



HMRC's Compliance Revenues - how HMRC will change how it reports 'Future Revenue Benefit'

Summary

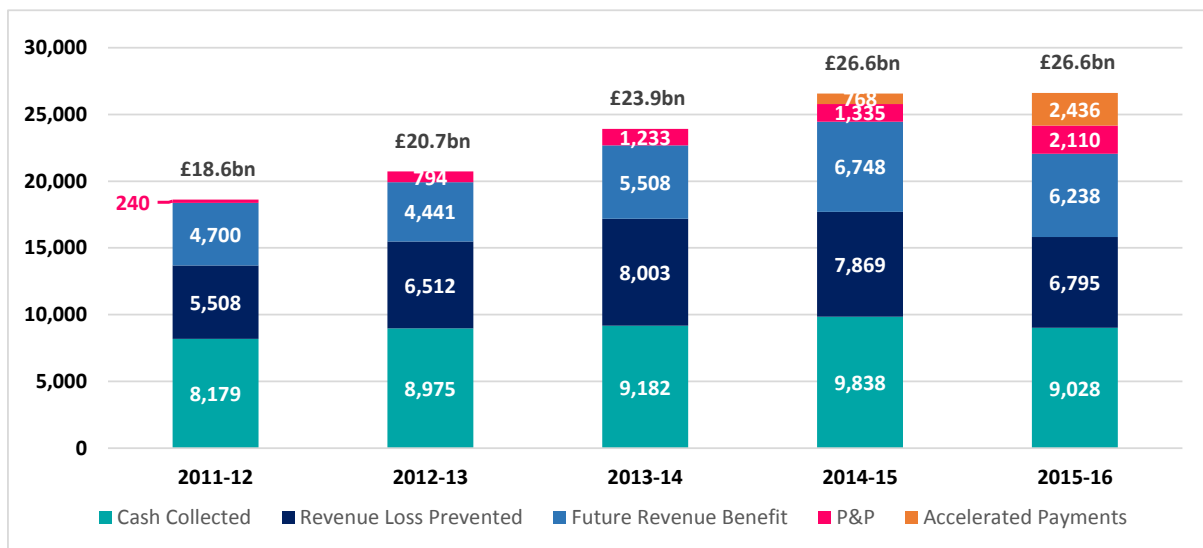
HM Revenue and Customs (HMRC) annually carries out a huge number of compliance interventions which lead to the reporting of an annual amount of additional revenue arising from this work. Since 2011, we have quantified and included 'future revenue benefits' across all of HMRC's compliance work as this helps us reflect and understand the full impact of our compliance work.

In their 2014-15 Standard Report, the National Audit Office (NAO) said that there were inconsistencies between how we recorded 'Future Revenue Benefit' (FRB) and Product and Process yield. FRB was reported in the year the compliance intervention concluded, whereas Product and Process yield is reported when the product or process change impacts Exchequer receipts. Responding to the NAO's recommendation, we will report FRB for the Spending Review 2015 period in the year in which the FRB has an impact on Exchequer receipts rather than in the year in which we complete our compliance interventions.

Introduction

1. Compliance yield is a measure of the full effect of HMRC's compliance and enforcement activities and we record it under five classifications. These are:
 - **Cash collected** — while the amounts of tax due from these cases is very clear, we cannot trace every compliance assessment through to final payment so there is an element of estimation involved in this figure
 - **Revenue loss prevented** — the value of our activities where we have prevented revenue from being lost to the Exchequer; for example, by stopping a fraudulent repayment claim. It also includes the impact of our compliance work to disrupt criminal activity
 - **Future revenue benefit** — the effects of our compliance interventions on customers' future behaviour
 - **Product and process yield** — the estimated annual impact on the net tax receipts of changes to tax law that reduced opportunities to avoid or evade tax. While an estimate, this is subject to rigorous independent scrutiny by the [Office for Budget Responsibility](#)
 - Revenue from **Accelerated Payments** notices — the disputed amounts of tax that some people using tax avoidance schemes are now required to pay upfront within 90 days, as well as the estimated behavioural change generated by the policy.

Figure 1 – Total Compliance Revenues (£m)



- Other than the inclusion of compliance yield from Accelerated Payments in 2014-15, the methodology for calculating compliance yield has remained broadly stable throughout the last Spending Review period. This covered the years 2011-12 to 2014-15 and extended to 2015-16. The contribution of Accelerated Payments is shown separately in HMRC’s Annual Report and Accounts to enable like for like comparison over the SR10 period.
- 2016-17 is the first year of the Spending Review 2015 (SR15) period, which runs to 2019-20. HMRC has reviewed the methodology for compliance yield to ensure that it remains effective for measuring HMRC’s performance for the SR15 period. One change will be made to how the future revenue benefit element of compliance yield is reported. This paper sets out the change.
- HMRC’s compliance yield target of £27.0 billion for 2016-17 has been set as part of Budget 2016, using the amended compliance yield methodology. The Government will set future compliance yield targets annually as part of the Budget process, taking account of latest forecasts and operational compliance measures.

Future Revenue Benefit

- Many of our compliance interventions have an effect not just on the particular period that the return relates to, but future years too. For example, if we make changes to the rate at which a business has claimed capital allowances or tax relief for interest payments, then the change will affect both the liabilities under investigation (cash collected) and future years’ liabilities as well. More widely, where we have identified errors or tax avoidance, our activity influences the customer’s behaviour in future years. Since 2011, we have quantified future revenue benefits across all of HMRC’s compliance work as this helps us reflect and

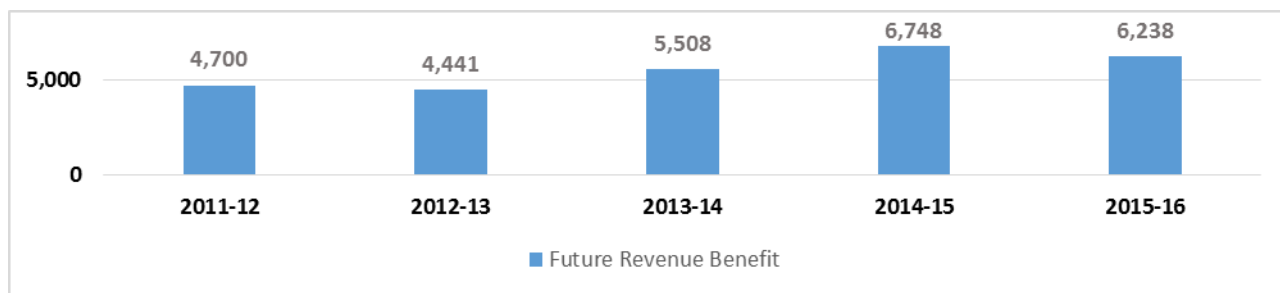
understand the full impact of our compliance work. This is important to inform how we resource to areas of highest risk. Future revenue benefit can only be recorded by caseworkers where there is sufficient evidence – there is detailed guidance in place which sets out the conditions that must be met to justify recording FRB and there are limits to the number of future years for which FRB can apply.

6. Since 2011 we have reported FRB in the year in which we complete each compliance intervention. However, the NAO pointed out in Part Three of their 2014-15 “Report by the Comptroller and Auditor General” that there was an inconsistency between how we recorded FRB and Product and Process yield. Product and Process yield is reported when the product or process change impacts Exchequer receipts.
7. Responding to the NAO’s recommendation, we intend to report FRB for the SR15 period in the year in which the FRB has an impact on Exchequer receipts rather than in the year in which we complete our compliance interventions.
8. Our operational management information systems have been changed from the beginning of 2016-17 so that caseworkers can now record separate FRB amounts against each future year. This contrasts with the management information records since 2011 which have only captured one value for FRB against each case, covering the benefits in all future years. These are underpinned by detailed calculations on case files.
9. This means that for compliance work completed from 2016-17, we will have detailed data on the expected FRB impact in each future year. However, throughout the SR15 period and in the early years of the period in particular, Exchequer receipts will be affected by compliance work that was completed in 2015-16 and previous years. To estimate the full impact on Exchequer receipts of HMRC’s compliance and enforcement work, we have therefore assessed how FRB generated over the SR10 period will impact 2016-17 and the rest of the SR15 period.

Calculating the impact of FRB generated between 2011-12 and 2015-16

10. Detailed guidance on when and for how long FRB can be scored is in place across HMRC compliance and enforcement directorates. Where we have Customer Relationship Managers in place and FRB is appropriate to be claimed, FRB can be claimed for 3 or 5 years, for other cases it’s 2 or 3 years.
11. Total amounts of FRB generated between 2011-12 and 2015-16 are set out in HMRC’s 2015-16 Annual Report and Accounts. These are shown in Figure 2 below.

Figure 2 – FRB generated, 2011-12 to 2015-16 (£m)



12. We have specifically separated FRB from VAT cases from other heads of duty. VAT works in the main on a quarterly return basis, whereas other heads of duty involve annual returns, so the profile of future periods affected by a VAT compliance intervention is more complex and needs to be modelled separately.
13. Figure 3 sets out the amounts FRB generated each year, split according to whether the FRB relates to VAT or other heads of duty.

Figure 3 – FRB generated from VAT and other Heads of Duty (£m)

£m	2011-12	2012-13	2013-14	2014-15	2015-16
VAT	1,265	1,447	1,734	3,397	3,303
Other HoDs	3,435	2,994	3,774	3,351	2,936
TOTAL	4,700	4,441	5,508	6,748	6,238

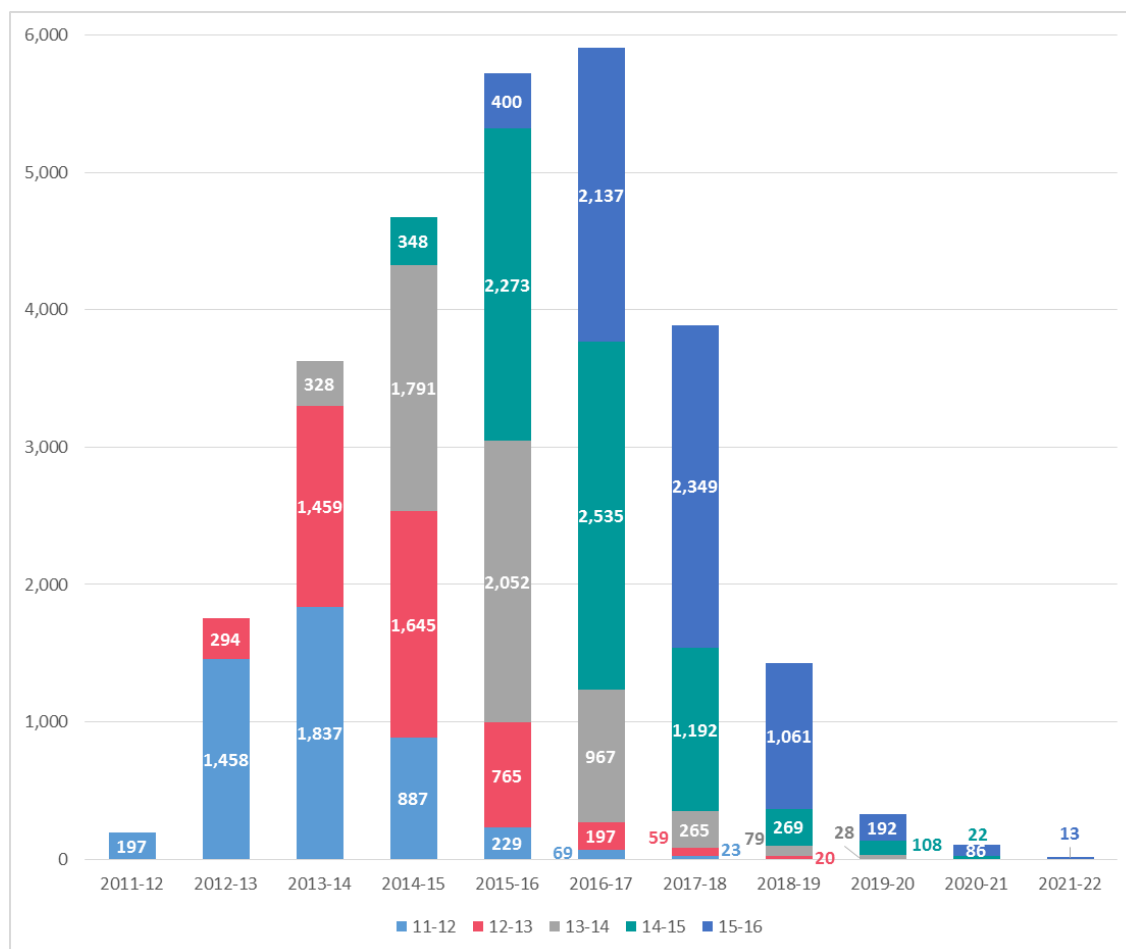
14. For VAT, the behaviour change measured by FRB starts in the first quarter after the conclusion of an investigation, which means that some FRB that is generated has an impact in the same year as the investigation. For example, a business has an investigation that concludes in quarter 2 of 2014/15 and 2 years of FRB is appropriate to be claimed. Therefore, FRB will be reported against quarter 3 and 4 of 2014/15, the whole of 2015/16 and quarters 1 and 2 of 2016/17.
15. For all other heads of duty, we have spread the amounts of FRB generated each year across the number of future years affected. We have spread the amounts on a straight line basis. So for example, for the £1.9bn generated in 2011-12 and spread over 2 future years, we have assumed 50% impacts 2012-13 and 50% impacts 2013-14.

16. Figure 4 and Figure 5 below summarise how FRB generated between 2011-12 and 2015-16 is expected to impact revenues in 2016-17 and future years of the SR15 period. It is important to note that for 2016-17 onwards the FRB elements will build up from activity undertaken in those years which will impact on future year's receipts.

Figure 4 – Estimated year of impact of FRB generated between 2011-12 and 2015-16 (£m)

		Impact											
£'m		2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22	Total
Activity	2011-12	197	1,458	1,837	887	229	69	23					4,700
	2012-13		294	1,459	1,645	765	197	59	20				4,441
	2013-14			328	1,791	2,052	967	265	79	28			5,508
	2014-15				348	2,273	2,535	1,192	269	108	22		6,748
	2015-16					400	2,137	2,349	1,061	192	86	13	6,238
Total		197	1,752	3,624	4,670	5,719	5,905	-	-	-	-	-	

Figure 5 – Estimated year of impact of FRB generated between 2011-12 and 2015-16 (£m)



How will the FRB methodology change affect compliance yield targets and reported results?

17. We expect the change of basis for reporting FRB to have a small impact on overall compliance yield results. This is because, from 2016-17 onwards, the reported annual FRB result will include amounts generated over a 6 year period of activity – amounts generated in the preceding 5 years plus small amounts of FRB generated in year from VAT interventions. This compares with the approach to reporting FRB over the SR10 period, when reported FRB related to a one year period of activity which impacted 6 years’ of future revenues – amounts generated that would affect tax receipts in the subsequent 5 years plus small amounts generated in year from VAT interventions.
18. The compliance yield target for 2016-17 of £27.0 billion is based on our best estimate of FRB using the new methodology. This includes the £5.9 billion already generated that impacts 2016-17 (see Figure 4 above), as well as a forecast of the amounts of VAT related FRB that will be generated and affect tax receipts in year. The scale of the impact of the change in methodology depends on the amount of FRB that is generated in 2016-17. Levels of FRB generated have varied significantly from year to year over the SR10 period so there is some uncertainty about exactly how much FRB will be generated in 2016-17. Figure 6 below illustrates the scale of difference that may arise under different forecast scenarios.

Figure 6 - Illustrative impact of methodology change on 2016-17 target (£bn)

Forecast FRB – new methodology	FRB generated in 2016-17: forecast scenarios	Difference
6.2	6.0	+0.2
6.2	6.1	+0.1
6.2	6.2	0.0
6.2	6.3	-0.1
6.2	6.4	-0.2

Transparency

19. We will maintain the ability to analyse FRB according to the year in which it is generated and plan to show a reconciliation of how the change in FRB methodology affects the 2016-17 compliance yield results in our 2016-17 Annual Report and Accounts.
20. This methodology change is in response to NAO recommendations on transparency and consistency. The start of the SR period is an appropriate time to make the methodological change. NAO also recommended strengthening evidence on cash collection. Work is underway on this. We will keep the Accelerated Payments methodology under review but are not currently proposing any changes to the approach used in 2014-15.