HM Treasury

Class (2013) 2:

Receipts

August 2013

HM Treasury

Class (2013) 2:

Receipts

August 2013

Any enquiries regarding this publication should be sent to us at public.enquiries@hm-treasury.gov.uk.

You can download this publication from www.gov.uk

ISBN 978-1-909790-23-0
PU1548

Contents

1 Introduction

Purpose of this document

1.1 The purpose of this document is to provide advice to departments on how actual or potential income streams are likely to be classified in the National Accounts, and the impact of this classification on the Public Sector Finances, and the fiscal position.

1.2 This paper specifically deals with current non-financial transaction income streams only. The paper discusses general issues, provides definitions, and gives advice on the application of those definitions in the public sector context.

1.3 This paper does not provide guidance on how to treat income in departmental budgets, which is dealt with in the Consolidated Budgeting Guidance (CBG). However, before the budgeting treatment of a given receipt can be settled the underlying economic nature of that transaction and its impact on the National Accounts needs to be ascertained – this paper provides guidance on that process.

1.4 The paper does not address the classification of financial transactions or non-financial transactions classed as capital. Further guidance on these issues can be found in CLASS (2013)03: Capital and Financial Transactions.

Background

Who decides

1.5 The independent Office for National Statistics (ONS) has the final say on how a particular stream of income should be classified for the purpose of National Accounts. The ONS should only be approached via HM Treasury – departments should consult their Spending Team with their classification queries. HM Treasury may settle more straightforward cases without reference to ONS.

1.6 Decisions are currently made in accordance with international guidelines set out for European Community member states in the European System of Accounts (ESA95), published by Eurostat. ESA95 is legally binding in the European Union.

1.7 A new set of National Accounts rules set out in the European System of Accounts 2010 (ESA10) are expected to replace the ESA95 rules from 2014. The rules governing receipts in ESA10 are largely expected to remain very similar to the existing ESA95 rules.

Status of the note

1.8 This is a publicly available document. The content has been agreed with the ONS. It does not represent any fundamental change on how receipts should be classified in the National Accounts. It supersedes all previous versions of this paper.

1.9 This document contains technical guidance on receipt classification and is intended to inform departments when planning the public finances consequences (if any) of introducing a fee.

1.10 This guidance should not be seen as a substitute for the rules set out in ESA95 and its accompanying manuals.

Further guidance

1.11 Departments should contact in the first instance their normal Treasury Spending Team. The Spending Team will put further questions on classification to the Classification Branch, Andrew Evans (020 7270 4623), Alex Cole (020 7270 4743) or Lesley Neill (020 7270 5338) in the General Financial Reporting (GFR) team.

1.12 Other guidance includes:

- the Consolidated Budgeting Guidance sets out the how income streams should be treated within the Department's own budgets;
- Chapter 6 (fees, charges and levies) of Managing Public Money sets out in greater detail what how a fee should be calculated; and
- the Financial Reporting Manual provides details of how income should be scored in departmental accounts.

2 Classification of receipts

General classification of income

2.1 The National Accounts are prepared according to European guidelines (the European System of Accounts 1995 (ESA 95), which in turn is based on international guidelines (The System of National Accounts 1993 (SNA 93), and supporting manuals), which enable comparisons to be made between countries that use the system. These guidelines are largely expected to remain the same under the new ESA 2010 and SNA 2008.

2.2 In National Accounts receipts can be treated in one of two ways; either as:

- financial transactions – such as issuing debt, lending or purchasing of shares, which in themselves do not impact on levels of public spending, the current balance or net borrowing, but may impact public sector net debt; or
- non-financial transactions – which may be broken down into current receipts and capital receipts, and which affect measures of Public Sector Net Borrowing and Debt.

2.3 This paper is concerned with current receipts; i.e. a subset of non-financial transactions as described above.

Types of receipts

Taxes

2.4 The European System of Accounts says taxes are:

"compulsory, unrequited payments in cash or in kind which are levied by general government or by the Institutions of the European Union"

2.5 For a receipt to be classified as tax it must therefore be levied by government and be both compulsory and unrequited:

- Compulsory – there are almost no actions that are truly compulsory – e.g. if you wish to avoid paying income tax then you could stop earning an income. So in application of this term ONS use a very broad definition, and view any payment for which there is no reasonable alternative as compulsory. Where government finds itself in a monopolistic position supplying something required by the market (e.g. a license), it should be assumed that any purchase is compulsory.
- Unrequited – there is a very narrow definition of what it means to be requited. If a payment of £x is made, then £x of service should be provided in return. If there is no personal good or service provided or if the service provided is less than £x and the rest of the payment goes towards subsidising another group leading to a cross-subsidisation, then clearly the payment was not fully requited. However, it is possible for an appropriate market rate of return to be achieved without the charge becoming unrequited. Where both of these conditions are satisfied then an income stream will be classified as tax in National Accounts.

2.6 A tax would normally be recorded where receipts arise because of government's power to make laws requiring payments in respect of economic or other activities, and which are of a type that cannot be demanded by other sectors of the economy, or where the charge is out of all proportion to the cost of the work undertaken by government. 'Out of all proportion' in this context should be taken to cover scenarios where government deliberately overcharges fee payers to generate a significant surplus over costs to be used to fund other government expenditure.

2.7 Payments for services at market prices, and payments of rent on land, interest and dividends, and occupational pension contributions can all be made to other sectors of the economy and so are not taxes. Any payment for goods in a competitive marketplace would also not be classified as a tax.

Payments for goods and services

2.8 A body will benefit from receipts where it produces goods or services for sale. In National Accounts this production will fall into one of two categories:

- market output consisting of goods and services sold onto the market at economically significant prices; or
- non-market output includes of goods and services produced where the major output is free or not at an economically significant price.

Market vs. non-market

2.9 The distinction between market and non-market will have a bearing on how a body is classified in National Accounts. A public sector body which is principally financed through market income will be classified as a Public Corporation (details on classification of bodies are available in CLASS (2013)1: Sector Classification).

2.10 The definitions above depend on what is viewed to be an economically significant price. In National Accounts how this is applied depends on the main area of activity of the body. For a Public Corporation (i.e. a market body), all output sold into the market place is assumed to be market output. However, for a general government body (i.e. a non-market producer) to record market income, the individual product being sold must cover more than 50 per cent of production costs.

2.11 In the public sector it may not always be clear whether it is correct to classify a receipt as sale of goods/services or as a tax. The section above sets out the defining characteristics of a tax, below are the details of what constitute the sale of goods and services.

Clear and direct link

2.12 If the payments received for goods and services are to avoid being classified as tax there must be a clear and direct link between the charge the purchaser pays and the benefits they gained:

- the individual paying the charge must receive separately identifiable goods or services (e.g. car parking facilities in return for a car park fee);
- the benefits must be individual to the person paying - it is not enough if the benefits accrue to a wide category of persons, or to an industry in general, of which the person paying is a member; and
- if the reason why the activity exists is to provide benefits to the public as a whole, then the function is in most cases regulatory or a levy – see separate section in Chapter 4.

2.13 Note that goods and services supplied for payment are usually of a sort that are, or could, be provided by the private sector in the market, e.g. car parking facilities; professional inspections (including the testing of an ability or level of performance or the assessment of standards); or prescriptions.

2.14 They can also include activities where the State has an actual or effective legal monopoly over, at least some aspects, of the service so long as they provide a service to the individual rather than the public in general or a general fee paying cohort. For example, courts have powers that private arbitrators do not have, but civil court fees are nonetheless payments for services.

The charge meets the costs

2.15 To score as a payment for goods and services the charge should not exceed the identifiable costs of providing the goods and services delivered to the individual, plus a reasonable market rate of return. Where there is a clear intention to set charges so as to produce receipts in excess of the identifiable costs, or where a charge consistently turns out to produce income well in excess of the identifiable costs, then the government would be deemed to be using its unique position in the economy to levy a tax.

2.16 This caveat need not apply to sales in a competitive market (see below).

2.17 In general the costs that are to be used in calculating the charge for services are those detailed under the Treasury's Managing Public Money guide.

2.18 These costs include pay, stationery, procurement of goods and services, payments to contractors, utilities, rent, and tax, which are incurred in the direct provision of the service. They include notional costs, such as imputed insurance premia where applicable, depreciation and a cost of capital set at the appropriate rate – either at the standard rate of 3.5 per cent real, or the risk adjusted market rate where applicable. These costs also include a share of overheads and the costs of a parent government department only insofar as the parent department provides services to the selling body. Senior management or corporate policy time on the delivery, or management, of the good or service is an allowable cost, but note that the costs of policy work in general are excluded.

2.19 Allowable costs do not include capital expenditure as it is made; rather the cost of consuming capital in the production of the good or service should be recovered through the price (through depreciation a reasonable rate on capital employed). Allowable costs do not include a provision for creating a return beyond the normal return to capital found in a comparable business, assumed to be 3.5 per cent for most statutory services.

Prices set in a competitive market

2.20 A receipt for a sale of goods and services will be recognised where:

- the receipt is from the provision of a good or service that could be classified as negative public expenditure;
- the price is set by the market; and
- the good or service is being provided in full, fair and direct competition with private sector providers.

Intra public sector receipts

2.21 A difficult issue is determining whether payments made by a government unit to another public unit in respect of work done should be classified as sales or as grants. In general the payments would be classified as sales if they are related to specific volumes or values of output under arms-length contracts and are not paid if that output is not delivered. Payments made by government bodies for general running costs or to cover an overall deficit are treated as grants. Bodies funded mainly by grants are non-market bodies and so will be either part of general government or a private not-for-profit institution.

Fines and penalties: enforcement income

2.22 Fines and penalties are also compulsory, unrequited payments, but are distinct from taxes as they should be punitive in nature and imposed by a judicial (or quasi-judicial) body.

2.23 Receipts associated with enforcement activities – e.g. a payment for declamping a car - are classified as fine income. Further details of defining the division between enforcement and monitoring are available in Chapter 4.

2.24 The exceptions to this are fines connected with taxes, either late payment penalties or fines for evasion; these are added to the relevant tax.

Property income

2.25 In National Accounts current receipts generated by a financial asset or rent provided in exchange for the use of a non-financial asset are accounted for under the heading of property income.

Dividends

2.26 A dividend is a payment made to a shareholder in consideration of having put equity finance into a body. The equity finance may be in the form of Companies Act shares, Public Dividend Capital (PDC) or the implied equity in a statutory public corporation.

2.27 Public sector bodies may hold equity in other public sector bodies or in private sector organisations. Dividends from either of the sources are recorded as current receipts.

2.28 If dividends are greater than the profits of the current and two previous years - super-dividends - they count as equity withdrawals in the National Accounts (a financial transaction as opposed to a current receipt). Therefore equity withdrawals count as capital income for budgeting. Therefore in comparison to dividend incomes equity withdrawals will have no impact on Public Sector Net Borrowing (PSNB) but reduce Public Sector Net Debt (PSND).

2.29 In Departmental Accounts, reductions of equity in the form of sales of shares or PDC reductions would not normally go through the Statement of Comprehensive Net Expenditure (SoCNE). But special payments from bodies that are not accompanied by actual reductions in equity holdings would go through the SoCNE; they may be termed super-dividends. Such super-dividends would be equity withdrawals in the sense above.

Interest

2.30 Where a financial asset recorded on a department's balance sheet, usually as a loan, pays interest Budgets, accounts and National Accounts all treat the receipt as a current benefit. Care should be taken to make sure that recorded interest payments do not include repayments of the principle of the financial asset.

Economic rent

2.31 Economic rents arise where government has ownership rights over land and other natural resources, and receives income in return for providing access to that asset. Rents receivable for land score as revenue receipts, as they are considered as rents for natural assets, as are receipts from licences to exploit certain sub-soil assets.

2.32 Where the government obtains an economic rent that is a revenue receipt, but the government's costs in making it available in usable form may be recovered in a fee. In practice a department should only aim to split the fee payable for services provided from the economic rent where it is sensible to so.

Rent of land and buildings

2.33 Rentals received for buildings are treated as a charge for a service, and not property income. Building management charges also score as charges for services. In contrast receipts of rent for land are considered as rents for natural assets, rather than sales of services. Therefore income from sale or rent of land will not count towards the 50 per cent needed for an entity to be classified as a public corporation.

2.34 Where a single payment covers both rentals of buildings and rent of land, departments should aim to separate the two payment streams. Where this separation cannot be done objectively or would involve disproportionate cost, the whole of the income should be classified according to what is likely to be the greater part of it.

Grants/donations

2.35 A voluntary unrequited donation from the private sector will score as a current receipt in both departmental accounting and National Accounts. To be considered a donation it must be clear that the transfer was voluntary, and that if the donation was not given then there would be no negative impact on the private sector body.

2.36 Common examples of this type of transfer to the public sector include donations collected by museums, and funds collected to finance a specific project for the benefit of the public.

Capital grants

2.37 There is a strong presumption that most grants will be current expenditure, however grants can also be capital in nature. This is the case where a grant is intended to transfer wealth permanently. There are further details on this distinction in CLASS (2013)3: Capital and Financial Transactions.

Social contributions

2.38 Social contributions are payments either from employees or employers in exchange for social benefits in the future, or to insure against risk in the future. The payment is usually hypothecated towards the service on which it is to be spent; however the actual connection between the level of payments and the level of service is often weak. For example National Insurance contributions are hypothecated towards paying for the NHS, although there is no connection between the service provided by the NHS and the level of contributions an individual has made.

2.39 Social contributions are not taxes themselves. However these contributions may be added to measurements of the tax burden:

- Compulsory social contributions are included in measures of the tax burden. For example, National Insurance contributions.
- Voluntary social contributions are excluded from measures of the tax burden. For example, payments to pension schemes.

3 Accounting and measurement

Revenue receipts vs. negative public expenditure receipts

3.1 In some cases HM Treasury chooses to present expenditure figures net of certain types of receipt. This breakdown has no fiscal effect and does not imply a specific budgetary treatment. It is not reflected in National Accounts presentations.

Negative public expenditure receipts

3.2 Receipts classified as negative public expenditure receipts are netted off, and hence reduce levels of total public spending.

3.3 The most common examples are payments for goods and services. However negative PE receipts also include: royalties for Intellectual Property Rights (IPR), income from insurance payments, guarantee fees and income from rent of buildings (but not land).

Revenue receipts

3.4 Revenue receipt refers to income that cannot be netted-off of public expenditure. It covers income that is used to finance expenditure rather than acting to reduce it.

3.5 The most common example of a revenue receipt is tax income. However it also includes: fines and penalties, payments of compensation, economic rents, interest and dividends, donations, and income from the EC.

Recording

Timing of transactions

3.6 Generally income from sales of services accrues when the service is delivered, and income from taxes accrues when the liability is created. Care should be taken to ensure that income that can be said to accrue in departmental resource accounts can actually be accrued in the National Accounts at the same time. Departments should check with their spending team contact in situations involving licences or taxes.

Calculation of allowable costs

3.7 Allowable costs for goods and services are set out in the section above. Allowable costs for licences are to be calculated by adopting the same principles as in the case of sales of services. Since the service of issuing a licence is in the various tests that government will have to undertake, the fee should be payable and the calculation of allowable costs should be for the consideration of an application, not for the granting of a licence (i.e. unsuccessful applicants should pay). If fees are calculated in another way it is likely that they could end up being classified as a tax.

Mixed revenue

3.8 Generally an income stream is not split into a tax element and a service element. However, in certain situations this may be appropriate if for example a service is delivered to an individual and in addition a tax is levied on the consumption of that product or service.

3.9 More normally where a receipt includes payment of some tax plus some elements that may be judged as a fee for a service, the entire sum is classified as tax. Only where the taxable amount is so small as to be immaterial then the mixed income would be classified as payment for a service.

Comparison with Managing Public Money

3.10 In general, for a service-type licence where all or part of the receipt may be treated as negative public expenditure, the elements of allowable costs that may be treated as negative public expenditure are the costs that form the 'service' under the Managing Public Money, except that:

- the costs of enforcement may be part of the service for Managing Public Money purposes – provided that there are explicit statutory powers to include such costs in fees - but would point to the income stream being classified as a tax, fine or penalty for the purpose of National Accounts;
- it may be that some general public good work (such as general scientific research) can be charged for through the licence fee as part of the service under the Managing Public Money purposes. Again for National Accounts purposes this would point to a tax;
- it may be that some cross subsidisation may be allowed under the Managing Public Money, subject to consideration of appropriateness and correct legal powers. Again for National Accounts purposes this would point to the income being classified as a taxl; and
- in some cases, there may be other features in services or charges that lead to a difference between what is treated as a service for Managing Public Money purposes and what is classified as payment for a service under this CLASS paper.

3.11 General policy work (other than policy on the exclusive delivery of a licence or service) is both outside the definition of recoverable costs in respect of a statutory service under the Managing Public Money and outside the boundary for negative public expenditure treatment of receipts.

3.12 In addition, voluntary transactions (such as sales of goods or services (including monitoring where appropriate)) which are not provided under a statutory duty should be unbundled from the fee and charged for as a separate non-statutory service (e.g. a commercial service), if they are to attract negative public expenditure treatment and satisfy Managing Public Money requirements.

4 Example cases

Common examples

Auctions

4.1 Selling goods at auction does not inherently change the classification compared with selling through other processes. So the classifications would remain as laid out in Chapter 2. However, conduct of an open market auction is a service to participants for which a charge may be made. The part of an auction receipt that covers auction costs may be sales of a service so long as it can be identified robustly, even if the rest of the receipt is a revenue receipt.

Advertising/sponsorship

4.2 Provision of space for advertising/ sponsorship should be considered as the sale of a service.

Sales of surplus capital goods and sale of seized goods

4.3 National Accounts score capital accumulation net of sales. The sale proceeds, measured at the open market value, from the disposal of capital assets reduce recorded levels of capital expenditure. (Note that the budgeting framework splits sale proceeds into net book value and any profit or loss on disposal – please refer to the Consolidated Budgeting Guidance (CBG) for further details).

4.4 Sales of goods seized through the courts as punishment score as current receipts; the income is treated as fine income as the income was from seized assets. This transaction is recorded at the point the assets are sold, no transaction needs to be recorded when they are seized.

Recycling mechanisms

4.5 Methods of redistributing income from one party to another as a way of incentivising behaviour are used increasingly often in the regulation of industries. Such schemes are particularly common in environmental policy but more are being considered in other areas.

4.6 For example, government may set energy generators a specific level of energy to generate from renewable sources. For each unit of energy produced in this way, they will receive a certificate (often these certificates are tradable). At the end of the year the generators surrender the certificates to government. Where generators do not have enough certificates to meet their commitments they must pay into a buyout fund, the proceeds from this fund are then redistributed to generators who hold excess certificates.

4.7 This arrangement is treated as an imputed tax and public expenditure is recognised in National Accounts: where payments by the companies which fail to meet targets are made into the buyout fund these receipts will score as tax while the associated redistribution to other organisations which exceeded their targets is treated as a subsidy from government to industry.

4.8 Where this type of scheme arises departments should discuss the scoring implications with Treasury.

Insurance and lotteries

4.9 Where the government activity for which a charge is made is the provision of insurance or the operation of lotteries or other gambling, special rules apply; HM Treasury should be consulted.

Licences and levies

Licences

4.10 Licences that do not offer a significant benefit to the applicant are classified as taxes in National Accounts. So for example a licence or registration issued automatically without tests of quality, and where the purpose is to assist an agency in its data collection or enforcement work would be considered a tax. So would 'licences' that are used primarily to raise money for collective goods and services - see also section on levies below.

4.11 In cases where a licence offers a high degree of service to the applicant these may be classified as sales of services. Examples would include work done to inspect the sea worthiness of a fishing vessel, or health inspection costs for a restaurant.

Regulatory licences

4.12 Some payments for government activities are made under the terms of licences, such as the regulation of privatised utilities. This regulation is a service to the community (or cohort of consumer), as a whole rather than to the utilities themselves. So the income from such licences is a tax also.

Levies

4.13 Where there is a compulsory levy imposed by a public sector body, and the payment of the levy does not bring a clear and direct benefit to the individual payer, the levy scores as tax in the National Accounts (and any expenditure funded by the levy scores as public expenditure). An example might be a compulsory levy on all the firms in an industry, payable in relation to their turnover, collected by a public sector research council which determines and funds a programme of research work relevant to the industry, or a compulsory levy based on staff numbers which was passed to a government body which gave grants to fund training for people working in the industry. The fact that the levy payer is a member of a group which benefits collectively or where many members of the group benefit does not provide a clear and direct link: the levy payer would have to benefit personally for it to be a negative public expenditure receipt in the National Accounts.

4.14 If the levying body is not in the public sector, or is a public corporation, then it may be necessary to impute flows to general government: a flow of tax income, and a flow of public expenditure. This is because in National Accounts only government can levy taxes and a tax is a tax, even if a private sector body collects it.

4.15 The same might apply if the levy was not explicitly identified as such. For example: suppose a regulated utility was to be required by a government body to start to subsidise one identified group of customers, implicitly charging the rest more. This transaction has characteristics of a levy. So tax and public expenditure might have to be imputed.

4.16 Charges made by certain private sector self-regulatory bodies, such as The Law Society, are payments for services made by one private sector organisation to another.

4.17 The administration of a levy is not a service to the levy-payer.

Licences and levies – tax vs. charge

4.18 As discussed above, the majority of licences and levies are considered as tax receipts. However, where the licence provides a high degree of service to the individual recipient, as opposed to society as a whole, or a general fee paying cohort, and provided that the fee covers only allowable costs, and raises no more than those costs (issuing the licence/ making the registration), it may be treated as a payment for services – see below.

ESA95 rules on licences

4.19 Under the current European System of Accounts rules (ESA95) all licences are primarily for the benefit of the public as a whole, but:

- in some cases, there is also a significant element of service to the individual fee-payer. Subject to conditions, these may be treated as payment for services; and
- the remaining licences, where there is not a substantial element of service to the fee-payer, are to be treated as tax.

4.20 ESA95 further sets out how certain specified licences are to be treated, having regard to the way they are organised in the majority of EU Member States. However, this does not mean that ONS will treat ostensibly similar licences in the same manner: it may be that there are differences in the way a licence is constructed in the UK, meaning that a different classification to the equivalent licence in other EU member states is warranted.

Licences with significant element of service to the applicant

4.21 The issuance of a licence is a service primarily to the community as a whole, as it is normally seen to be an improvement to the regulation of an industry. However, in some cases, there may be a significant element of service to the individual applicant, for example:

- the essence of the decision whether to issue a licence or not may be the result of a test of the competence or quality or suitability of the applicant or her/his premises, staff, equipment or products. In such cases, the licence may also be seen as a service to the applicant in that it provides an objective statement of fitness which once obtained allows the holder to operate in the market place, or
- the licence may be materially useful in the licence-holder’s dealings with others, e.g. a passport helps British travellers deal with foreign governments.

4.22 In such cases the income might be treated as sales of a service in the National Accounts if it meets the criteria discussed above and further explored below.

Setting prices

4.23 What costs can be included in the calculation of costs, if the receipt is to be classified as negative public expenditure? Activities that may be treated as allowable costs for service type licences include:

- the cost of pre-issue checks of competence, quality, fitness of the applicant or the applicant’s premises, factory, vehicles etc;
- the cost of subsequent checks on the accuracy of information provided at the time of issuing the licence;
- the cost of pre-issue checks other than on the applicant. For example, suppose the regulatory body will allow a river to receive a certain amount of pollution: before issuing a licence the body checks whether the river can take more pollution or not;

- the regulatory body's own costs in legal proceedings are covered, including orders for legal costs against it (but not orders for damages);
- post-issue individual monitoring is a service, where this is or could be structured as a marketed service. For example, a licence might permit a licence holder to deposit a ton of pollutants each month. The licence might require monthly audit reports from an independent person to the regulator. Such reports would be objective and could be provided in a market place. (Enforcement or continuing regulation requiring an exercise of discretion and judgment would be outside the boundary) (but see below for the difference between enforcement and monitoring);
- licence fee administration (paperwork) and post-issue administration. It is reasonable for the initial fee to cover the costs of e.g. noting a subsequent change of address, or recording the cancellation of a licence because a court has annulled it; and
- management, share of overheads, senior management and corporate policy work on the executive delivery of the licence/service (but not policy in general, even if on a related area).

4.24 Certain costs are outside the boundary of what can be recovered if the fee is still to be considered a charge for a service to the individual:

- policy work (other than policy on the executive delivery of a licence or service);
- recovery of externalities imposed on society by the licence-payer (e.g. pollution reduction charges);
- public good work, i.e. where there is not a clear and direct link between payment of a fee and receipt of a service - e.g. using part of the licence fee to finance research even if it is of general interest to many of the people paying the charge, or continuing economic and consumer protection regulation of an industry (see above for details on levies); and
- enforcement. Enforcing licence conditions is similar to enforcing a requirement for non-licence holders to obtain licences. It is thus a form of general policing and hence a government activity (but see below for the difference between enforcement and monitoring).

4.25 The inclusion of the above costs in the calculation of fees is likely to mean that the fee could end up being classified as a tax or a fine.

Enforcement vs. monitoring

4.26 Since enforcement is outside the boundary of recoverable cost but monitoring is inside, the difference between these two concepts is crucial for classifying whether income is tax or payment for a service. Guidance on making the distinction are set out below:

- enforcement is about proactively using state powers of compulsion to do something. An implication is that the potential criminal would know (or not care) that s/he was doing something wrong, and is having actual or potential enforcement done to them; and
- individual Monitoring is about measuring. It suggests a process by which an innocent licence-holder makes sure that they stay on the right side of the law. Monitoring is or could credibly be initiated by the licence-holder. Any resultant

provision of information to the regulator is incidental and the regulator is a passive recipient.

4.27 Some examples:

- a car speedometer is part of monitoring; a radar speed trap is part of enforcement;
- a requirement to provide a monthly certificate from an independent person that the speedometer is accurate is monitoring, as it is a by-product of the motorist satisfying themselves that the speedometer works. Even if the regulator is (for some good reason) such a recognised independent person, the Regulator's work is a service to the licence-holder. Chasing people who fail to provide a monthly certificate is enforcement. A spot check by the regulator to test speedometer accuracy is enforcement; and
- if the firm copies a speedometer printout to the regulator and the regulator reviews it looking for breaches, this is enforcement; if the regulator acts on speed limit breaches revealed by the printout that too is enforcement.

4.28 Further:

- ensuring that unlicensed people who need licences/ registration have them is enforcement (other than providing general guidance on the need for a licence and how to apply);
- enforcement processes are instigated by the enforcers, perhaps in response to complaints, perhaps on a sample or perhaps on all licence holders;
- where the regulator does the monitoring/ enforcement (e.g. a routine check of equipment 3 months after a licence has been issued), to be monitoring it should be credible that the person being monitored is also interested in the information and uses it to stay the right side of a licence condition. So monitoring information made available to the regulator is (or could be organised so as to be) a by-product of the processes of the person being monitored acting in good faith to comply with the terms of the licence;
- where the 'monitoring' done by the regulator duplicates monitoring done by or for the licence-holder, that suggests that the regulator is enforcing;
- Where monitoring shows up a breach, the proceedings that follow would be enforcement; and
- Random checks to see whether operatives hold a licence are enforcement.

HM Treasury contacts

This document can be downloaded from www.gov.uk

If you require this information in another language, format or have general enquiries about HM Treasury and its work, contact:

Correspondence Team
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

Tel: 020 7270 5000

E-mail: public.enquiries@hm-treasury.gov.uk

ISBN 978-1-909790-23-0