivable. For those taxes where HMRC is yet to receive taxpayer returns, principally Income Tax (Self Assessment) and Corporation Tax, HMRC has estimated accrued revenue receivable.

Tax debt

1.10 As at 31 March 2023, HMRC's tax debt balance was £43.9 billion, £4.7 billion (11.9%) more than the tax debt reported at 31 March 2022 (**Figure 3**).[4] As a proportion of annual revenues, tax debt remained at 5.4%. During 2022-23, the number of taxpayers in debt increased from 7.7 million to 8.4 million. The tax debt balance at 31 March 2023 is lower than the £68.5 billion reported at the height of the pandemic, largely due to the government's Self Assessment and VAT deferral schemes having ended in January and March 2021 respectively and the majority of those debts having now been repaid.

1.11 The tax debt balance remains higher than reported historically. For instance, in the five years between 2015-16 and 2019-20, tax debt was typically around £14 billion. This is partly due to the related increase in tax revenues, but also reflects the impact of the current economic conditions on taxpayer finances, meaning more taxpayers are getting into debt than HMRC can manage and debts are getting older as taxpayers struggle to pay them. HMRC's research suggests taxpayers may be prioritising other debts before paying their debts to HMRC. In a letter to the Committee of Public Accounts in January 2023, HMRC said it expects the debt balance to be at an elevated level into 2023-24.

1.12 The composition of HMRC's tax debt is changing. In 2022-23 HMRC cleared 21.0 million tax debts. The number of new tax debts in the year (25.8 million) increased 7% from 2021-22 and was more than one-fifth higher than the number of debts cleared. HMRC's analysis indicates a large number of taxpayers are getting into debt for the first time as they face temporary financial difficulties. Older debts are also increasing, with a 25% increase in the number of debts older than 12 months. As debts get older, there is an increased risk that HMRC will not be able to recover the debt.

1.13 HMRC considers that the level of 'managed debt' is a good indicator of its debt management performance. Managed debt is mostly debt that is within a time to pay arrangement, but also includes debt that HMRC considers has reached the end of its processes for pursuing and may be considered for remission. As at 31 March 2023, managed tax debt comprised £7.4 billion (16.9% of tax debt), compared with £6.8 billion (17.5%) at 31 March 2022. The average duration of agreed time to pay arrangements has increased from under 10 months in 2019-20 to more than 21 months in 2021-22 and 2022-23.

4 In addition to tax debt, HMRC was owed £2.1 billion in tax credits debt at 31 March 2023, down from £2.4 billion at 31 March 2022.

Figure 3
HM Revenue & Customs' (HMRC's) tax debt and managed tax debt balance, June 2019 to March 2023

Between 31 March 2022 and 31 March 2023, HMRC's tax debt balance increased from £39.2 billion to £43.9 billion

	Jun 2019	Sep 2019	Dec 2019	Mar 2020	Jun 2020	Sep 2020	Dec 2020	Mar 2021	Jun 2021	Sep 2021	Dec 2021	Mar 2022	Jun 2022	Sep 2022	Dec 2022	Mar 2023
Total tax debt balance (£bn)	14.9	15.4	15.5	19.0	57.6	66.0	62.1	54.5	47.4	41.6	37.0	39.2	39.7	44.6	45.8	43.9
(Of which) managed tax debt balance (£bn)	2.1	2.0	1.9	2.0	1.5	3.3	3.1	14.7	16.4	11.1	5.9	6.8	7.0	8.4	7.2	7.4

Notes

1 Data are as at the end of the month.

2 Managed tax debt is tax debt which is within a time to pay arrangement or, since 2020-21, tax debt which HMRC considers has reached the end of its processes for pursuing and may be considered for remission. It is part of the total tax debt balance.

Source: National Audit Office analysis of HM Revenue & Customs data

1.14 HMRC has taken steps to increase its capacity for managing debt. The number of staff in its debt management function increased from 4,289 in 2021-22 to 4,720 in 2022-23. In the Spring Budget 2023, HM Treasury gave HMRC an additional £47.2 million to improve its ability to manage tax debts, including increasing its capacity through debt collection agencies and making it easier for taxpayers to service their own debt arrangements online, for instance, by setting up time to pay arrangements. HMRC expects this investment to help it recover an additional £1.4 billion in tax debt between 2022-23 and 2027-28. HMRC spent £34.0 million in 2022-23 on debt collection agencies to recover tax debt, compared with £20.6 million in 2021-22, and since September 2022 it has entered a new contract that allows it to place more debt with agencies for the same level of investment. In 2022-23, private agencies recovered £813 million in tax debt, an increase from £455 million in 2021-22.

1.15 In a letter to the Committee of Public Accounts in January 2023, HMRC explained its new strategy for managing tax debt. It said its aim is to support customers in short-term financial difficulty to manage their way out of debt quickly and sustainably, while taking enforcement action for taxpayers who can, but choose not to pay. HMRC has expanded its online services to make it easier for taxpayers to manage their debt repayments and has developed six customer profiles so it can tailor its approach to taxpayers in debt. It is using funding from the Spring Budget 2023 to purchase data from credit reference agencies for 2023-24 and 2024-25 to improve the accuracy of its taxpayer segmentation. HMRC told us it expects the long-term impact of its strategy to include taxpayers clearing their debts more quickly and the proportion of older debts reducing.

Impairments

1.16 The receivables balance of £60.0 billion is money that taxpayers were liable for at the end of the financial year but they had not paid. There is a risk that some of the receivables balance will not be collected or may prove not to be due. HMRC estimates the amounts that may not be recovered from taxpayers – for instance where the taxpayer is experiencing financial difficulty – and processes a reduction to the receivables balance in the accounts to reflect this, known as an 'impairment'. HMRC has estimated that it may not be able to collect £19.2 billion (2021-22: £14.4 billion) of these receivables. The impairment as a proportion of receivables increased from 28.1% in 2021-22 to 32.0% in 2022-23. HMRC attributes this to the uncertain economic conditions increasing the volume of older debts, which HMRC has a lower chance of recovering. HMRC's approach to calculating the impairment is set out in Note 4.3 of the Trust Statement.

Losses

1.17 In certain cases, HMRC stops debt collection activity and incurs a 'revenue loss' – such losses are likely to relate to amounts due in earlier financial years. Revenue losses increased 56% between 2021-22 and 2022-23, from £2.4 billion to £3.8 billion, with nearly half (£1.8 billion) relating to VAT debt. There are two forms of revenue losses: write-offs of £3.2 billion during 2022-23 (£1.9 billion in 2021-22) and remissions of £0.6 billion in 2022-23 (£0.5 billion in 2021-22). Write-offs are where debts are irrecoverable because there is no practical means of pursuing the liability. Remissions are where HMRC decides not to pursue the liability on value-for-money or hardship grounds. Revenue losses are mainly driven by individual and corporate insolvencies. Corporate insolvencies in England and Wales increased 36% in 2022-23 as government support to companies during the pandemic ended and the adverse impact the current economic conditions have had on some companies.

Provisions and contingent liabilities

1.18 HMRC recognises a provision in the Trust Statement where it considers that it is probable that it will need to repay taxes already received in the current or previous financial years, in accordance with accounting standards. HMRC has identified two categories of such probable repayments:

- **Legal claims,** where taxpayers have disputed the interpretation of legislation through the courts and want the tax payable to be reassessed. The outcome depends on the court ruling. In 2022-23, HMRC repaid £0.3 billion to taxpayers in respect of legal provisions (2021-22: £0.5 billion). As at 31 March 2023, HMRC expects it will have to repay £3.0 billion (2021-22: £3.2 billion). Claims in respect of Corporation Tax account for 70% of the overall provision. HMRC also separately discloses contingent liabilities for legal claims, where it considers that it is possible, rather than probable, that it will be required to repay tax. Contingent liabilities were £4.1 billion as at 31 March 2023 (2021-22: £3.2 billion).

- **Oil and gas field decommissioning costs,** where companies decommissioning oil and gas infrastructure in the North Sea are entitled to recover tax previously paid in relation to profits from those oil and gas fields. As at 31 March 2023, HMRC estimates that it will have to repay £4.5 billion of tax in relation to oil and gas decommissioning (2021-22: £10.4 billion), based on an estimate of the decommissioning costs they will incur in future periods. The decrease in the 2022-23 estimate relates to sustained increases in oil prices and lower decommissioning costs, both of which are expected to continue for the foreseeable future. The impact of this on oil and gas company profitability is expected to result in less tax being repaid to those companies by HMRC.

Tax compliance

Tax gap

1.19 HMRC defines the tax gap as "the difference between the amount of tax that should, in theory, be paid to HMRC, and what is actually paid".[5] The tax gap occurs for a number of reasons. Some taxpayers make mistakes, others choose not to comply, and some cannot pay because of insolvency. In other cases, taxpayers interpret tax rules differently from HMRC, which can affect the amount of tax they pay, or construct artificial arrangements to avoid tax. The tax gap can also be affected by factors such as the performance of the economy, demographic changes and the perceived fairness of tax policy. HMRC publishes its tax gap estimates each year. The accounting framework under which HMRC produces its accounts means that the tax gap is not included in its annual Trust Statement.

1.20 On 22 June 2023 HMRC published its latest estimates for the tax gap. It has estimated that the tax gap for 2021-22 – the latest year for which data are available – was 4.8% of total theoretical tax liabilities, or £35.8 billion against total theoretical liabilities of £739.3 billion. It also revised downward its estimate of the tax gap for 2020-21 to 4.8% of total theoretical tax liabilities (£30.8 billion) from the previously reported 5.1% of total theoretical tax liabilities (£32.2 billion). These two years are notable in that they relate to the main time period of the COVID-19 pandemic.

1.21 HMRC's estimate of total theoretical liabilities is difficult to reconcile with total tax revenues for 2021-22 of £731.1 billion, which is just £8.2 billion less than its estimate of total theoretical liabilities. It defines theoretical tax liabilities as the tax gap plus the amount of tax it actually receives. HMRC told us that the relationship between theoretical liabilities and receipts is also complex, and some tax gap models may use tax liabilities instead of actual receipts. In HMRC's *Measuring tax gaps 2023 edition*, it has adjusted the VAT receipts figures used to estimate the VAT gap to account for the impact of the VAT deferred between March 2020 and June 2020 under the VAT payment deferral schemes.

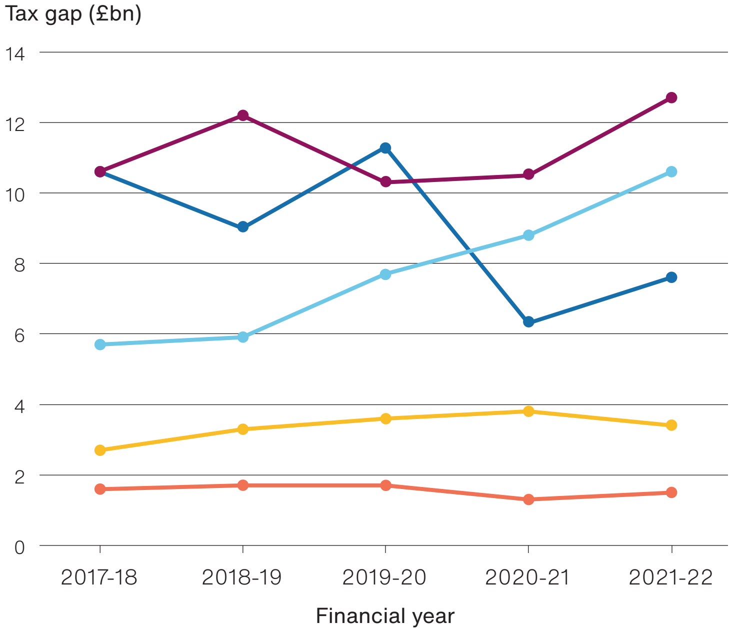
1.22 The tax gap split by different types of tax is shown in **Figure 4**. HMRC revised down its VAT tax gap estimate for 2020-21 due to updated data on consumer expenditure from the Office for National Statistics. In contrast, it revised up its estimate of the Corporation Tax gap due to additional information from random enquiry programmes on levels of tax compliance among small businesses.
For 2021-22 HMRC estimates that the tax gap for personal income taxes increased the most in monetary terms, up £2.2 billion from 2020-21. This was driven by an increase in the tax gap for Self Assessment, which, as a percentage of theoretical tax liabilities, increased from 10.4% in 2020-21 to 11.2% in 2021-22. By customer group, small businesses make up 56% of the tax gap, up from 40% in 2017-18.

5 HMRC's *Measuring tax gaps 2023 edition* is available at: www.gov.uk/government/statistics/measuring-tax-gaps

Figure 4

HM Revenue & Customs' (HMRC's) estimates of tax gap by type of tax, 2017-18 to 2021-22

HMRC's estimates indicate that the tax gap remained at 4.8% of total theoretical tax liabilities, with personal income taxes remaining the largest component



	2017-18	2018-19	2019-20	2020-21	2021-22
Personal income taxes (Income Tax, National Insurance Contributions, Capital Gains Tax) (£bn)	10.6	12.2	10.3	10.5	12.7
Corporation Tax (£bn)	5.7	5.9	7.7	8.8	10.6
Value Added Tax (VAT) (£bn)	10.6	9.0	11.3	6.3	7.6
Excise duty (£bn)	2.7	3.3	3.6	3.8	3.4
Other taxes (£bn)	1.6	1.7	1.7	1.3	1.5
Total tax gap (£bn)	**31.2**	**32.1**	**34.5**	**30.8**	**35.8**
Total tax gap as a percentage of total theoretical liabilities (%)	5.0	4.9	5.2	4.8	4.8

Notes

1 The tax gap is HMRC's estimate of the difference between the total taxes theoretically owed and those actually paid.

2 Total theoretical liabilities are HMRC's estimate of the total amount of tax theoretically owed. The tax gap is generally presented as a proportion of this.

3 The figures presented in this table are in nominal terms.

4 'Other taxes' include stamp duties, Inheritance Tax, Landfill Tax and other taxes, levies and duties.

Source: National Audit Office presentation of HM Revenue & Customs data

1.23 The tax revenue HMRC generates from its tax compliance work (compliance yield) should, in theory, either reduce the tax gap or stop it from increasing. During the pandemic, however, in the years 2020-21 and 2021-22, compliance yield as a proportion of total theoretical tax liabilities declined whereas HMRC's estimates indicate the size of the tax gap also reduced (**Figure 5**). HMRC calculates the tax gap and compliance yield in different ways, based on different time periods, making precise comparisons difficult.

Compliance activities and compliance yield

1.24 Compliance activities can take many different forms. These can include disrupting organised criminal groups or tackling the use of tax avoidance schemes, as well as measures to promote compliance and prevent non-compliance, such as guidance to taxpayers and changes to administrative or filing processes, for instance through HMRC's Making Tax Digital programme.

1.25 The aim of HMRC's compliance work is for everyone to pay the right tax that is legally due, no matter who they are. It considers that its role is to help people to pay the right tax through well-designed systems (preventing non-compliance), to provide education (promoting compliance) and to step in when tax is at risk of not being paid (responding to non-compliance). When taxpayers are not compliant, HMRC's aim is to work with them to get them back on the right track. It will investigate where it believes a business or individual is trying to cheat the tax system. Its compliance strategy is to focus increasingly on preventing non-compliance, which it considers more cost-effective and better for taxpayers if it helps them to get their tax right the first time.

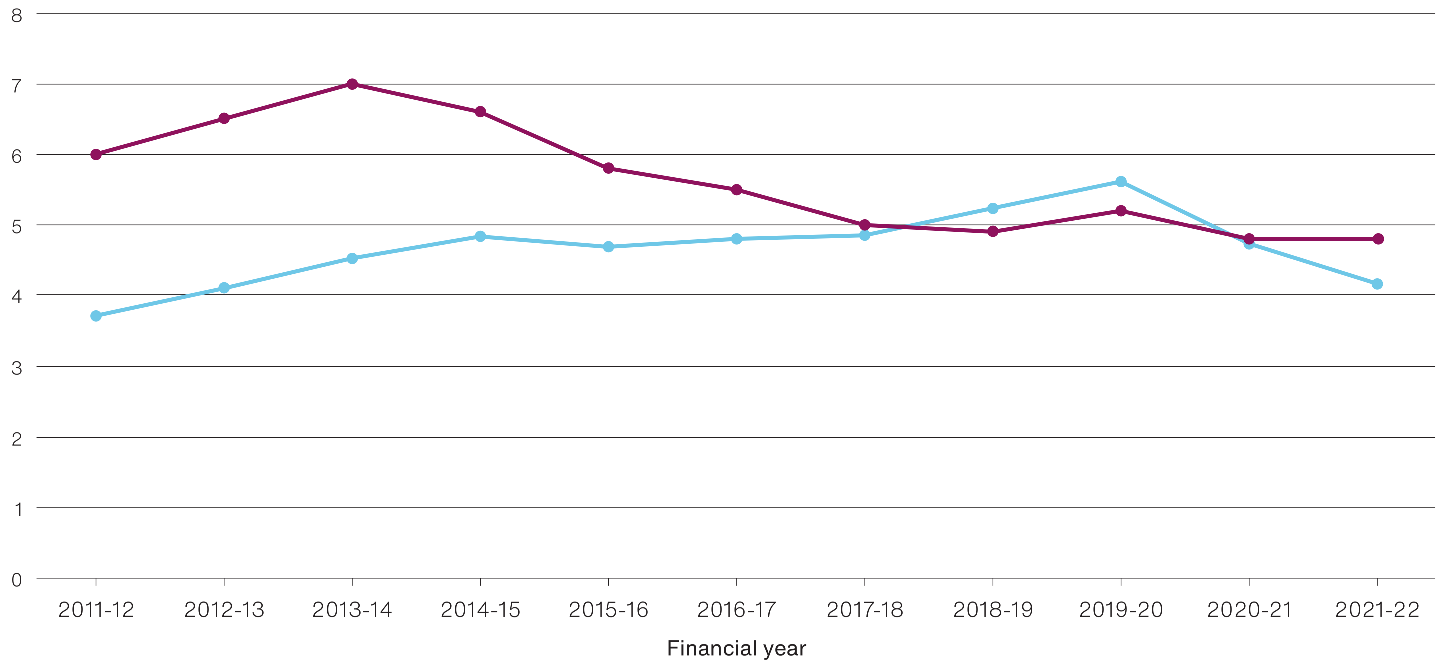
1.26 HMRC measures the effectiveness of its compliance and enforcement activities through compliance yield – that is, the estimate of the additional revenue that HMRC considers it generated, and the revenue losses it prevented. Each year, it agrees a target with HM Treasury and ministers for compliance yield, set at a level that will maintain the tax gap at its current level. Total compliance yield in 2022-23 was £34 billion, a 10% increase compared with 2021-22 (£30.8 billion), and higher than the average over the past five years (2018-19 to 2022-23) of £33.2 billion.[6] Compliance yield for 2022-23 was below the target of £36 billion. HMRC explained that compliance yield is affected by interventions in previous years and that it is still seeing the effects of reduced compliance activity during the COVID-19 pandemic in its 2022-23 performance.

6 The average over the past five years includes two unusual and exceptionally large settlements in 2018-19 and 2019-20.

Figure 5

Compliance yield and tax gap estimates as a proportion of total theoretical tax liabilities, 2011-12 to 2021-22

In 2021-22 the tax gap remained stable despite a decrease in compliance yield



	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22
Tax gap (%)	6.0	6.5	7.0	6.6	5.8	5.5	5.0	4.9	5.2	4.8	4.8
Compliance yield (%)	3.7	4.1	4.5	4.8	4.7	4.8	4.9	5.2	5.6	4.7	4.2

Notes

1 Compliance yield is defined by HM Revenue & Customs (HMRC) as the revenue collected and protected that would otherwise have been lost to the Exchequer if not for its interventions.

2 The tax gap is HMRC's estimate of the difference between the total taxes theoretically owed and those actually paid.

3 Total theoretical liabilities are HMRC's estimate of the total amount of tax theoretically owed. The tax gap is generally presented as a proportion of this.

4 HMRC's tax gap estimates are not yet available for 2022-23.

Source: National Audit Office analysis of HM Revenue & Customs data

1.27 Compliance yield increased in 2022-23 for three of the five categories that HMRC uses to analyse its compliance performance and decreased for the other two (**Figure 6** on pages R25 and R26). HMRC explained that the changes were due to a variety of factors, including more compliance checks in 2022-23 following reductions in the previous two years due to restrictions on compliance activity and the temporary redeployment of staff to support other parts of HMRC during the pandemic, as well as HMRC's strategy to move more of its compliance activity 'upstream', encouraging voluntary compliance and preventing non-compliance before it happens. HMRC has set an aspiration that upstream work will contribute at least 25% of total compliance yield by 2024-25. HMRC achieved this in 2022-23 but acknowledges it needs to exploit new opportunities, including through legislative changes, to maintain this proportion.

1.28 In May 2023 the Committee of Public Accounts expressed concern that any compliance yield targets stated in cash terms will not be sufficiently stretching during a period of high inflation and recommended that HMRC set a target for compliance yield as a percentage of tax revenues.[7] HMRC explained its compliance yield target takes into account growth in receipts, inflation and changes in the wider economy. In the five years before the pandemic, HMRC's compliance yield was on average 5.2% of total revenues. The Committee said that HMRC will need compliance yield to exceed this historical performance of 5.2% if it is to catch up with the impact of the pandemic. HMRC's compliance yield in 2022-23 equated to 4.2% of total revenues, the same as in 2021-22 (**Figure 7** on page R27).

1.29 In 2022-23, HMRC opened 299,000 compliance cases (2021-22: 265,000) and closed 280,000 (2021-22: 256,000). This represents a reduction of 63,000 (17%) cases opened and 71,000 (20%) cases closed compared with 2019-20 before the pandemic. HMRC says this partly reflects its strategy to focus increasingly on upstream efforts to ensure taxpayers comply in the first place, and to prioritise larger and higher-impact cases. As the nature of cases opened and closed can vary in complexity and duration, HMRC's mix of compliance activity will change year on year and so it considers compliance yield rather than levels of activity to be the key measure of compliance performance.

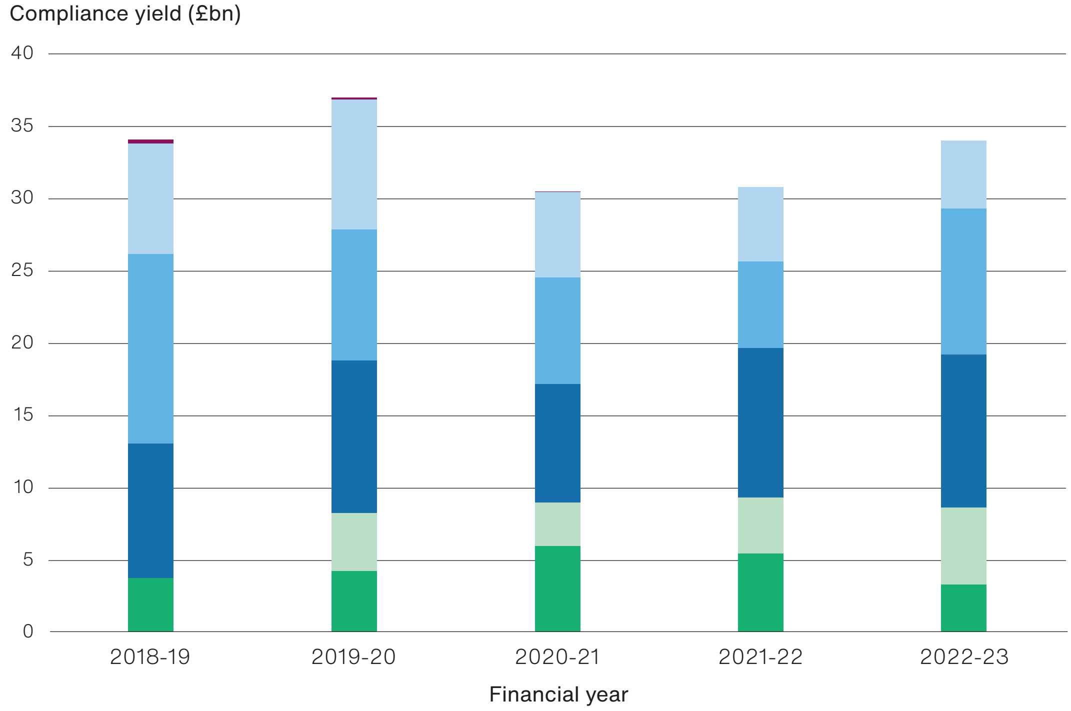
1.30 HMRC's criminal investigations resulted in 240 prosecutions in 2022-23 (2021-22: 236), lower than the 691 prosecutions in 2019-20. HMRC told us that this decrease is a result of delays in the criminal justice system as well as its strategy to increasingly focus its criminal investigations on the most serious cases. In May 2023, the Committee of Public Accounts expressed concern that, without sufficient numbers of prosecutions, HMRC cannot demonstrate a credible deterrent effect from its compliance work.

7 Committee of Public Accounts, *Managing tax compliance following the pandemic*, Session 2022-23, HC 739, May 2023.

Figure 6

Compliance yield performance by category, 2018-19 to 2022-23

Compliance yield reported by HM Revenue & Customs (HMRC) increased by 10.4% in 2022-23



	2018-19	2019-20	2020-21	2021-22	2022-23
Upstream product and process yield (£bn)	3.7	4.2	5.9	5.4	3.3
Upstream operational yield (£bn)	–	4.1	3.1	3.9	5.3
Revenue loss prevented (£bn)	9.3	10.6	8.2	10.3	10.6
Cash expected (£bn)	13.1	9.0	7.4	6.0	10.1
Future revenue benefit (£bn)	7.6	9.0	5.9	5.2	4.7
Accelerated payments (£bn)	0.3	0.1	0.0	–	–
Total compliance yield (£bn)	**34.1**	**36.9**	**30.5**	**30.8**	**34.0**
Percentage change from previous year (%)	–	8.4	-17.6	1.1	10.4

Figure 6 *continued*
Compliance yield performance by category, 2018-19 to 2022-23

Notes
1 Compliance yield is defined by HMRC as the revenue collected and protected that would otherwise have been lost to the Exchequer if not for its interventions.
2 HMRC's definition of the compliance categories:
- Accelerated payments – estimate of the amount that users of avoidance schemes have paid to HMRC upfront while their dispute is being resolved, as well as an estimate of the behavioural change that this policy has generated. Since 2021-22, HMRC has no longer included yield from accelerated payments as a separate category and has instead incorporated it within cash expected and upstream product and process yield.
- Future revenue benefit – estimate of the effect of HMRC's compliance work on taxpayers' future behaviour.
- Upstream operational yield – estimate of the impact of HMRC's operational activities undertaken to promote compliance and prevent non-compliance before it occurs. In 2019-20, HMRC started reporting upstream operational yield as a distinct category as it become a more significant proportion of total yield. It had previously been included as part of 'cash expected'.
- Upstream product and process yield – estimate of the net tax receipts from legislative changes to close tax loopholes, and changes to HMRC's processes that reduce opportunities to avoid or evade tax.
- Revenue loss prevented – estimate of the tax revenue HMRC has prevented from being lost to the Exchequer (for example, by stopping fraudulent repayment claims and disrupting criminal activity).
- Cash expected – an estimate of the amount of additional revenue paid when HMRC identified past non-compliance.

3 Totals for 2019-20 and 2020-21 do not sum due to rounding.
4 The figures include two unusual and exceptionally large settlements in 2018-19 and 2019-20, which were spread across revenue loss prevented and future revenue benefit.
5 The values presented in this figure are in nominal terms.

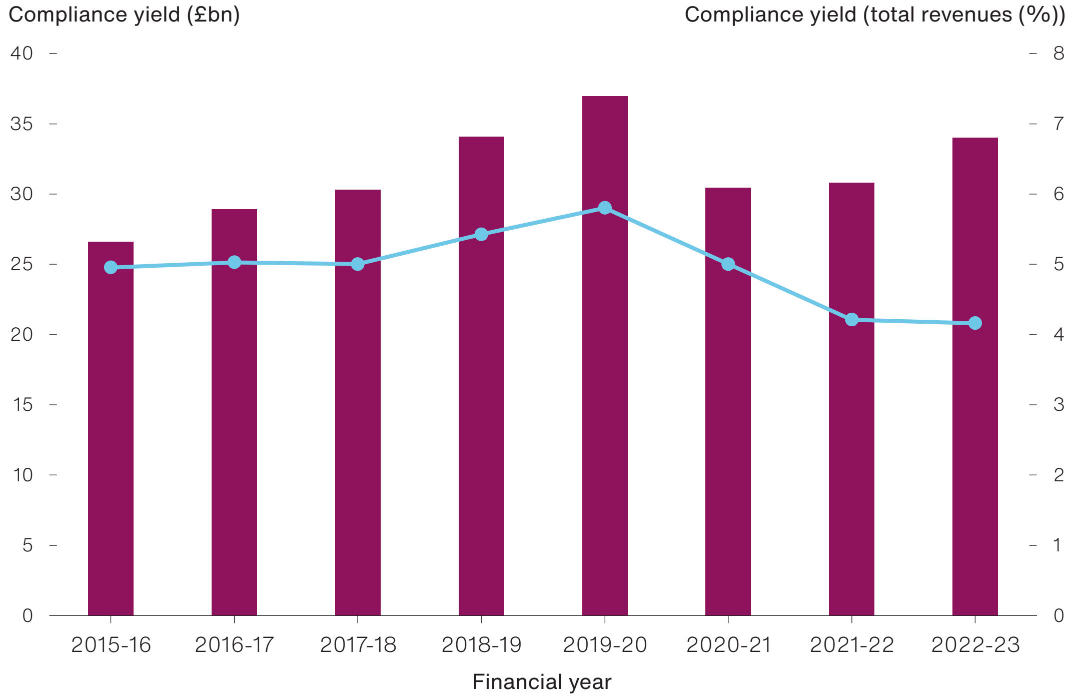
Source: National Audit Office presentation of HM Revenue & Customs data

1.31 HMRC's planned compliance activities are influenced by a number of factors, including compliance yield targets, the relative size of the estimated tax gap in a particular area, and reputational factors and affordability within HMRC budgets. HMRC told us it prioritises its compliance resources in order to ensure sufficient coverage of each area of risk and to maintain levels of voluntary compliance. In 2022-23, HMRC increased its compliance workforce by 12%, from 25,442 to 28,526. In the 2022 Autumn Statement, the government committed an additional £79 million for additional HMRC capacity between 2023-24 and 2027-28 to tackle more cases of serious tax fraud and address tax compliance risks among wealthy taxpayers. HMRC expects this to yield an additional £725 million between 2023-24 and 2027-28.

Figure 7

Compliance yield compared with total revenues, 2015-16 to 2022-23

Compliance yield has fallen as a proportion of total revenues since the start of the COVID-19 pandemic at the end of 2019-20



	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23
Compliance yield (£bn)	26.6	28.9	30.3	34.1	36.9	30.5	30.8	34.0
Compliance yield (total revenues (%))	5.0	5.0	5.0	5.4	5.8	5.0	4.2	4.2

Notes

1 Compliance yield is defined by HM Revenue & Customs (HMRC) as the revenue collected and protected that would otherwise have been lost to the Exchequer if not for its interventions.

2 Values are in cash terms and have not been adjusted for inflation, to align with conventional reporting of tax revenues. To illustrate how compliance yield performance has changed over time, we have also included it as a proportion of total revenues on a secondary axis.

3 The figures include two unusual and exceptionally large settlements in 2018-19 and 2019-20.

Source: National Audit Office analysis of HM Revenue & Customs data

Error and fraud in the COVID-19 employment support schemes

1.32 The Comptroller and Auditor General qualified his regularity opinion on the 2020-21 and 2021-22 HMRC Resource Accounts due to the material levels of error and fraud present in the main COVID-19 employment support schemes, which comprise: the Coronavirus Job Retention Scheme (CJRS) and the Self-Employment Income Support Scheme (SEISS). The schemes ended in September 2021, so the 2022-23 accounts do not record any related expenditure. The estimated value and rate of error and fraud across the lifetime of the schemes was reported in the 2021-22 accounts as: CJRS £3.5 billion (5.0%) and SEISS £1.0 billion (3.6%).

1.33 In drawing the schemes to a close, HMRC has calculated a final estimate of the levels of error and fraud present in the schemes. These estimates reflect the results of further compliance activity undertaken since HMRC prepared the 2021-22 accounts, details of which are included in HMRC's 2022-23 Annual Report. HMRC's final estimates of error and fraud in respect of the schemes were: CJRS £3.5 billion (5.1%); SEISS £1.5 billion (5.2%) (**Figure 8**). The final estimate for error and fraud across both schemes is £5.0 billion (5.1%) in total, which is £0.5 billion (0.5 percentage points) more than reported in the 2021-22 Annual Report and Accounts.

1.34 The increase in overall error and fraud in the schemes relates mainly to higher levels of non-compliance identified from HMRC's sample testing of SEISS claims since the 2021-22 estimate was produced. HMRC considers that this is largely due to non-compliance with the 'reasonable belief' declaration which it introduced for tranches 4 and 5 of the SEISS scheme. HMRC estimates that this identified a further £615 million of error and fraud compared with its 2021-22 estimate for SEISS, although other causes of error and fraud were lower than HMRC had previously estimated.

1.35 Using additional funding from HM Treasury, HMRC set up a Taxpayer Protection Taskforce in April 2021 to identify and recover error and fraud in the COVID-19 support schemes. By the end of 2022-23, the Taskforce had recovered £520 million of error and fraud in addition to £536 million recovered before the Taskforce was in place. This is compared with HMRC's expectation that the Taskforce will recover between £525 million and £625 million across its lifetime, revised down from between £800 million and £1 billion due to lower levels of error and fraud on the schemes than HMRC anticipated.

1.36 Between March and September 2023, HMRC is shifting the activities of the Taskforce into its business-as-usual tax compliance function. HMRC says that this will help it consider all aspects of a customer's potential non-compliance issues when planning and prioritising its compliance activity. HMRC says it has already tackled the riskiest claims and will see diminishing returns from its compliance work. In 2022-23, HMRC estimates each full-time equivalent officer on the Taskforce returned £0.28 million in prevented or recovered error and fraud, compared with £1.15 million for business-as-usual tax compliance work in recent years.

Figure 8

HM Revenue & Customs' (HMRC's) final central estimate[1] of error and fraud in the main COVID-19 employment support schemes

HMRC has estimated there was £5.0 billion of error and fraud across the lifetime of the schemes

	Coronavirus Job Retention Scheme (CJRS)	Self-Employment Income Support Scheme (SEISS)	Total
Net cost (£bn)	69.2	28.1	**97.3**
HMRC's final central estimate of the cost of error and fraud (£bn)	3.5	1.5	**5.0**
HMRC's final central estimate of the rate of error and fraud (%)	5.1	5.2	**5.1**

Notes

1 HMRC also reports lower and upper estimates of error and fraud.

2 HMRC estimates the residual error and fraud within the schemes. Residual error and fraud is defined as the monetary value of error and fraud remaining after pre-payment checks but before the effects of post-payment compliance activity have been realised. HMRC's estimates of the cost of error and fraud is determined on the basis of gross expenditure less unprompted repayments and repayments related to disclosures. HMRC classify this as net cost.

3 HMRC's estimates of the likely levels of error and fraud in CJRS are based upon a combination of a mandatory random enquiry programme into a sample of claims, and insights from HMRC administrative data; internal and external surveys; pre-payment risking and verification checks; post-payment compliance data; and experience from error and fraud rates in other tax and benefit streams it administers. HMRC's estimates for SEISS are based upon modelling using a combination of a random enquiry programme into a sample of claims, data from 2020-21 and 2021-22 Self Assessment tax returns, insights from HMRC administrative data and post-payment compliance outputs. HMRC's estimates for both CJRS and SEISS remain subject to uncertainty.

Source: National Audit Office analysis of HM Revenue & Customs data

Customer service performance

1.37 This section considers HMRC's customer service performance in 2022-23 and the factors affecting it. It also sets out the latest developments in the measurement of its customer service performance. Taxpayers' satisfaction with HMRC's customer services fell further in 2022-23, continuing a trend seen since the pandemic. HMRC has improved performance on customer correspondence, although from a low base in 2021-22 and still below HMRC's expected standard. Taxpayers' satisfaction with HMRC's digital services remained broadly at 2021-22 levels.

1.38 In 2022-23, HMRC's customer service performance was adversely affected by IT performance problems, particularly towards the end of the 2022 calendar year. For example, between 1 and 5 December 2022, HMRC closed all of its telephone-based services due to poor call quality and the inability of advisers to access relevant information. Webchat was also unavailable at this time. HMRC estimates it would have handled approximately 99,000 calls from taxpayers during the period the telephone services were suspended.[8] In 2022-23, HMRC recorded 45 separate instances of significant disruption to its IT services, up from 25 in 2021-22.

Performance in 2022-23

1.39 In 2021-22, HMRC set out in its Outcome Delivery Plan five priority metrics it would use to monitor its customer service performance, aligned to its strategic objectives. They seek to measure how easy or hard it is for taxpayers to access services, and whether HMRC has helped taxpayers to resolve their queries. For 2022-23, HMRC has added two further priority metrics, on the percentage of customers who were able to resolve their issue ('Once and Done') and performance in clearing customer correspondence within 40 days.

1.40 HMRC published its customer service standards for 2022-23 having not been set any formal targets by HM Treasury for 2021-22 due to the uncertainty caused by the pandemic. HMRC did not meet any of the service standards it set for 2022-23 (**Figure 9**).

1.41 Customer correspondence performance improved compared with the previous year, although HMRC missed its service standard for responding to enquiries within 15 days or 40 days in all four quarters of 2022-23. HMRC reported receiving 10% more items of correspondence requiring a response in 2022-23 compared with 2021-22. HMRC's performance against its Net Easy service standard reduced compared to 2021-22, with performance deteriorating in every quarter in 2022-23, driven by reported problems with the telephone service. HMRC received 9% more calls in 2022-23 compared with 2021-22. Performance in the last quarter of 2022-23 was particularly low. HMRC told us that demand for its services during this period was higher than it had forecast.

1.42 While HMRC has introduced a new set of customer service measures, it has continued to report its performance against most of its long-standing measures, mainly response time. HMRC's reported data show that its performance has declined for all of these measures since 2018-19 except for customer service satisfaction for digital services. Performance declined in 2022-23 for all measures except for customer correspondence (**Figure 10** on page R32). In that time, average call waiting times have more than trebled, from 05:14 minutes to 16:24 minutes, with average wait times exceeding 20 minutes in the last quarter of 2022-23.

8 See HMRC letter to Treasury Committee, dated 7 December 2022, available at: https://committees.parliament.uk/publications/31952/documents/179382/default/

Figure 9

HM Revenue & Customs' (HMRC's) quarterly performance in 2022-23 for seven key customer service measures

HMRC did not meet any of the service standards it set for 2022-23

Measure	Service standard for 2022-23	April to June	July to September	October to December	January to March	2022-23 outturn	2021-22 outturn[1]
Net Easy – phone, webchat and digital services[2]	70.0	63.9 A	61.7 R	59.6 R	55.7 R	59.8 R	65.5
Telephony adviser attempts handled[3]	85.0%	73.0% R	77.2% A	74.6% R	61.9% R	71.1% R	77.3%
Webchat adviser attempts handled[4,5]	–	94.9%	95.3%	95.1%	93.8%	94.7%	92.9%
Customer correspondence (post and iForms) cleared within 15 working days of receipt[6]	80.0%	63.5% R	76.5% A	76.9% A	74.3% A	72.7% A	45.5%
Customer correspondence (post and iForms) cleared within 40 working days of receipt[6]	95.0%	86.1% A	90.0% A	90.8% A	90.8% A	89.4% A	64.1%
Customer satisfaction with phone, webchat and digital[7]	80.0%	81.1% G	80.1% G	79.2% A	77.3% A	79.2% A	82.0%
Once and Done[5,8]	–	85.7%	85.0%	84.5%	83.1%	84.4%	–

G Green – performance exceeded service standard

A Amber – performance below service standard but within 10%

R Red – performance more than 10% below service standard

Notes

1 Performance in 2021-22 was assessed against quarterly performance expectations rather than annual service standards so these have not been colour-coded here.

2 A survey conducted on telephone and digital services. The survey question is: "How easy was it to deal with us today?" The figures represent the total of positive responses minus the total of negative responses. The score that can be achieved ranges from -100 to 100.

3 The proportion of callers who go through to an adviser after hearing the automated messages and choosing the option to speak to an adviser.

4 The proportion of customers taking up a webchat offer that successfully got through to a webchat adviser.

5 Although HMRC identified webchat adviser attempts handled and Once and Done as priority metrics for 2022-23, it did not set corresponding targets.

6 Targeted post and iForms cleared within 15 and 40 days divided by total targeted post and iForms received. The day of receipt is counted as day zero.

7 A measure of the percentage of HMRC customers that responded that they were either 'satisfied' or 'very satisfied' with the service.

8 The proportion of customers who responded 'yes' when asked whether they were able to achieve what they needed to today. This measure is new for 2022-23.

Source: National Audit Office analysis of HM Revenue & Customs data

Figure 10
HM Revenue & Customs' (HMRC's) customer service performance, 2018-19 to 2022-23

All customer service performance measures have declined since 2018-19, with the exception of digital services performance, which has been broadly maintained during that time

Measure	2018-19 outturn	2019-20 outturn	2020-21 outturn	2021-22 outturn	2022-23 outturn	Performance trend
Average speed of answering calls to HMRC helplines (queue time in minutes)[1]	05:14	06:39	12:04	12:22	16:24	Declining
Customers waiting more than 10 minutes to speak to an adviser[1]	19.7%	29.9%	44.7%	46.3%	62.7%	Declining
Customer correspondence responded to within 15 days[2]	76.6%	70.3%	64.4%	45.5%	72.7%	Improved in 2022-23
Customer correspondence responded to within 40 days[2]	96.4%	88.0%	85.3%	64.1%	89.4%	Improved in 2022-23
Average time to handle new tax credits and Child Benefit claims and changes of circumstances – UK customers	12.0 days	13.2 days	11.2 days	15.4 days	14.2 days	Improved in 2022-23
Average time to handle new tax credits and Child Benefit claims and changes of circumstances – international customers	61.5 days	65.7 days	64.8 days	84.1 days	134.1 days	Declining
Customer satisfaction with digital services[3]	80.4%	81.6%	85.2%	83.4%	82.7%	Broadly maintained

Notes

1 Speed of answering calls covers the time customers spend in the queue waiting for an adviser. It excludes the time customers are in HMRC's automated telephony system before entering the queue. Historically, HMRC had been reporting against customer-facing telephone numbers (such as Tax Credits, Pay As You Earn and Self Assessment). From 2021-22, all HMRC helplines are included in the measure.

2 The customer correspondence measures cover post only for 2018-19 to 2020-21. Subsequent years cover post and iForms. iForms can be filled in and filed online.

3 Customer satisfaction for digital services is measured using an exit survey.

Source: National Audit Office analysis of HM Revenue & Customs data

HMRC's strategy for improving customer services

1.43 Key stakeholders, including the professional accountancy and tax bodies, wrote to the Chancellor of the Exchequer in March 2023 to raise concerns about the deterioration in HMRC's customer service performance and the impact this is having on taxpayers and their advisers.[9] They expressed particular concern about the severe delays, disruption and frustration when dealing with HMRC, and the impact these delays are having on cashflow and costs. In June 2023, the Adjudicator's Office reported concerns with HMRC's complaints procedures, with significant backlogs in parts of the business and increasing numbers of customers receiving little or no meaningful response from HMRC for long periods of time.[10]

1.44 HMRC wrote to the Committee of Public Accounts in May 2023 to set out its plan to improve customer service performance. HMRC said that its existing resources are insufficient to meet forecast demand for phone and post services in line with its expected levels of service. Instead, improving service levels will rely on HMRC enabling and encouraging taxpayers who can self-serve using digital services to do so in the first instance. In this way, HMRC hopes to free up its advisers to offer a better service for those taxpayers with more complex queries or that are unable to use online services.

1.45 HMRC's Making Tax Digital transformation programme, established in 2015-16, aims to modernise HMRC's separate IT systems for three business taxes, requiring business taxpayers to keep and submit digital tax records. The programme is part of the government's 10-year tax administration strategy to improve its resilience, effectiveness and support for taxpayers. However, we reported in June 2023 that HMRC's initial timeframe for the programme was unrealistic and has since faced repeated delays and rephasing, undermining its credibility and increasing its costs. We concluded that HMRC had not demonstrated the programme offers the best value for money for digitalising the tax system, with later business cases significantly underplaying the total cost to customers of making the change. We recommended that HMRC should develop a more robust business case and resolve key questions about the design of the programme.[11]

9 Association of Accounting Technicians, Association of Chartered Certified Accountants, Association of Taxation Technicians, Chartered Institute of Management Accountants, Chartered Institute of Payroll Professionals, Chartered Institute of Taxation, Institute of Chartered Accountants in England and Wales, Institute of Chartered Accountants of Scotland, Institute of Certified Bookkeepers, STEP, *Open letter on HMRC service levels ahead of the Spring Budget 2023,* 1 March 2023, available at: www.aat.org.uk/prod/s3fs-public/assets/Open-letter-HMRC-service-levels-ahead-of-Spring-Budget-2023.pdf

10 The Adjudicator's Office, *The Adjudicator's Office annual report 2023*, June 2023.

11 Comptroller and Auditor General, *Progress with Making Tax Digital*, Session 2022-23, HC 1319, National Audit Office, June 2023.

1.46 The Committee of Public Accounts has previously raised concern that HMRC's plans for digital services will not sustainably reduce demand for phone and post services.[12] HMRC acknowledges it will take some time to encourage customers to move to digital services and is planning to employ an average of 1,630 additional temporary staff each month between April and September 2023 to meet some of the demand on phone and post services during the transition. This follows a reduction of 834 (5%) in 2022-23 in the number of customer service staff not involved in debt management.

1.47 HMRC is closing down some of its customer services, either permanently or temporarily at less busy times of the year, to provide additional capacity elsewhere. In June 2023, HMRC closed its Self Assessment helpline for three months, with HMRC redirecting callers to use its digital services. HMRC says this will free up 350 advisers to respond to written correspondence and urgent calls on other helplines. In May 2023, HMRC closed its VAT registration helpline indefinitely.

12 Committee of Public Accounts, *HMRC performance in 2021–22*, Session 2022-23, HC 686, January 2023.

Part Two

Corporation Tax research and development reliefs

2.1 The Comptroller and Auditor General (C&AG) has qualified his opinion on the regularity of HM Revenue and Customs' (HMRC's) 2022-23 financial statements due to the material level of error and fraud in Corporation Tax research and development reliefs. This part of the report covers:

- an overview of HMRC's estimates for Corporation Tax research and development reliefs error and fraud; and
- developments in tackling error and fraud in the administration of these reliefs.

Corporation Tax research and development reliefs

2.2 HMRC is responsible for administering Corporation Tax research and development reliefs, which support companies that work on innovative projects in science and technology. The reliefs can be claimed by a range of companies that carry out research or seek to make an advance in the field. There are two separate schemes: the SME scheme for small- and medium-sized enterprises (SMEs), and the research and development expenditure credit (RDEC) scheme, mainly for larger companies. The SME scheme provides an extra deduction from companies' taxable income for research and development expenditure. Both schemes allow loss-making companies to receive a tax credit paid in cash by HMRC.

2.3 HMRC operates both schemes as part of administering the Corporation Tax system, the revenues from which HMRC reports in its Trust Statement. HMRC's Resource Accounts report expenditure on the schemes because they often result in cash payments (expenditure) unlike most other types of tax relief.

2.4 Note 5.1.4 to the Resource Accounts records Corporation Tax research and development reliefs expenditure of £10.2 billion in 2022-23 (£9.5 billion in 2021-22). Of this, £3.7 billion (£3.6 billion in 2021-22) relates to the RDEC scheme and £6.5 billion (£5.9 billion in 2021-22) to the SME scheme.

Qualification of the C&AG's audit opinion on the regularity of Corporation Tax research and development reliefs

2.5 The Corporation Tax Act 2009 specifies the eligibility criteria for research and development reliefs that companies can claim. Where error and fraud results in HMRC overpaying or underpaying Corporation Tax research and development reliefs to claimants who are either not entitled to these reliefs or are not paid the correct amount according to the legislation, the transactions do not conform with Parliament's intention and are irregular.

2.6 HMRC's latest estimate for 2022-23 indicates that the level of error and fraud present within Corporation Tax research and development reliefs was £1.1 billion or 13.3% of related expenditure in 2022-23 (excluding adjustments relating to earlier periods) (**Figure 11**). HMRC says this estimate should be viewed as illustrative only, based on a revised estimate of error and fraud in 2020-21 using the results of a mandatory random enquiry programme (MREP), further details of which are set out in paragraphs 2.10 to 2.14. Prior to this, HMRC estimated error and fraud using a different methodology that produced much lower estimates of error and fraud. Its most recent estimate prior to applying the MREP was £469 million or 4.9% in 2021-22.

2.7 Of the £1.1 billion of error and fraud that HMRC has estimated for 2022-23, £1.0 billion relates to the SME scheme (19.5% of SME expenditure) and £48 million relates to the RDEC scheme (1.7% of RDEC expenditure). HMRC's estimate for 2022-23 includes an assumption that recent compliance interventions will have reduced error and fraud by £250 million. It will not know the actual impact of these interventions until it has completed and evaluated its random enquiries on 2022-23 returns from claimants for that year.

2.8 The current estimates present a more realistic assessment of the underlying level of error and fraud that has always been present in the schemes. Now that HMRC has a better understanding of the extent to which the schemes are being abused, it will need to consider: whether the scale and focus of its current compliance arrangements are adequate; and the value-for-money case of inspecting more claims made prior to the period covered by its current estimates.

2.9 In the C&AG's view, the level of error and fraud in Corporation Tax research and development reliefs remains material by reference to the related expenditure, and he has qualified his audit opinion on that basis.

Figure 11

Estimated value and rate of error and fraud in Small- and Medium-sized Enterprise (SME) and Research and Development Expenditure Credit (RDEC) relief schemes, 2019-20 to 2022-23

The introduction of HM Revenue & Customs' (HMRC's) mandatory random enquiry programme (MREP) has revealed far higher levels of error and fraud than previously detected, mostly within the SME scheme, for which HMRC has estimated an error and fraud rate of 19.5% in 2022-23

		HMRC's previously reported estimates, calculated using its previous methodology[2]			Estimates based on the results of HMRC's MREP[3]	
		2019-20	2020-21	2021-22	2020-21	2022-23
Value of error and fraud (£mn)	SME scheme	271	303	430	1,038	1,003
	RDEC scheme	40	33	39	90	48
	Overall	**311**	**336**	**469**	**1,127**	**1,051**
Rate of error and fraud (%)	SME scheme	5.6	5.5	7.3	24.4	19.5
	RDEC scheme	1.0	0.9	1.1	3.6	1.7
	Overall	**3.6**	**3.6**	**4.9**	**16.7**	**13.3**

Notes

1 The rate of error and fraud in the schemes is the value of error and fraud as a percentage of total expenditure in the schemes.

2 HMRC has previously reported error and fraud on the schemes based on an analysis of compliance case reviews. This gave HMRC estimates up to and including 2021-22.

3 HMRC has since changed its methodology and its estimates now use the results of an MREP. Its revised estimate for 2020-21 is based on an MREP covering claims filed in 2020-21, relating to expenditure incurred by claimants in 2018-19 and 2019-20. HMRC has also produced an estimate for 2022-23 based on these same MREP results and an assumption about the impact of recent compliance interventions. It has not produced an estimate for 2021-22 based on the MREP results.

Source: National Audit Office analysis of HM Revenue & Customs data

Estimated level of error and fraud in Corporation Tax research and development reliefs

2.10 The C&AG has qualified his regularity opinion on Corporation Tax research and development reliefs every year since 2019-20, the first year HMRC produced an estimate of error and fraud in those reliefs. The factors that informed the C&AG's risk assessment and request that HMRC produces an estimate remain relevant and included:

- HMRC's own assessment through its 'Strategic Picture of Risk', which highlighted a significant increase in the level of expenditure on these schemes that may be at risk of abuse;
- the significant growth in expenditure under the schemes in recent years, which has continued into 2022-23; and
- an increase in public reporting of instances of abuse of these schemes, including through unregulated agents.

2.11 Between 2019-20 and 2021-22, HMRC based its estimate of error and fraud on an analysis of compliance case reviews where it had assessed the claims as being at risk of error or fraud, together with a series of assumptions, including that unreviewed cases have a lower rate of error and fraud. We have previously reported that, while these estimates were sufficient to demonstrate that the levels of error and fraud present in the schemes were material to the accounts, they were limited by the quality and availability of data on unreviewed cases that meant the actual level of error and fraud could be significantly different. This is borne out in the significantly higher levels of error and fraud reported in HMRC's current estimates.

2.12 In response to our recommendations from previous audits, HMRC's current estimates of error and fraud were calculated using the results of a Mandatory Random Enquiry Programme (MREP) for the first time. This involved inspection of a random sample of claims filed in 2020-21, relating to expenditure incurred by claimants in 2018-19 and 2019-20. These were the most recent claims available to HMRC at the time it commenced its work.

2.13 In addition to its 2022-23 estimate, HMRC has also produced a revised estimate for 2020-21, which indicates that error and fraud in Corporation Tax research and development reliefs was £1.1 billion or 16.7% of related expenditure; £1.0 billion of this relates to the SME scheme. Given the two-year lag between claimants incurring qualifying expenditure and submitting a return to HMRC and the time needed to open and close its random enquiries, it considers that applying the results from its random enquiry programme to 2020-21 expenditure produces the most statistically robust estimate of error and fraud. HMRC estimates that in 2020-21, error and fraud in Corporation Tax research and development reliefs could have been as high as £1.6 billion (23.2%) or as low as £0.9 billion (13.0%). Its central estimate for error and fraud on the SME scheme was 24.4%, which is among the highest reported across all government spending programmes, including those administered in response to the pandemic.

2.14 The implementation of an MREP represents good practice in the measurement of error and fraud and is a welcome development. The key features of HMRC's approach to its estimates included that:

- HMRC's compliance team selected 500 SME scheme claims filed in 2020-21. Of these, HMRC had closed 484 investigations at the time it produced the estimate. HMRC estimated the yield from the remaining 16 open cases and included this in its overall estimate;
- HMRC evaluated the error and fraud identified from review of the sampled claims to estimate an error and fraud rate and value for 2020-21;
- HMRC applied a 'non-detection multiplier' to the results to estimate any error or fraud that caseworkers may have missed during their reviews; and
- HMRC applied the error and fraud rates identified through its MREP to 2022-23 expenditure in calculating the value of error and fraud for 2022-23. It reduced this amount by £250 million to reflect its estimate of the impact compliance interventions it has introduced since 2020-21 will have had on error and fraud in 2022-23.

2.15 HMRC chose not to undertake an MREP in respect of large business claims under the RDEC scheme. HMRC considered this was unnecessary due to the historically lower levels of error and fraud it has identified for the scheme and the involvement of dedicated customer compliance managers who work with large businesses eligible for RDEC reliefs. HMRC's estimate of error and fraud by large companies in the RDEC scheme is, therefore, based substantially on detailed Business Risk Reviews and risk assessments of large business claims, similar to the approach in previous years. The increase in error and fraud in the RDEC scheme is driven by SMEs claiming RDEC where eligible.

2.16 The key findings from our review of HMRC's estimates and the areas we have identified that could improve HMRC's approach in future years include that:

- based on our audit work, we are satisfied that HMRC's approach to the SME scheme is reasonable and provides a more realistic assessment of the level of error and fraud present in the schemes than the approach in previous years;
- of the 484 claims that HMRC reviewed, 244 (50%) were found to include an element of non-compliance, where some or all of the claim was for expenditure that did not meet the qualifying criteria;
- more than half (32) of the 60 cases that we sampled related to claims for research and development in respect of information technology. In some instances where caseworkers considered a claim was sufficiently technically complex to evaluate against the eligibility criteria, they referred the case to internal experts within HMRC's Chief Digital Information Officer (CDIO) function for review. This appears to have been at the discretion of individual caseworkers because HMRC's guidance did not specify when they should consult. In one of the 60 cases we inspected, the caseworker recommended a referral to CDIO but this was not undertaken due to capacity issues. In another two cases, the caseworker felt they had sufficient knowledge not to refer the case to CDIO;
- in some instances, the low value of error and fraud identified in a claim means HMRC did not pursue it with the taxpayer or include within its estimate. HMRC did not set a 'de-minimis' threshold for the value of claims not to be pursued and, therefore, the judgement appears to have been at the discretion of individual caseworkers. Notwithstanding, we would expect HMRC to include all error or fraud in its estimate, irrespective of value. HMRC has applied a non-detection multiplier to account for non-compliance that it missed or did not fully investigate;
- we found two instances in our review of 60 claims where HMRC made adjustments to the claims that resulted in the companies having profits chargeable to tax. These profits were then offset by losses brought forward from previous years. As a result, there was no additional tax liability for the company. However, we consider HMRC should have included these adjustments in its overall evaluation of error and fraud;
- HMRC does not apply a non-detection adjustment to RDEC claims made by large businesses, implying it has identified all error and fraud in the cases it has inspected. The evidence base for this is unclear and could mean that HMRC has understated the level of error and fraud in the RDEC scheme. The non-detection adjustment is made to RDEC claimed by SMEs which were evaluated through the MREP; and
- in three of the 60 cases that we sampled, we found HMRC had initially used the incorrect yield figure in its estimate.

Developments in tackling error and fraud

2.17 The Committee of Public Accounts made a number of recommendations in February 2022 on HMRC's approach to tackling abuse of Corporation Tax research and development reliefs. HMRC accepted those recommendations, requiring it to set out:

- how it will improve its understanding of the reasons for growth in the cost of these reliefs and how much of that is due to abuse by claimants; and
- the reduction in the level of error and fraud it is seeking to achieve, together with how and when it expects that to happen.

2.18 HMRC formally responded to these recommendations in a Treasury Minute in April 2022, outlining measures announced in the Autumn Budget 2021 and other action HMRC was taking to:

- introduce a cross-cutting team of around 50 staff focused on abuse of these reliefs, in partnership with HMRC's Fraud Investigation Service. HMRC told us it launched this team in July 2022 and has provided additional capacity to look into the most complex cases. HMRC estimates the team's compliance work between July 2022 and April 2023 recovered £16.5 million;
- require companies to make all claims digitally, with more detail and endorsed by a named senior officer. HMRC implemented a digital submission form from 6 April 2023 on a voluntary basis, which will become mandatory for all claims from 1 August 2023;
- develop a programme of customer education to improve the upstream compliance programme;
- complete further analysis by winter 2023 to understand the reasons for the growing cost of research and development reliefs, including sectoral analysis of the number and average value of claims. HMRC is working with the Office for National Statistics to gain further insight into recent trends in research and development expenditure; and
- progress its MREP, randomly checking claims to inform its estimates for 2022-23 and future years.[13]

13 HM Treasury, *Treasury Minutes: Government Response to the Committee of Public Accounts on the Thirty-Sixth to the Forty-Second reports from Session 2021-22*, CP 667, April 2022.

2.19 In the Finance Act 2023, the government introduced further reforms to the rates of research and development reliefs. It increased the tax credit rate under the RDEC scheme from 13% to 20%, reduced the SME additional deduction rate from 130% to 86% and reduced the SME payable credit rate from 14.5% to 10%. These changes, which came into force in April 2023, are designed to make the two schemes more similar in terms of the level of support they provide to claimants. The legislation was, in part, in response to the estimated level of error and fraud for the SME scheme being considerably higher than for the RDEC scheme.

2.20 In January 2023, the Committee of Public Accounts recommended that HMRC should develop its analysis of the additional research and development expenditure its relief schemes result in, to consider what impact that expenditure has on the UK economy.[14] The Committee told HMRC to report on its findings within 12 months. The government has not accepted this recommendation in full but told the Committee that it intends to carry out further analysis in future to evaluate the impact on research and development expenditure of upcoming reforms to the related tax relief policy, once the data are available.

2.21 The impact of action HMRC is taking to tackle abuse of Corporation Tax research and development reliefs will not become clear until 2023-24 and beyond when the legislative changes take effect and HMRC has implemented its proposed improvements to its compliance processes and conducted an evaluation of the impact of these improvements. Given what HMRC now knows about the extent to which companies are abusing the schemes, particularly the SME scheme, it will need to consider whether the steps it is currently taking are adequate.

14 Committee of Public Accounts, *HMRC performance in 2021-22*, Session 2022-23, HC 686, January 2023.

Part Three

Personal Tax Credits

3.1 This part of the report covers the reasons and context for the Comptroller and Auditor General's (C&AG's) qualified audit opinion in relation to error and fraud in Personal Tax Credits (tax credits).

3.2 Under the Government Resources and Accounts Act 2000, the C&AG must obtain enough evidence to give reasonable assurance that the expenditure and income recorded in the financial statements have been applied to the purposes intended by Parliament, and that the financial transactions recorded in the financial statements conform to the authorities that govern them (the C&AG's regularity opinion).

3.3 The C&AG has qualified his opinion on the regularity of HM Revenue & Customs' (HMRC's) 2022-23 financial statements due to the material level of error and fraud in tax credits expenditure.

3.4 The explanation for the qualified opinion for this area of expenditure is supported by:

- an overview of HMRC's estimates for tax credits; and
- the causes of, and development in tackling, error and fraud in the administration of tax credits.

Personal Tax Credits

3.5 HMRC is responsible for administering tax credits to support families with children and to help ensure that work pays more than welfare; and for making payments to claimants on time, and in full, in accordance with legislation and the related regulations.

3.6 HMRC bases tax credits awards on initial estimates, then finalises them following the end of the tax year. The process for finalising awards relies on claimants providing complete and accurate data, and HMRC calculating awards accurately. Error and fraud in tax credits has been a significant challenge for HMRC and has led to a qualified opinion every year since they were introduced. The government is gradually replacing tax credits with Universal Credit, which is administered by the Department for Work & Pensions (DWP).

3.7 In 2022-23, HMRC spent £8.8 billion on tax credits, representing 21.6% of the total expenditure of £40.7 billion recorded in HMRC's 2022-23 Resource Accounts. Tax credits supported around 1.15 million families and around 2.13 million children.

Qualification of the C&AG's audit opinion on the regularity of tax credits expenditure

3.8 The Tax Credits Act 2002 specifies the eligibility criteria for tax credits and how HMRC calculates the amounts to be paid. Where error and fraud result in HMRC overpaying or underpaying tax credits to an individual who is either not entitled to tax credits or is paid at a different rate from that specified in the legislation, the transaction does not conform with Parliament's intention and is irregular.[15]

3.9 In the C&AG's view, the overall value of overpayments and underpayments due to error and fraud in tax credits remains material by reference to the related expenditure, and he has qualified his audit opinion on that basis.

Estimated level of error and fraud in tax credits expenditure

3.10 HMRC's latest estimate of the level of error and fraud in tax credits relates to 2021-22. This is because, under the normal tax credits annual cycle, HMRC finalised awards for 2021-22 between April and July 2022 following the end of the tax year, or in January 2023 for claimants required to submit a Self Assessment return. HMRC cannot complete its required testing to estimate the level of error and fraud until it has finalised all claims.

3.11 HMRC estimates that in 2021-22, error and fraud resulted in overpayments of 4.5% of tax credits expenditure, which is lower than the overpayment rate that HMRC initially reported in the previous year (5.0%). HMRC has now revised the 2020-21 figure to 4.7% (**Figure 12** and note 5.1.3 to HMRC's Resource Accounts). Errors in tax credits resulting in underpayments amounted to 0.4% of expenditure, which is lower than the underpayment rate in the previous year (0.8%). These rates for 2021-22 equate to overpayments of £510 million from an estimated 280,000 claims (on average, £1,821 per claim), a reduction of £220 million compared with finalised 2020-21 estimates (£730 million) and underpayments of £40 million from an estimated 70,000 claims (on average, £571 per claim), a reduction of £80 million compared with finalised 2020-21 estimates (£120 million). HMRC revisits the estimates each year to take account of new information received after the original publication.

15 HMRC's published statistics refer to error and fraud resulting in overpayments – where claimants have received more than their entitlement and this has not been corrected before finalisation – as 'error and fraud favouring the claimant', and error resulting in underpayments – where claimants have received less than their entitlement – as 'error and fraud favouring HMRC'. We use the terms overpayments and underpayments in Part Three of this report. This is not the same as overpayments reported by HMRC during the year or that arise when tax credits awards are finalised. These overpayments arise because tax credits are calculated annually, and so relate to the natural cycle of tax credits and are not included in the error and fraud statistics discussed here.

Figure 12

Overpayments and underpayments as a percentage of total tax credits expenditure, 2011-12 to 2021-22

HM Revenue & Customs' (HMRC's) central estimate of overpayments decreased compared with the final estimate for 2020-21 and has not been more than 5% for seven of the past nine years. HMRC has now revised the 2020-21 figure to 4.7%

Note

1 Estimates for 2021-22 are provisional. Final estimates will be published next year alongside the provisional 2022-23 estimates.

Source: National Audit Office analysis of HM Revenue & Customs data

3.12 The estimated overpayment rate in 2021-22 of 4.5% is at the lower end of HMRC's forecast range of 4.2% to 5.7%. HMRC analysis suggests that the tax credits population is becoming more stable due to the continued migration from the tax credits regime of those with frequent changes of circumstance whose claims present a higher risk of error and fraud.

3.13 In forming his opinion on the regularity of tax credits expenditure, the C&AG has considered whether the error and fraud rates for 2021-22 provide appropriate evidence that tax credits error and fraud remains material in 2022-23. Based on its current forecasts, HMRC expects that the error and fraud rate will remain in the range of 4.3% to 6.0% for 2022-23, although it will not publish the actual level of error and fraud until June 2024. The C&AG has, therefore, qualified his opinion based on HMRC's 2021-22 estimate and its forecast of error and fraud for 2022-23.

Causes of error and fraud in Personal Tax Credits

3.14 HMRC has reduced the size of the random sample of tax credits cases that it tests to estimate the level of error and fraud, from 3,000 in prior years to 2,000 in 2021-22. We are content that this change in methodology remains statistically valid in producing a reliable estimate. HMRC no longer reports on the full range of causes of error and fraud in its published statistics. For 2021-22, it only reported the error and fraud caused by the misreporting of income and working hours by tax credits claimants. It estimates that £190 million of overpayments are attributable to the income risk category in 2021-22, an increase of £5 million from the revised central estimate for 2020-21 (£185 million). HMRC's analysis suggests that misreporting of income by claimants is responsible for more than one-third (37%) of overpayments, up from 25% in 2020-21. An estimated £115 million of overpayments are attributable to the risk category for the misreporting of hours worked by claimants in 2021-22, a reduction of £55 million from the revised figures for 2020-21. These two categories of error and fraud account for 60% of overpayments.

Replacement of tax credits by Universal Credit

3.15 HMRC and DWP's plan is for Universal Credit to fully replace tax credits by the end of the 2024-25 financial year. HMRC remains responsible for administering tax credits until all claimants and any debt associated with their claims have either moved to Universal Credit or left the tax credits regime.

3.16 Claimants move over to Universal Credit in one of two ways:

- **Natural migration** occurs when a tax credits claimant has a relevant change in circumstances that affects their claim. Their tax credits award comes to an end, and they move across to Universal Credit. Claimants can also voluntarily apply for Universal Credit, for example where they believe they will be better off.
- **Move to Universal Credit** is a process managed by DWP to move claimants across, where no change in circumstance has occurred that would lead to natural migration.

3.17 During 2022-23 the number of claimants migrating to Universal Credit was 128,228. HMRC has indicated that it remains on target to complete the transfer of all tax credits to Universal Credit by 2024-25. It expects 482,780 migrations to take place in 2023-24 and the remaining 502,865 in 2024-25.

Transfer of tax credits debt to DWP

3.18 Between 2016 and March 2023 HMRC transferred £3.6 billion of tax credit debt to DWP. HMRC's latest forecast suggests that a further £1.0 billion of debt is still to transfer. In 2022-23, HMRC transferred £0.3 billion of tax credit debt (2021-22: £0.8 billion).

Appendix One

Our evidence base

1 This report presents our factual commentary on HM Revenue & Customs' (HMRC's) performance during 2022-23. We prepared our commentary using evidence collected between April and July 2023.

2 The report covers:

- HMRC's performance against its 2022-23 objective of collecting revenues and managing compliance; looks at the main components of the £814.0 billion raised in 2022-23; and considers HMRC's customer service and debt management performance (Part One);
- the basis of the Comptroller and Auditor General's (C&AG's) qualification of his opinion on the regularity of HMRC's Resource Accounts in relation to error and fraud in Corporation Tax research and development reliefs (Part Two); and
- the basis of the C&AG's qualification of his opinion on the regularity of HMRC's Resource Accounts in relation to error and fraud in Personal Tax Credits (Part Three).

Part One

Document review and data analysis

3 As part of our financial audit work, we reviewed the supporting information for HMRC's Trust Statement and Resource Accounts. We analysed the supporting internal data and performance information prepared by a variety of business units within HMRC, in particular from the Customer Compliance Group, the Customer Service Group including its debt management function, and the Knowledge, Analysis and Intelligence directorate. This included a review of:

- board meeting minutes;
- internally commissioned research papers;
- risk assessments; and
- performance monitoring dashboards.

4 Our review focused on information in those documents relevant to the period between 1 April 2022 and 31 March 2023.

5 During our analytical review, we examined the numbers in HMRC's financial statements, plus supporting information provided during the financial audit, and performance statistics published regularly by HMRC, such as its quarterly performance updates.

6 We reviewed *Measuring Tax Gaps 2023,* published by HMRC in June 2023, as well as *Economic and fiscal outlook,* published by the Office for Budget Responsibility in March 2023.

7 We also relied on evidence from our value for money reports relevant to the work of HMRC, and associated reports from the Committee of Public Accounts. Our reports of particular relevance were:

- *Progress with Making Tax Digital* (June 2023);
- *Managing tax compliance following the pandemic* (December 2022); and
- *Managing tax debt through the pandemic* (November 2021).

Departmental interviews

8 We conducted three virtual interviews with representatives from HMRC's business groups responsible for compliance, customer services and debt management.

9 We undertook these interviews to corroborate the evidence collected from our document review and quantitative analysis, and to understand better:

- HMRC's objectives for 2022-23 and its performance in the year;
- challenges it faced in achieving its objectives in 2022-23, and risks to performance in future years;
- HMRC's plans for maintaining and improving performance in 2023-24; and
- HMRC's views on current issues.

Parts Two and Three

10 Parts Two and Three rely principally on evidence collected as part of our financial audit work on Corporation Tax research and development reliefs and Personal Tax Credits. This work is done in accordance with International Standards on Auditing (ISAs) (UK) and Practice Note 10 'Audit of Financial Statements of Public Sector Entities in the United Kingdom'. As part of this work, we reviewed HMRC's error and fraud statistical analysis. We interviewed key staff and reviewed documents including an update on HMRC's strategy for tax credits.