Report by the Comptroller and Auditor General

HM Revenue & Customs 2021-22 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 £731.1 billion of tax revenue for 2021-22. 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. 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 taxes are adequate. We found that HMRC's systems are adequate, subject to the observations in this report and other reports to Parliament.
Resource Accounts	The cost of running HMRC in 2021-22 was £6.2 billion. HMRC paid out £51.8 billion, including £10.6 billion of Personal Tax Credits payments, £11.4 billion of Child Benefit and £17.3 billion in relation to the main COVID-19 employment support schemes, which comprise: the Coronavirus Job Retention Scheme and the Self-Employment Income Support Scheme. 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 • material levels of error and fraud have been identified in the COVID-19 support schemes (Part Two); • there remains a material level of error and fraud in Personal Tax Credits expenditure (Part Three); and • there remains a material level of error and fraud in Corporation Tax research and development reliefs (Part Three).
Annual Report	We reviewed HMRC's performance against its objective of collecting tax revenues and considered the main components of the £731.1 billion raised during 2021-22 (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, 2021-22

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 2021-22, 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 2021-22 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 Two). Each audit comes under different legislation (see 'Coverage of this report', page R4). 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 2021-22 objective of collecting revenues and managing compliance, look at the main components of the £731.1 billion raised in 2021-22 and consider HMRC's customer service 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 the COVID-19 employment support schemes (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 Corporation Tax research and development reliefs and Personal Tax Credits (tax credits) (Part Three).

Summary findings

Total revenues

4 **HMRC reported total revenues of £731.1 billion for 2021-22, the highest on record, representing a 20.1% increase on 2020-21.** Its total revenues increased by £122.3 billion compared with 2020-21 (£608.8 billion). Increases were reported in all revenue streams, most notably in relation to Income Tax, Value Added Tax (VAT) and Corporation Tax, which increased by 21.6%, 21.9% and 27.2%, respectively. This reflects the recovery of the economy now that the impact of the pandemic has begun to subside and is broadly consistent with the Office for Budget Responsibility's expectations for 2021-22. The three largest components of revenue in 2021-22 were Income Tax, National Insurance Contributions and Value Added Tax (VAT), which together accounted for 73.9% (£540.5 billion) of the total. Of the reported total revenue of £731.1 billion, HMRC reported £173.8 billion (23.8%) from tax liabilities that had not been paid by 31 March 2022 (paragraphs 1.2 to 1.4, 1.7 to 1.10 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 5.1% of all tax liabilities, equivalent to £32 billion in 2020-21.** HMRC's estimate of the tax gap for 2019-20 was 5.1% and £34 billion; HMRC revised it down from the 5.3% and £35 billion previously reported after updating its estimates and adjusting for an error it identified. The precise scale of the tax gap is inherently uncertain and difficult to estimate, and HMRC's 2020-21 estimates of the tax gap are more uncertain than usual due to the impact of COVID-19 on the data it uses to inform its estimates. The tax gap may be caused by 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. The tax HMRC generated from its tax compliance work declined during the pandemic, but HMRC's estimates do not indicate any increase in the size of the tax gap as a result. HMRC assigned some of the reductions in compliance yield in 2020-21 to previous years based on the years of liability of the cases under investigation, which resulted in a reduction of £0.7 billion or 0.1 percentage point to the 2020-21 total tax gap estimate while increasing the tax gap for earlier years by the same amount in total. In monetary terms, HMRC estimates that the tax gap reduced most for VAT, and increased most for Self Assessment Income Tax (paragraphs 1.18 to 1.20 and Figure 3).

6 **HMRC estimates that the yield from its tax compliance activities in 2021-22 was £30.8 billion, up 1.1% compared with 2020-21.** 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 2021-22 is lower than the £36.9 billion reported in 2019-20 before the impact of the pandemic on HMRC's compliance activity occurred. The average compliance yield over the past 5 years was £32.5 billion. In 2021-22, HMRC opened 265,000 compliance investigations and closed 256,000, compared with 361,000 and 351,000 respectively in 2019-20. As in 2020-21, HMRC and HM Treasury agreed that COVID-19 had created too much uncertainty to determine an appropriate compliance target for 2021-22 (paragraphs 1.21 to 1.28 and Figure 4).

7 **Total tax debt was £41.6 billion at 31 March 2022, £15.9 billion less than the debt reported at 31 March 2021.** The main reason for the decrease was the repayment of debt that had been deferred under the government VAT and Self Assessment deferral schemes, which allowed taxpayers to defer the payment of some of their tax liabilities during the pandemic. As at 31 March 2022, HMRC's debt balance of £41.6 billion was 86% (£19.2 billion) higher than the level of debt reported at 31 March 2020, before the impact of the pandemic. HMRC told us that it expects to raise an additional £1.8 billion for the Exchequer between 2022-23 and 2024-25 from an additional investment of £62 million in debt management resources and new operational capability. HMRC's forecasts, which it uses for management purposes indicate that the debt balance is currently expected to be £42.5 billion at 31 March 2023. The forecast is subject to uncertainty and external factors such as the performance of the economy, which are not within HMRC's direct control (paragraphs 1.8 and 1.11 to 1.14).

Customer service performance

8 **HMRC's post and call handling performance fell significantly during the pandemic but satisfaction with digital services has been broadly maintained.** In 2021-22, HMRC responded to 39.5% of post within 15 days (2019-20: 70.3%) and the average speed of answering calls to HMRC helplines was 12:22 minutes (2019-20: 6:39 minutes). Satisfaction with digital services was 83.4% (2019-20: 81.6%). In 2021-22, HMRC developed new performance measures to provide a broader overview of the customer experience. The new measures seek to capture how easy or hard it is for taxpayers to access services, and whether HMRC has helped taxpayers to resolve their queries. These measures are now HMRC's principal means of evaluating customer service performance. For 2021-22, HMRC told us that it set expectations to help it manage its performance, rather than as a mechanism to promote accountability. HMRC achieved nine of the 20 quarterly performance expectations it set for 2021-22 in respect of customer service. Four of the eleven expectations not met in 2021-22 related to performance in handling taxpayer postal and iForm correspondence, which was below expectations in all four quarters. In October 2021, HMRC took steps to address this, including by redeploying customer service staff, although the focus on recovering correspondence performance has caused performance to fall in some other customer service areas such as Net Easy and Telephony (paragraphs 1.29 to 1.34 and Figures 6 to 8).

HMRC's Resource Accounts qualifications

9 **The C&AG has qualified his opinion on the regularity of HMRC's 2021-22 Resource Accounts due to the material levels of error and fraud in the main COVID-19 support schemes.** These comprise the Coronavirus Job Retention Scheme (CJRS) and the Self-Employment Income Support Scheme (SEISS). The government's priority at the start of the pandemic was to get support to those who needed it as quickly as possible. From the outset of the schemes, HMRC's view was that the pace of implementation, and the need to process payments quickly, would limit its opportunities to mitigate error and fraud. HMRC's current most likely estimate of the level of error and fraud in the 2021-22 COVID-19 support scheme payments is £617 million, of which £241 million relates to CJRS and £376 million to SEISS (paragraphs 2.2, 2.7, 2.10 and Figure 9).

10 **Total error and fraud across the lifetime of the schemes based on HMRC's current estimates is £4.46 billion, of which £3.46 billion relates to CJRS and £1 billion to SEISS.** HMRC's 2021-22 and revised 2020-21 error and fraud estimates now reflect direct evidence at the claim level from a mandatory random enquiry programme and analysis of Self Assessment tax return data. However, the estimates remain subject to considerable uncertainty, and the actual levels of error and fraud in the schemes could differ significantly from the rate and values reported. HMRC has sought to evaluate this uncertainty through the estimated ranges it has reported. The key sources of uncertainty that require significant judgement to be exercised, include: reliance on internal and external survey data where there is no direct evidence at the claim level; the availability of more current random enquiry and Self Assessment return data requiring the results of earlier analysis to be extrapolated across the remainder of the schemes; and weaknesses in certain aspects of the random enquiry programme that did not find evidence of organised crime or non-payment of furlough to employees. This could be because either these risks did not materialise or they were not detected by HMRC (paragraphs 2.9, 2.12, 2.16. 2.18 and Figure 9).

11 **The C&AG has qualified his opinion on the regularity of HMRC's 2021-22 Resource Accounts due to the material level of error and fraud in Personal Tax Credits.** The most recent estimate indicates that in 2020-21 error and fraud resulted in overpayments of 5% of tax credits expenditure, the same as the overpayment rate initially reported in the previous year. The 2019-20 finalised figure has now been revised to 5.3% (note 5.1.3 to the HMRC Resource Accounts). Errors in tax credits resulting in underpayments amounted to 0.8% of expenditure. The underpayment rate reported in the previous year was also 0.8% but has now been revised to 0.9%. These rates equate to overpayments of £780 million from an estimated 400,000 claims, or on average, £1,950 per claim (a reduction of £160 million compared with finalised 2019-20 estimates) and underpayments of £120 million from an estimated 300,000 claims, or on average £400 per claim (a reduction of £50 million compared with the finalised figures for 2019-20) (paragraphs 3.2, 3.13 and Figure 9).

12 **The C&AG has qualified his opinion on the regularity of HMRC's 2021-22 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's most recent estimate shows that the level of error and fraud present in this area of expenditure is £469 million or 4.9% of related expenditure (2020-21 – £336 million or 3.6% of related expenditure). HMRC indicated that the increase in the estimated error and fraud rate relates to an increase it has identified in the number of erroneous and fraudulent claims being made for costs that do not qualify for these reliefs. HMRC continues to implement changes to understand the risks of scheme abuse better and measures to strengthen compliance (paragraphs 3.28, 3.20 and 3.36 to 3.46).

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 2021-22, 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 has made some progress in restoring its operational performance during 2021-22, with the acute phase of the pandemic having now ended. The backlog of customer correspondence it is handling has reduced. However, tax debt levels remain high, and compliance activity and customer service performance are lower than pre-pandemic levels. Where HMRC intends to return to historical levels of performance, this will require careful prioritisation and deployment of resources and will be particularly challenging against the backdrop of dealing with the post-EU transition period and its plans to modernise the tax system. When deciding what further steps it should take on recovery of error and fraud in the COVID-19 support scheme payments, HMRC will need to evaluate its costs and the returns it is achieving.

Part One

Performance in 2021-22

1.1 This part of the report sets out HM Revenue & Customs' (HMRC's) performance in 2021-21 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 performance reported by HMRC in 2021-22.

Total revenue in 2021-22

1.2 The total revenue HMRC reported in its Trust Statement in 2021-22 was £731.1 billion (£608.8 billion in 2020-21) (**Figure 1** overleaf).[1] Total revenues increased by £122.3 billion (20.1%), reflecting the recovery of the economy now that the impact of the pandemic has begun to subside. The following four types of taxes accounted for 81.3% of the increase: Income Tax (£41.4 billion, 21.6%), Value Added Tax (£26.7 billion, 21.9%), National Insurance Contributions (£16.8 billion, 11.9%) and Corporation Tax (£14.6 billion, 27.2%). Total revenues in 2021-22 were £94.4 billion (14.8%) higher than revenues reported in 2019-20 before the pandemic, which was the highest reported revenue collected at that time.

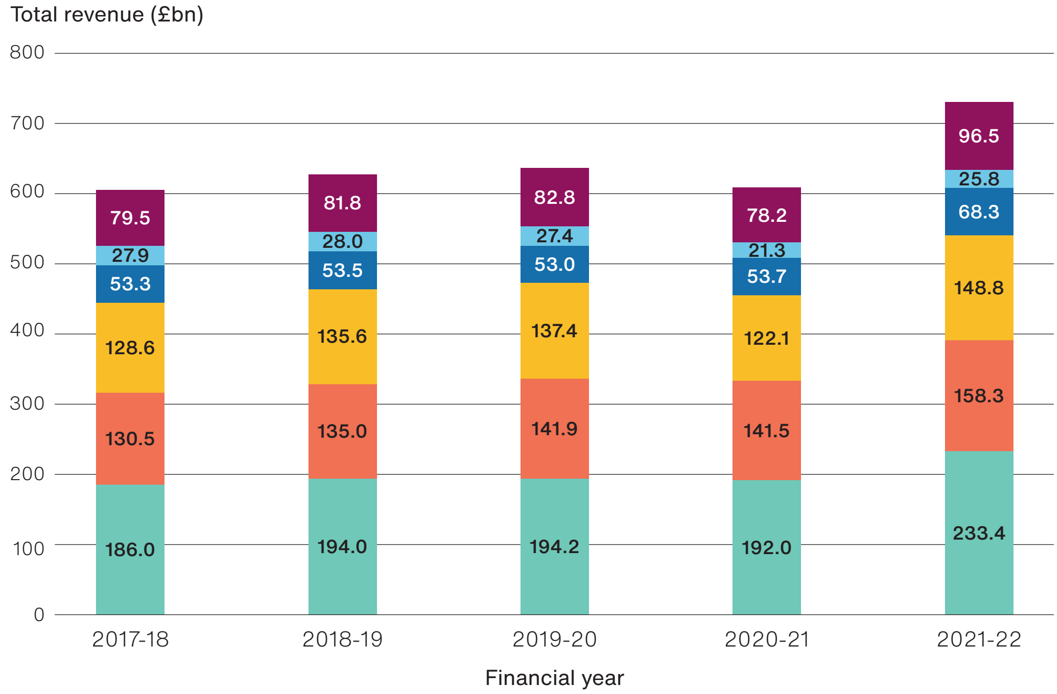
1.3 Total revenues reported for 2021-22 includes £10.2 billion in respect of under-estimates of accrued revenues receivable in 2020-21, most notably £8.0 billion in respect of Self Assessment receivables. This arose due to HMRC under-estimating the extent to which Self Assessment receipts would increase following the pandemic, reflecting the economic uncertainty at the time its estimates were produced. HMRC has not estimated the revenue that has arisen from Income Tax and National Insurance Contributions due on grants it paid through the Coronavirus Job Retention Scheme and Self-Employment Income Support Scheme.

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 the cash is received, Values throughout this 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) from 2017-18 to 2021-22

In 2021-22, total revenues increased by 20.1%, exceeding pre-pandemic levels



	2017-18	2018-19	2019-20	2020-21	2021-22
Total revenue (£bn)	**605.8**	**627.9**	**636.7**	**608.8**	**731.1**
Change in total revenue (£bn)	–	22.1	8.8	-27.9	122.3
Change in total revenue (%)	–	3.6	1.4	-4.4	20.1

- Other[1]
- Hydrocarbons oils duty
- Corporation Tax
- Value Added Tax
- National Insurance Contributions
- Income tax

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 Three largest components of revenue in 2021-22 were Income Tax, National Insurance Contributions and Value Added Tax, which together accounted for 73.9% (£540.5 billion) of the total.

Source: National Audit Office analysis of HM Revenue & Customs, Annual Report and Accounts 2017-18 to 2021-22

1.4 In March 2022, the Office for Budget Responsibility (OBR) set out its expectations that public receipts in 2021-22 would increase by £106.4 billion (13.4%) compared to 2020-21, outperforming growth in the nominal gross domestic product (GDP), which was expected to rise by 10.4%.[2] The OBR's assessment of the level of recovery in receipts between 2019-20 and 2021-22 following the pandemic highlighted:

- Pay as You Earn (PAYE) Income Tax and NICs receipts, with wages and salaries growing faster than nominal GDP mainly due to fiscal support measures;
- Value Added Tax (VAT), where receipts remained broadly flat with a fall in household consumption relative to nominal GDP being offset by a rise in the effective tax rate, as consumer behaviour shifted to higher rated goods as well as a higher share of non-refundable government procurement;
- Corporation Tax, boosted by higher profits by financial and non-financial companies and those sectors that are typically large sources of Corporation Tax receipts and have either been little affected by the pandemic or benefitted from the shifts in activity that it induced, for example, financial and professional services and retail; and
- Other taxes, where some taxes have fallen relative to GDP, for example, the drop in air travel that has hit passenger duty receipts.

Repayments

1.5 The total revenue figure of £731.1 billion is net of £126.6 billion of repayments to taxpayers (£114.2 billion in 2020-21) (**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 their full liability is assessed, which can lead to repayments.

1.6 Most repayments relate to VAT (£107.4 billion in 2021-22, which compares with total VAT revenue in 2021-22 of £148.8 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.

Receivables, impairment and revenue losses

Receivables and accrued revenue receivables

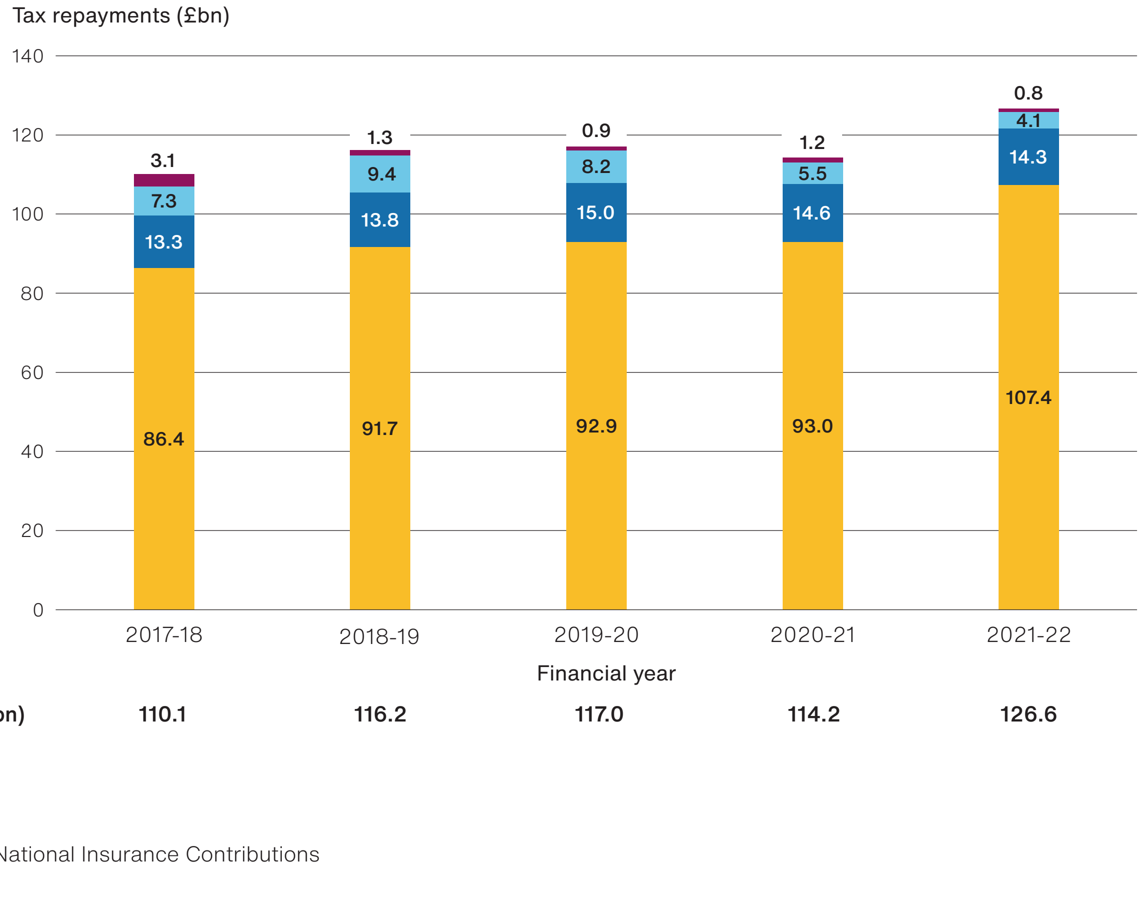
1.7 Receivables represent taxpayer liabilities to HMRC that have been established, irrespective of whether they are due or overdue. They can include taxes, duties, recovery of tax credits, penalties and interest charges owed by individuals and businesses.

2 Office for Budget Responsibility, *Economic and fiscal outlook*, March 2022, paragraph 3.21. 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 from 2017-18 to 2021-22

Repayments in 2021-22 increased by 14.3%, largely due to an increase in repayments of Value Added Tax



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 2017-18 to 2021-22

1.8 As at 31 March 2022, HMRC total receivables amounted to £173.8 billion – 23.8% of revenue (March 2021: £159.8 billon, 26.2%). This balance consisted of:

- **receivables** – £51.2 billion (29.5%) due from taxpayers but not yet received. This is a decrease in the value and proportion outstanding since 31 March 2021 (£65.3 billion; 40.9%). HMRC's analysis indicates that the decrease was largely due to the repayment of tax deferred under the government VAT and Income Tax (Self Assessment) deferral schemes; and
- **accrued revenue receivables** – an estimated £122.6 billion (70.5%) (31 March 2021: £94.5 billion; 59.1%) of taxes not yet due from taxpayers but relating to 2021-22 revenues where a tax return has not been received from the taxpayer by the end of the reporting period.[3] Most of the £28.1 billion increase in the accrued revenue receivables was attributable to Income Tax (Self Assessment) and VAT of £12.2 billion and £8.9 billion respectively, and was largely due to the increase in related tax revenues during the year.

1.9 Of the £122.6 billion accrued revenue receivable balance, 93% comprises taxpayer liabilities for VAT (£46.1 billion), Income Tax (£41.9 billion), National Insurance Contributions (£16.7 billion) and Corporation Tax (£9.4 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 6 of the Trust Statement.

1.10 We review HMRC's models and assumptions as part of our financial audit of HMRC, and are satisfied that its estimates are reasonable based on the data available to HMRC at the time.

1.11 In response to the pandemic, the government allowed businesses and individuals more time to pay their VAT and Self Assessment liabilities, and paused or reduced debt collection activity for those taxpayers it assessed were in most difficulty. HMRC reduced its debt collection activity for two months in 2021-22 (pausing activity twice, between March and June 2020 and again between December 2020 and May 2021). During these pauses, HMRC did not undertake proactive campaigns with businesses and other taxpayers to collect their tax debt, although it did continue to provide debt services, including agreeing time to pay arrangements.[4] These factors led to a significant increase in tax debt. As at 31 March 2022, HMRC's debt balance of £41.6 billion was 86% (£19.2 billion) greater than the level of debt at the end of March 2020 before the impact of the pandemic. Over the same period, the number of taxpayers in debt had increased by 22% from 6.3 million in March 2020 to 7.7 million in March 2022.

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 receivables.

4 For taxpayers who cannot pay their tax bill in full, HMRC may suggest they pay what they owe in instalments. This is called a 'time to pay arrangement'.

1.12 In November 2021, the National Audit Office published *Managing tax debt through the pandemic*.[5] The report considered how well HMRC had managed tax debt through the pandemic – in particular, whether it had adapted sufficiently to the changing nature and scale of that debt and the wider circumstances that affect taxpayers' ability to repay tax. We noted that HMRC had prioritised which debts to chase based on its understanding of the likely impact of the pandemic on taxpayers' ability to pay. The report also noted that HMRC had a limited understanding of how the pandemic will affect the amount of specialist work needed to manage debt – for example, in relation to 'phoenix' companies, whereby companies are wound up and re-formed specifically to avoid paying debts. We recommended that HMRC should identify how its debt management needs to operate differently to deal with the changed nature and amount of debt.

1.13 HMRC's debt balance is affected by other external factors that are not within its direct control – for instance the Omicron wave that developed during the year and the impact of the Ukraine conflict on taxpayers' ability to meet their tax liabilities. These factors have led to the level of debt reported at 31 March 2022 remaining higher than HMRC had previously anticipated. 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 2022, 'managed debt' constituted £7.5 billion (18%) out of the total debt balance of £41.6 billion.

1.14 HMRC told us that it is taking steps to improve its debt management capability, including by drawing on private sector expertise and insolvency analytics, and by developing a customer segmentation model based on taxpayers' propensity to pay, allowing better targeted debt recovery action. The number of staff in HMRC's debt management function has also increased from 3,975 in 2019-20 to 4,289 in 2021-22. HMRC expects to raise an additional £1.8 billion for the Exchequer between 2022-23 and 2024-25 from an additional investment of £62 million over the three years in additional debt management resources and capability. HMRC's forecasts, which it uses for operational management purposes, suggest that the tax debt balance will be £42.5 billion at 31 March 2023. The forecast is subject to uncertainty and external factors, such as the performance of the economy, which are not within HMRC's direct control.[6]

5 Comptroller and Auditor General, *Managing tax debt through the pandemic*, Session 2021-22, HC 799, National Audit Office, November 2021.

6 HMRC forecasts suggest the debt balance at 31 March 2023 will most likely be between £37.1 billion and £45.5 billion.

Impairments

1.15 The receivables balance of £51.2 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 £14.4 billion (2020-21: £14.7 billion) of these receivables. When adjusted to reflect this, the overall receivables balance due from taxpayers is £36.8 billion (2020-21: £50.6 billion). The receivables impairment rate increased from 22.5% in 2020-21 to 28.1% in 2021-22. HMRC's analysis identifies a number of factors that have contributed to the increase in the impairment rate. These include the higher probability of impairment associated with the residual debts deferred under the government VAT and Self Assessment deferral schemes, and a general increase in the age profile of HMRC's debt. HMRC's approach to calculating the impairment is set out in Note 4.2 of the Trust Statement.

Losses

1.16 In certain cases, HMRC stops debt collection activity and incurs a 'revenue loss' – such losses are likely to relate to total revenue due in earlier financial years. There are two forms of revenue losses: write-offs of £1.9 billion during 2021-22 (£1.5 billion in 2020-21) and remissions of £0.5 billion in 2021-22 (£0.4 billion in 2020-21). 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 insolvencies. These are returning to pre-pandemic levels, following a reduction in 2020-21 caused partly by the government's measures to financially support individuals and businesses during the pandemic. The reduction in HMRC's compliance activities during the pandemic also contributed to reduced levels of reported losses.

Provisions and contingent liabilities

1.17 HMRC recognises a provision in the Trust Statement whereby 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**, whereby 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 2021-22, HMRC repaid £0.5 billion to taxpayers in respect of legal provisions (2020-21: £1.1 billion). As at 31 March 2022, HMRC expects it will have to repay £3.2 billion (2020-21: £3.4 billion). Claims in respect of Corporation Tax account for 67% 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 £3.2 billion as at 31 March 2022 (2020-21: £3.1 billion).
- **Oil and gas field decommissioning costs**, whereby 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 2022, HMRC estimates that it will have to repay £10.4 billion of tax in relation to oil and gas field decommissioning (2020-21: £9.5 billion). This is the estimated amount that HMRC will repay to oil and gas companies and is based on an estimate of the decommissioning costs they will incur in future periods. In 2021-22, companies recovered £0.5 billion of Petroleum Revenue Tax from HMRC in relation to decommissioning losses.

Tax compliance

Tax gap

1.18 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”.[7] 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.

7 HMRC’s *Measuring tax gaps 2022 edition* is available at: www.gov.uk/government/statistics/measuring-tax-gaps

1.19 HMRC has estimated that the tax gap for 2020-21 – the latest year for which data are available – was £32 billion (2019-20: £34 billion). The tax gap for 2020-21 represents 5.1% of the total theoretical tax liabilities of £635 billion and is consistent with the 5.1% tax gap estimated by HMRC for 2019-20.[8] HMRC's estimate of the tax gap for 2019-20 was 5.1% and £34 billion. This was revised down from 5.3% and £35 billion after updating estimates using established methodologies and identifying an overestimation of the Corporation Tax gap, which affected the overall tax gap by 0.1 percentage points. The tax gap split by the different types of tax is shown in **Figure 3** overleaf.

1.20 The precise scale of the tax gap is inherently uncertain and difficult to estimate. However, HMRC's 2020-21 estimates of the tax gap are subject to more uncertainty than usual due to the impact of COVID-19 on the data used in HMRC's estimation processes. The proportion of the tax gap estimates in 2020-21 with a 'high' or 'very high' uncertainty rating was 30% (2019-20: 18%). The tax HMRC generated from its tax compliance work declined during the pandemic, but HMRC's estimates do not indicate any increase in the size of the tax gap. HMRC assigned some of the reductions in compliance yield in 2020-21 to previous years based on the years of liability of the cases under investigation, which resulted in a reduction of £0.7 billion or 0.1 percentage point to the 2020-21 total tax gap estimate while increasing the tax gap for earlier years by the same amount in total. In monetary terms, HMRC estimates that the tax gap reduced most for VAT, while the gap increased most for Self Assessment income tax. HMRC estimates that the tax gap was unchanged for PAYE, despite many companies needing employment support during the pandemic. HMRC accounts for non-payment in the tax gap when it stops pursuing debts and the debts are written off or remitted.

Compliance activities and compliance yield

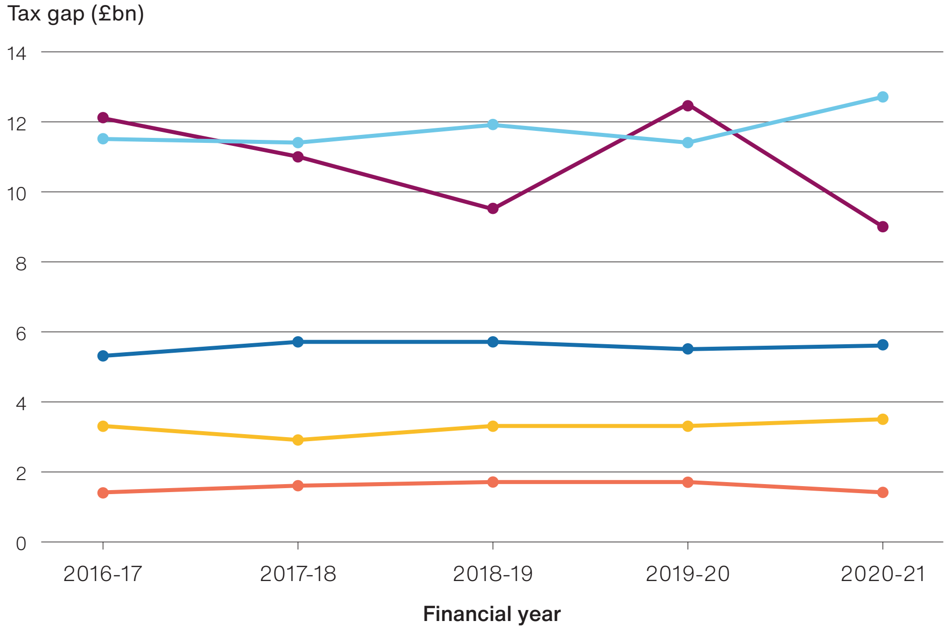
1.21 Compliance activities can take many different forms. These can include disrupting organised criminal groups or tackling the use of tax avoidance schemes, as well as measures to promote compliance and prevent non-compliance, such as guidance to taxpayers and the Making Tax Digital changes.

1.22 HMRC told us that the aim of its compliance work is for everyone to pay the 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. HMRC will investigate where it believes a business or individual is trying to cheat the tax system.

8 See footnote 7.

Figure 3
HM Revenue & Customs' (HMRC's) estimates of the 2020-21 tax gaps by type of tax

HMRC estimates that the tax gap, in absolute terms, on Value Added Tax reduced, from 2019-20 to 2020-21, while most others increased



	2016-17	2017-18	2018-19	2019-20	2020-21
Value Added Tax (£bn)	12.1	11.0	9.5	12.5	9.0
Income Tax, National Insurance Contributions, Capital Gains Tax (£bn)	11.5	11.4	11.9	11.4	12.7
Corporation Tax (£bn)	5.3	5.7	5.7	5.5	5.6
Excise duty (£bn)	3.3	2.9	3.3	3.3	3.5
Other taxes[3] (£bn)	1.4	1.6	1.7	1.7	1.4
Net tax gap[1] (£bn)	33.6	32.6	32.1	34.4	32.2
Total tax gap as a percentage of total tax due (%)	5.6	5.2	4.9	5.1	5.1

Notes

1 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. The net tax gap is the remaining tax gap after HMRC has deducted the money it brings in through compliance activities.

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

3 '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 Historically, HMRC has measured the effectiveness of its compliance and enforcement activities through compliance yield – that is, the estimate of the additional revenues that HMRC considers it generated, and the revenue losses it prevented. HMRC is currently working to widen its measurement framework to take into account a broader set of key metrics that include harm prevention and customer experience. HMRC's aim is to embed a more cross-cutting and outcome-focused performance measurement framework with concepts such as fairness and harm reduction complementing the more traditional measures of its effectiveness at closing the tax gap. Compliance yield remains one of the few measures HMRC can apply consistently across many areas and it remains a key measure used to inform discussions with HM Treasury about funding for compliance work.

1.24 Total compliance yield in 2021-22 of £30.8 billion was 1.1% up on 2020-21 levels (£30.4 billion) but remained below pre-pandemic levels (16.7% less than in 2019-20). The average compliance yield over the past five years was £32.5 billion. The compliance yield increased for two of the six categories compared with the previous year and decreased for the other four (**Figure 4** on pages R22 and R23). HMRC explained that the changes were due to a wide variety of factors, including economic conditions, resourcing decisions and natural year-on-year fluctuations.

HMRC told us that its strategy of focusing more on preventing non-compliance reduced the impact of COVID-19 on compliance yield because this was now less reliant on HMRC investigating cases of non-compliance. HMRC generated compliance yield from preventative work (which it categorises as 'upstream product and process' and 'upstream operational') of £9.3 billion in 2021-22, up from £9.0 billion in 2020-21.

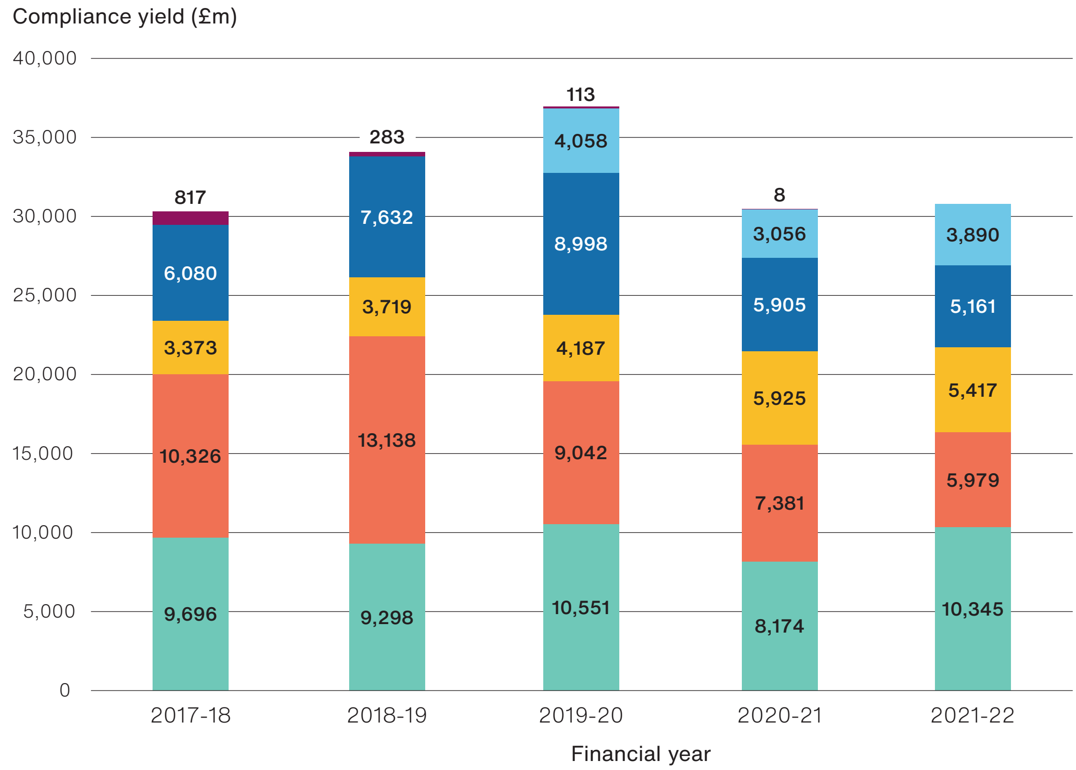
1.25 HMRC usually agrees a target for compliance yield with HM Treasury each year. HMRC has not set a target since 2020-21 because of the uncertainty caused by the pandemic and the need to respond quickly to urgent government priorities. Instead, from summer 2020, HMRC published forward-looking performance 'expectations' for yield for each quarter, starting with quarter two. HMRC told us that it set these expectations to help it manage its performance, rather than as an accountability mechanism. Targets will be reintroduced in 2022-23.

1.26 COVID-19 had a significant impact, both directly and indirectly, on the tax compliance landscape. The pandemic limited HMRC's ability to visit taxpayers to carry out its compliance investigations. In addition, it had fewer staff working in its compliance group because it redeployed on average 1,442 (6%) of its compliance staff to work on COVID-19 measures. In 2021-22, HMRC opened 265,000 investigation cases and closed 256,000. This is an increase in opened and closed cased compared with 2020-21, but represents a reduction of 97,000 (27%) open cases and 94,000 (27%) closed cases compared with 2019-20 before the pandemic.

Figure 4

Compliance yield performance by category between 2017-18 and 2021-22

Compliance yield reported by HM Revenue & Customs (HMRC) in 2021-22 is consistent with the prior year but remains below levels it reported before the pandemic



	2017-18	2018-19	2019-20	2020-21	2021-22
Total yield (£m)	**30,292**	**34,070**	**36,948**	**30,450**	**30,792**
Percentage change (%)	–	12.5	8.5	-17.6	1.1

- Accelerated payments
- Upstream operational yield
- Future revenue benefit[2]
- Upstream product and process yield
- Cash expected
- Revenue losses prevented

Figure 4 *continued*

Compliance yield performance by category between 2017-18 and 2021-22

Notes

1 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.
- 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 became 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 losses 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.

2 HMRC reports future revenue benefit in the year it has an impact on the Exchequer rather than in the year of the compliance intervention. In recognition of the economic impact of COVID-19, HMRC reduced the future revenue benefit brought forward into 2021-22 by £744 million.

3 In 2021-22, HMRC no longer included yield from accelerated payments as a separate category. Accelerated payments are incorporated within cash expected and upstream product and process yield from 2021-22.

4 Totals for 2019-20 and 2020-21 do not sum due to rounding.

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

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

1.27 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. **Figure 5** overleaf shows the returns on HMRC's funding of its compliance activities across the different segments of the taxpayer population. HMRC prioritises its compliance resources in order to ensure sufficient coverage of each area to maintain levels of voluntary compliance. It recruited a further 4,200 full-time equivalent compliance staff in 2021-22 who will complete their training in 2022-23.[9]

1.28 HMRC told us that, because of the wide range of its compliance interventions, its mix of activity will change year on year, with the nature of cases opened and closed varying in complexity and duration. For that reason, HMRC considers compliance yield rather than levels of activity to be the key measure of compliance performance. HMRC assesses the risks to the tax base on a regular basis and allocates its compliance activity in line with the risks. Ultimately, HMRC's compliance activities are limited by the resources available to it and not by the number of cases suitable for investigation. In that respect, HMRC does not consider there to be a backlog in compliance cases as a result of the pandemic. Rather, it has made judgements about the number of investigations to open during the pandemic period, based on prioritisation of resources and compliance risk.

9 HMRC's Customer Compliance Group, responsible for the department's enforcement and compliance activities had an average of 25,899 full-time equivalent in 2021-22.

Figure 5

HM Revenue & Customs' (HMRC's) returns from its compliance activities by customer group in 2020-21 and 2021-22

HMRC generates the highest returns from its compliance work on large businesses

Taxpayer group	2020-21				2021-22			
	2019-20 tax gap estimate	Costs of compliance activities	Yield	Rate of return	2020-21 tax gap estimate	Costs of compliance activities	Yield	Rate of return
	(£m)	(£m)	(£m)	(Yield per £ spent)	(£m)	(£m)	(£m)	(Yield per £ spent)
Individuals	2,600	410	2,600	6.3	2,500	410	2,700	6.6
Wealthy individuals	1,500	190	3,000	15.8	1,500	220	2,500	11.4
Small businesses	15,100	480	5,300	11.0	15,600	550	7,600	13.8
Mid-sized businesses	5,000	260	3,100	11.9	3,900	270	3,500	13.0
Large businesses	6,100	220	13,200	60.0	3,600	260	10,200	39.2

Notes

1 The yield and cost data do not necessarily directly correlate to each other due to timing differences. While the costs relate to the financial year under consideration, the yield will be the outcome of activities that cover a number of years.

2 The total yield shown in this figure (£26.5 billion in 2021-22) is only a subset of the total yield reported by HMRC (£30.8 billion in 2021-22 as shown in Figure 4). HMRC also reports yield from other types of activity – for example, those targeting criminals.

3 The figures presented in this table are in nominal terms. Tax gap and yield figures are estimates.

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

Customer service performance

1.29 This section considers HMRC's customer service performance in 2021-22 and the operational factors affecting it. It also sets out the latest developments in the measurement of its customer service performance. HMRC's post and call handling fell considerably during the pandemic and has resulted in a significant backlog of correspondence it is working through, but satisfaction with digital services has been broadly maintained. HMRC had to take action, including deploying staff from other parts of its customer service, to improve performance in dealing with correspondence. While this had some success, it resulted in a general fall in performance across some of the other measures in the last quarter of 2021-22.

HMRC's new customer service performance measures

1.30 HMRC has developed new performance measures to provide a broader overview of the customer experience. The new measures seek to address how easy or hard it is for taxpayers to access services, and whether HMRC has helped taxpayers to resolve their queries. These measures are now HMRC's principal means of evaluating customer service performance. There are five customer service performance metrics in HMRC's Outcome Delivery Plan to enable it to measure its performance against its strategic objectives (**Figure 6**).[10]

Figure 6

HM Revenue & Customs' (HMRC's) key customer service performance measures

HMRC has five customer service-related measures to gauge its performance against departmental strategic objectives

Measure	Purpose of measure	Definition and calculation of the measure	Relevant strategic objective
Net Easy – phone, webchat and digital	A direct feedback measure to provide a customer view of the ease of dealing with HMRC.	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.	Make it easy to get tax right and hard to bend or break the rules.
Percentage of telephony adviser attempts handled	A measure of HMRC's performance in supporting its customers via its phone lines.	The proportion of callers who got through to an adviser after hearing the automated messages and choosing the option to speak to an adviser.	
Percentage of webchat adviser attempts handled	A measure of HMRC's performance in supporting its customers via its webchat.	The proportion of customers taking up a webchat offer that successfully got through to a webchat adviser.	
Perentage of customer correspondence responded to within 15 working days of receipt	A measure of HMRC's performance in responding to post and iForms.	Targeted post and iForms cleared within 15 days divided by total targeted post and iForms received. The day of receipt is counted as day zero.	
Customer satisfaction with phone, webchat and digital services	A direct feedback measure to provide a customer view of their satisfaction of dealing with HMRC.	A measure of the percentage of HMRC customers that responded that they were either 'satisfied' or 'very satisfied' with the service.	Maintain taxpayers' consent through fair treatment and protect society from harm.

Source: HM Revenue & Customs Outcome Delivery Plan: 2021 to 2022

10 HMRC's 2021-22 Outcome Delivery Plan is available at: www.gov.uk/government/publications/hm-revenue-and-customs-hmrc-outcome-delivery-plan/hm-revenue-and-customs-outcome-delivery-plan-2021-to-2022--2

1.31 HMRC told us that its new customer service measures, introduced in response to a Committee of Public Accounts recommendation in November 2018, will better capture the experience of taxpayers in their interactions with HMRC. These new customer experience measures are one of the ways it plans to embed its revised Charter in its day-to-day activity.[11] The November 2020 Charter sets out the standards of behaviour and values customers can expect from HMRC. To support the Charter, HMRC has set principles for the support it will provide for customers who need extra help.

Performance in 2021-22

1.32 As with compliance yield (paragraph 1.25), HMRC did not set performance targets for customer service in 2021-22. Instead, it set quarterly performance expectations for five customer service measures for the quarter ahead to benchmark its performance. HMRC told us that performance targets will be re-introduced in 2022-23. The impact of COVID-19 on HMRC's customer service operations persisted throughout 2021-22. HMRC's actual performance was mostly below expected levels (**Figure 7**).

1.33 HMRC's performance on handling taxpayers' post was particularly poor because it had to deal with a large volume of items that had built up during the pandemic. In October 2021, it took steps, including redeployment of resources from other areas of its customer service, to recover its performance on handling of correspondence. The recovery in handling post came at the expense of a fall in performance across some of the other measures.

1.34 Customer correspondence performance saw a steady improvement over the year from 34.5% in the first quarter to 54.5% in the last quarter, although overall performance remains below expectations. Performance against Net Easy and Telephony saw reductions in the second half of the year reflecting HMRC's redeployment of resources; Net Easy moved from 64.0 in the third quarter to 62.6 in the last quarter and Telephony from 82.3% to 73.7% (Figure 7). HMRC's correspondence recovery plan has had some success in bringing down the volume of correspondence on hand from a peak of 3.3 million in July 2021 to 1.9 million by March 2022.

1.35 While HMRC has introduced a new set of customer service measures, it has continued to report its performance against its old, mainly response time, measures. HMRC will not, however, set any targets or performance expectations for its old set of measures. Previously, HMRC has used eight key measures to report its customer service performance (**Figure 8** on page R28). HMRC's reported data show that its performance has declined for all measures since 2018-19 except for customer service satisfaction for digital services which improved over the period from 80.4% to 83.4%. Customer service satisfaction, however, was slightly down from last year's peak of 85.2%.

11 HMRC's Charter is available at: www.gov.uk/government/publications/hmrc-charter

Figure 7

HM Revenue & Customs' (HMRC's) quarterly performance in 2021-22 for five key customer service measures

HMRC achieved nine of the 20 quarterly performance expectations it set for 2021-22 in respect of customer service

Measure		April to June	July to September	October to December	January to March
Net Easy – phone, webchat and digital services[3]	Outturn	68.2 (green)	67.5 (amber)	64.0 (amber)	62.6 (amber)
	Performance expectation	67.0	69.0	68.0	64.0
Telephony adviser attempts handled[4]	Outturn	74.3% (green)	80.3% (amber)	82.3% (green)	73.7% (amber)
	Performance expectation	72.0%	82.0%	80.0%	80.0%
Webchat adviser attempts handled[4]	Outturn	92.1% (green)	92.3% (green)	92.6% (green)	98.3% (green)
	Performance expectation	90.0%	92.0%	92.0%	95.0%
Customer correspondence (post and iForms) cleared within 15 working days of receipt[5]	Outturn	34.5% (red)	46.6% (red)	43.4% (red)	54.5% (red)
	Performance expectation	62.0%	57.0%	55.0%	69.0%
Customer satisfaction with phone, webchat and digital[6]	Outturn	83.4% (green)	82.9% (amber)	81.2% (amber)	80.9% (green)
	Performance expectation	81.0%	84.0%	83.0%	80.0%

Notes

1 Colour key: green – outturn exceeded expectation; amber – outturn below expectation but within 10%; red – outturn more than 10% below expectation.

2 For 2021-22, HMRC did not set targets due to the uncertainty around the COVID-19 pandemic and the need to respond quickly to urgent government priorities. Instead, it forecast expected quarterly performance.

3 The scope of the Net Easy measure changed for 2021-22 to include phone services as well as webchat and digital channels so there is no comparable 2020-21 data.

4 'Telephony adviser attempts handled' and 'Webchat adviser attempts handled' are new measure for 2021-22.

5 The customer correspondence measure now includes iForms and post, which were recorded separately in previous years.

6 The scope of the customer satisfaction measure has changed for 2021-22 to include phone services as well as webchat and digital channels so there is no comparable 2020-21 data.

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

Figure 8

HM Revenue & Customs' (HMRC's) customer service performance, 2018-19 to 2021-22

All customer services performance measures have been declining although customer satisfaction for digital services was broadly maintained

Measure	2018-19 outturn	2019-20 outturn	2020-21 outturn	2021-22 outturn	Performance trend
Average speed of answering calls to HMRC helplines (queue time in minutes)[1]	05:14	06:39	12:04	12:22	Declining
Customers waiting more than 10 minutes to speak to an adviser[1]	19.7%	29.9%	44.7%	46.3%	Declining
Post responded to within 15 days[2]	76.6%	70.3%	64.4%	39.5%	Declining
Post responded to within 40 days	96.4%	88.0%	85.3%	60.0%	Declining
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	Declining
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	Declining
Customer satisfaction for digital services[3]	80.4%	81.6%	85.2%	83.4%	Improvement halted in 2021-22
iForms and secure emails replied to within 7 days[2]	94.1%	87.6%	70.4%	64.6%	Declining

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. Average speed of answering customer-facing telephone numbers in 2021-22 was 12:59 minutes. On these telephone numbers, 49.2% of customers waited more than 10 minutes to speak to an adviser.

2 In 2021-22, the customer correspondence measure includes iForms and post, which were recorded separately in previous years. 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

Part Two

Employment support schemes: error and fraud

2.1 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 the two main COVID-19 support schemes: the Coronavirus Job Retention Scheme (CJRS) and the Self-Employment Income Support Scheme (SEISS).

2.2 The C&AG has qualified his opinion on the regularity of HM Revenue & Customs' (HMRC's) 2021-22 financial statements due to the material levels of error and fraud in CJRS and SEISS.

2.3 The explanation for the qualified opinion for these areas of expenditure is supported by:

- an overview of HMRC's estimates for error and fraud for 2021-22, its revised estimates for 2020-21 and the limitations of those estimates; and
- progress that HMRC is making in recovering overpayments arising from error and fraud in the schemes.

2.4 In autumn 2022, we plan to report on HM Treasury and HMRC's management of CJRS and SEISS, including the effectiveness of work to tackle error and fraud.

Qualification of the C&AG's audit opinion on the regularity of the COVID-19 support schemes

2.5 Under the Government Resources and Accounts Act 2000, the C&AG is required to obtain enough evidence to give reasonable assurance that the expenditure and income recorded in the financial statements have been applied for 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).

2.6 The legislative basis for the schemes is the Coronavirus Act 2020, Section 76, which gave HM Treasury powers to direct HMRC "to have such functions as the Treasury may direct in relation to coronavirus or coronavirus disease". After the Coronavirus Act 2020 received Royal Assent on 25 March 2020, HM Treasury issued a series of directions for each phase of the two schemes, setting out the scope and eligibility criteria.[12] Where error and fraud results in overpayment or underpayment to grant recipients who were either not entitled to support or were paid at a different rate from that specified in the HM Treasury directions, the transaction does not conform with Parliament's intention and is irregular.

2.7 Note 4.1 of HMRC's Resource Accounts sets out its estimates of the level of error and fraud present in each of the schemes for the 2021-22 reporting period as well as its revised estimates for 2020-21, which was the first full year in which the schemes operated. For both years, HMRC provides a range, with an upper, most likely and lower estimate. HMRC's most likely estimates are set out in **Figure 9**.[13] In November 2021, HMRC first published estimates of error and fraud in relation to scheme payments made in 2020-21 in its Annual Report and Accounts.[14] It plans to publish final estimates for each scheme for both 2020-21 and 2021-22 in its 2023 publication of Annual Report and Accounts.

2.8 In forming his regularity opinion, the C&AG:

- evaluated the control processes HMRC has designed and implemented to prevent and detect error and fraud in the schemes, recognising the pace at which they were delivered and the resulting trade-offs between financial controls and making payments on a timely basis;
- considered the existence of other sources of information that provide evidence of the level of error and fraud present in the schemes, for instance the results of HMRC's post-payment compliance processes; and
- evaluated the detailed input data, methodology, assumptions, and judgements applied by HMRC to produce its estimates and reviewed a sample of the compliance cases that informed HMRC's estimates.

2.9 Based on this work, the C&AG considers the level of error and fraud present in 2021-22 payments made for both CJRS and SEISS to be material and has qualified his regularity opinion in that respect. As set out below, HMRC's revised estimates for 2021-22 remain subject to a considerable level of uncertainty and, as a result, the actual levels of error and fraud in the schemes could differ significantly. HMRC's revised estimates for 2020-21 are also still subject to uncertainty.

12 HM Treasury directions for CJRS are available at: www.gov.uk/government/publications/treasury-direction-made-under-sections-71-and-76-of-the-coronavirus-act-2020; and for SEISS at: www.gov.uk/government/publications/treasury-direction-made-by-the-chancellor-under-sections-71-and-76-of-the-coronavirus-act-2020

13 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 full effects of post-payment compliance activity have been realised.

14 HM Revenue & Customs, *Annual Report and Accounts 2020 to 2021*, HC 696, November 2021.

Figure 9

HM Revenue & Customs' (HMRC's) current central estimate[1] of error and fraud in the main COVID-19 support schemes for 2021-22 and 2020-21

HMRC's current most likely estimates of the level of error and fraud in the main COVID-19 support schemes is £617 million in 2021-22 and £3,847 million in 2020-21

Scheme	2021-22			2020-21[1]			2021-22 and 2020-21 combined		
	Expenditure	HMRC's most likely estimate of the cost of error and fraud[2]	HMRC's most likely estimate of the rate of error and fraud	Expenditure	HMRC's most likely estimate of the cost of error and fraud[2]	HMRC's most likely estimate of the rate of error and fraud	Expenditure	HMRC's most likely estimate of the cost of error and fraud[2]	HMRC's most likely estimate of the rate of error and fraud
	(£m)	(£m)	(%)	(£m)	(£m)	(%)	(£m)	(£m)	(%)
Coronavirus Job Retention Scheme (CJRS)	8,201	241	2.8	60,677	3,218	5.3	68,878	3,459	5.0
Self-Employment Income Support Scheme (SEISS)	8,343	376	4.5	19,716	631	3.2	28,059	1,006	3.6
Total	**16,544**	**617**	**3.7**	**80,393**	**3,849**	**4.8**	**96,937**	**4,465**	**4.6**

Notes

1 HMRC also reports lower and upper estimates of fraud and error (Figure 10). We have derived the value of error and fraud by applying HMRC's current most likely estimate of error and fraud for each scheme to expenditure as reported in HMRC's accounts. Estimates for 2020-21 are revised, with estimates first published in HMRC's 2020-21 Resource Accounts.

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 most likely estimate 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. As net cost differs to the net expenditure figures reported in the Resource Accounts, it is not possible to derive HMRC's most likely estimate of the rate of error and fraud using the values included in this figure.

3 HMRC's estimates of the likely levels of error and fraud in CJRS are based upon a combination of the results 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 mixture of data from 2020-21 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 significant uncertainty.

Source: HM Revenue & Customs Resource Accounts 2021-22 and National Audit Office analysis of HM Revenue & Customs data

Estimated levels of error and fraud in the COVID-19 support schemes

2.10 HMRC told us that its priority from the start of the pandemic, as directed by ministers, was to get support to those who needed it as quickly as possible to protect jobs. As a consequence, while HMRC recognised that error and fraud were likely to occur in the COVID-19 support schemes, it understood that the pace of implementation, and the need to process payments quickly, would reduce its opportunities to mitigate error and fraud. In that respect, HMRC's strategy was based on preventing error and fraud before making payments whenever possible, and tackling abuse of the schemes through its compliance work after the payments were made.

2.11 In qualifying his regularity opinion on the schemes in 2020-21, the C&AG concluded that the controls implemented by HMRC were not adequate in preventing and detecting material levels of error and fraud. Based on our review of the controls implemented by HMRC in 2021-22, we remain of this view, which is borne out in the material levels of estimated error and fraud that HMRC has continued to report for the current year.

2.12 As set out in our 2020-21 report, HMRC's previous estimates of error and fraud were largely based on assumptions, with limited direct evidence available at the claim level to inform the estimates at that time. HMRC's 2021-22 estimates and revised 2020-21 estimates now take into account evidence gathered through a mandatory random enquiry programme, data from post-payment compliance work and analysis of Self Assessment tax return data, and to that extent the estimates now reflect direct evidence at the claim level. A description of HMRC's methodology and our view on the residual limitations of it are set out in paragraphs 2.14 to 2.18 for CJRS and paragraphs 2.19 to 2.23 for SEISS.

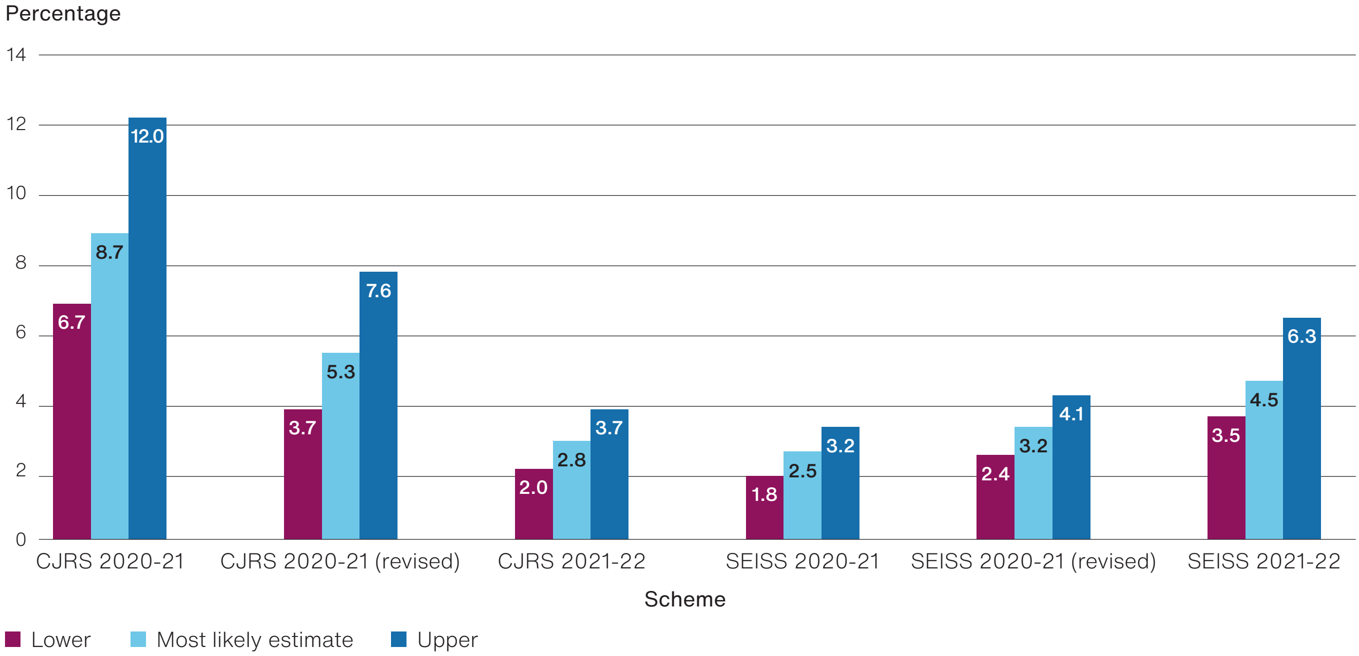
2.13 HMRC's statistical view is that its estimates provide 95% confidence that actual error and fraud lies within the upper and lower ranges it has calculated for each scheme. HMRC estimates that error and fraud in CJRS was in the range 2.0% to 3.7% in 2021-22, and 3.7% to 7.6% in 2020-21. For SEISS it estimates that error and fraud was in the range 2.4% to 4.1% in 2020-21 and 3.5% to 6.3% in 2021-22. HMRC's revised estimates for 2020-21 saw its estimate of error and fraud fall for CJRS as it reduced its estimate of fraud arising from employers claiming while employees were working. For SEISS, HMRC's revised estimate was higher, primarily because of the introduction of new eligibility conditions. The conditions aimed to reduce the cost of the fifth grant but also increased the risk of fraud as some claimants sought to avoid the conditions (**Figure 10** on pages R33 and R34).

Figure 10

HM Revenue & Customs' (HMRC's) estimates of the range of error and fraud in the two main COVID-19 support schemes for 2021-22 and 2020-21

HMRC's latest most likely estimate of error and fraud in the Coronavirus Job Retention Scheme (CJRS) in 2020-21 is 3.4 percentage points lower than it estimated in 2021 and for the Self-Employment Income Support Scheme (SEISS) in 2020-21 it is 0.5 of a percentage point higher than it estimated in 2021

Error and fraud ranges by scheme



Cost of error and fraud

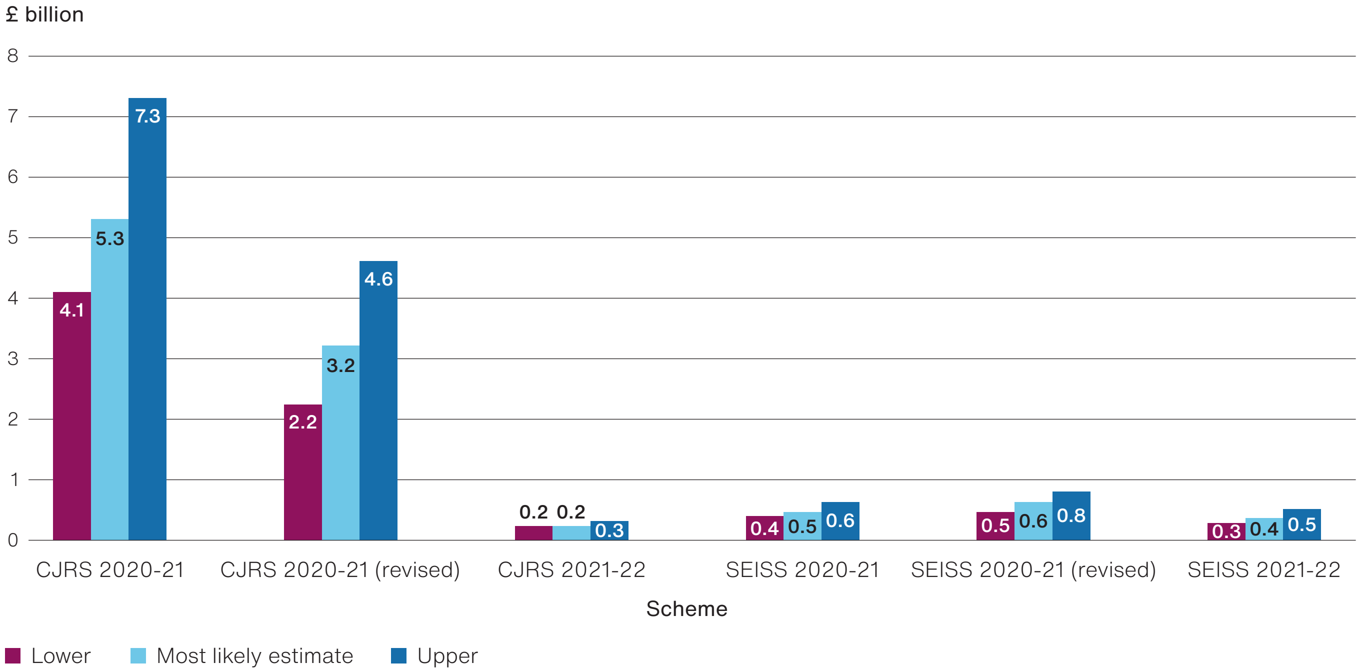


Figure 10 *continued*

HM Revenue & Customs' (HMRC's) estimates of the range of error and fraud in the two main COVID-19 support schemes for 2021-22 and 2020-21

Notes

1 HMRC also reports lower and upper estimates of fraud and error. We have derived the value of error and fraud by applying HMRC's current most likely estimate of error and fraud for each scheme to expenditure as reported in HMRC's accounts. The previous published range for CJRS in 2020-21 was 6.7% to 12.0%, the updated range is 3.7% and 7.6% with some overlap between the two ranges.

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 full effects of post-payment compliance activity have been realised.

3 HMRC's estimates of the likely levels of error and fraud in CJRS are based upon a combination of the results 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 mixture of data from 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 significant uncertainty.

Source: HM Revenue & Customs Resource Accounts 2021-22 and National Audit Office analysis of HM Revenue & Customs data

Coronavirus Job Retention Scheme (CJRS)

2.14 HMRC's current estimates of error and fraud present in CJRS are based on the results of a Mandatory Random Enquiry Programme (MREP), together with an estimated adjustment for employers claiming while employees were working, including those employees who did not know that they were being claimed for. Through the MREP, HMRC examined a sample of 490 CJRS claims, designed to assess most of the risks that it identified that could give rise to error, such as claimant mistakes, and fraud, including claimants intentionally inflating claims (paragraph 2.16). HMRC concluded that the MREP would not adequately detect working while claiming (WWC). It therefore made a separate estimate for this risk using its own data and external data, including surveys (paragraph 2.18).

2.15 The overall level of error and fraud reported by HMRC for CJRS brings the two components of the estimate together. Its estimate of error and fraud for 2021-22, comprises 1.1% for WWC and 1.7% for all other risks. For its 2020-21 estimate, the split is 3.6% and 1.7%. We reviewed both components of HMRC's estimates. HMRC classifies WWC as a mix of error – employers not understanding the rules – and opportunistic fraud – intentional rule breaking. It also classifies risks as error and organised crime (**Figure 11**).

Figure 11

HM Revenue & Customs' (HMRC's) current assessment of the nature of error and fraud present in the Coronavirus Job Retention Scheme (CJRS) in 2020-21 and 2021-22

HMRC's current estimates indicate that the error and fraud present in CJRS is mainly due to opportunistic fraud and error

	Estimated rates of the causes of error and fraud – most likely estimate (%)			
	Organised crime	Opportunistic fraud	Error	**Total**
Example of risks	Compromised accounts; organised labour fraud; fraudulent employments set up after CJRS announced in March 2020	Employees working while claiming furlough; inflated genuine claim	Error claimant's favour; error HMRC's favour (i.e., underpayment)	
Year				
2021-22	0.1	1.2	1.5	**2.8**
2020-21	0.2	2.5	2.6	**5.3**

Notes

1 Paragraph 2.16 explains issues in HMRC's mandatory random enquiry program (MREP) which increase uncertainty in the estimates of error and fraud HMRC has derived from it. We are not in a position to quantify the impact.

2 Causes of error and fraud are defined as follows: organised crime – organised criminals fraudulently accessing the schemes, either directly or through other businesses or individuals; opportunistic fraud deliberate manipulation of legitimate claims to access more funds than the recipient is entitled to, or to claim when ineligible; and errors – unintentional errors by either the claimant or HMRC resulting in underpayments or overpayments.

3 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 full effects of post-payment compliance activity have been realised.

4 HMRC's estimates of the likely levels of error and fraud in CJRS are based upon a combination of the results 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 the other tax and benefit streams that it administers.

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

Mandatory Random Enquiry Program

2.16 We identified the following issues in HMRC's MREP, which increase the uncertainty in the estimates of error and fraud HMRC has derived from it. We are not in a position to quantify the impact.

- The MREP only covers the period March 2020 to the end of October 2020 and the results have been extrapolated over the remainder of 2020-21. The results of the period July to October 2020 have been extrapolated over 2021-22. Accordingly, HMRC's estimate for 2021-22 assumes that the prevalence and factors giving rise to error and fraud did not change in the last 11 months of the scheme. HMRC is currently undertaking a second tranche of MREP cases and these cases have not been factored in to cover the period from the start of November 2020.
- The MREP included the risk of organised crime and non-payment of furlough to employees but caseworkers did not identify any instances of these because either these risks did not materialise or they were not detected by HMRC. We have subsequently established that cases with a risk of organised crime are investigated outside of the MREP.
- The MREP found few cases of underpayments. Case workers focused on identifying errors and fraud leading to overclaims. HMRC has told us that, in its view, it was easier for employers to submit a claim above what was allowable – misinterpretation of the rules or mistakes in calculation would be expected to result more often in an overclaim than an underclaim.
- HMRC's adjustment for non-detection of all errors in its sample of cases was not designed for CJRS, and it has been unable to assure us that it is appropriate for that purpose. It used the 20% adjustment it applies to its MREP covering small business compliance with Pay as You Earn (PAYE) and other obligations, but the risks of error and fraud, and non-detection, are likely to be different. CJRS was not an established tax but a new grant scheme potentially attractive to organised crime and paid at a time when businesses were under financial pressure. HMRC is considering developing a tailored adjustment for non-detection for its final estimate of CJRS error and fraud but it has not committed to doing so.
- HMRC recognises that its estimate for the level of fraud due to organised crime should be treated with caution. As its first MREP did not detect organised crime, HMRC drew on a panel of experts, its ongoing second MREP and post-payment compliance activities to estimate that organised crime led to fraud equivalent to 0.1 of a percentage point of CJRS spend in 2021-22, and 0.2 of a point in 2020-21. These sums are covered by HMRC's overall adjustment for non-detection.

- In 5% of 55 cases, we could not agree the overclaim amounts recorded by the caseworker in the specific phase of the CJRS to which they had been attributed and in 7% of cases an incorrect value for the errors recorded by the caseworker was included in the overall estimate calculation. In at least two other cases we were not able to agree the overclaim amounts to the underlying evidence because there was an insufficient audit trail. This may be indicative of further errors in the population of MREP cases not tested as part of the audit, which would have an effect on the error and fraud values reported by HMRC for 2020-21 and 2021-22. HMRC does not consider the impact of these errors and inconsistencies could have a material impact on the overall level of error and fraud reported.
- A subset of cases included in the MREP have not been investigated in full. For example, in some cases, only a selection of employees on a given claim have been investigated where there were many employees. HMRC's own analysis suggests that the impact of sub-sampling was limited. HMRC acknowledges that there is a residual risk of non-detection. It considers this is accounted for by both the non-detection adjustment and multiplier applied to the MREP results.
- Our evaluation of the errors identified suggests that the range about the most likely estimates of error and fraud for both 2020-21 and 2021-22 are likely to be wider than that reported by HMRC. The most likely estimate for 2020-21 could also be slightly understated.

2.17 Our review of a sample of MREP cases also found that it is unlikely to provide an accurate split between overpayments arising from error and those arising from fraud (Figure 11). Where HMRC's caseworkers identified overpayments, they had to judge whether the evidence was sufficient to prove that the claimant had deliberately overclaimed and, therefore, whether further action needed to be taken, including applying penalties. This judgement included consideration of the resource requirement needed to gather that evidence and the appropriateness of that action. If HMRC were not able to demonstrate fraudulent behaviour, the overpayment was recorded as an error because HMRC was not able to meet the high evidence bar required to record the case as fraudulent. Our autumn 2022 report will cover HMRC's compliance programme and explore this issue further (paragraph 2.4).

Working While Claiming

2.18 WWC accounts for around two-thirds of HMRC's total estimate of CJRS error and fraud across the scheme's 18-month life. HMRC's latest estimates for WWC rely on many of the same sources of input data, methods and assumptions it used in its initial estimates made in 2021, including external survey data and its own survey data. For the current estimates, HMRC has also used the results of post-payment compliance work to inform the WWC estimate. Accordingly, while some improvements have been made to HMRC's WWC estimate, there remain some limitations and uncertainties:

- The external survey data HMRC used was not designed specifically to develop the estimate. Interpreting and applying the survey results in that context involved significant judgements that HMRC sought to mitigate by considering different data sources and expressing uncertainty in the range of outcomes from its model.
- HMRC's estimate of the prevalence of WWC is based on partial data. HMRC's estimate is underpinned by data from the external April 2020 Understanding Society survey, triangulated with other survey data, covering all or part of the period from the start of CJRS to June 2020 and HMRC's own data.[15] Different surveys found rates of WWC that were both higher and lower than the April 2020 Understanding Society survey suggested. The survey gave an estimate of WWC that was central in comparison to this range. HMRC had no survey data for the 15-month period of flexi-furlough starting in July 2020. Flexi-furlough altered the risks of WWC. Under flexi-furlough, it was likely to be easier to disguise when furloughed staff were working and being paid by their employer for some of their hours, but the amount overclaimed for each employee was likely to be less.
- HMRC's adjustment for those furloughed staff legitimately undertaking training and volunteering is based on a survey it commissioned covering the period March 2020 to June 2020. The survey was undertaken to estimate the working while furloughed risk and the proportion of CJRS claimants completing allowable work. HMRC did not repeat this survey for the other 15 months of the scheme.
- To estimate overpayments from WWC in the period to the end of June 2020, HMRC used a 'scenario-based analysis'. This analysis includes the most frequent WWC scenario of people who admitted to working 'a little'. HMRC's own assessment of the assumptions used in its analysis is that they should be treated with caution. NAO's analysis tested the assumptions made by HMRC and produced an increase in the most likely estimate of WWC for 2020-21 of 0.8%. HMRC and NAO agree, however, that the difference in the methodological approaches would not result in a material difference in the estimate of error and fraud.

15 The UK household longitudinal study, available at: www.understandingsociety.ac.uk/

- To estimate overpayments from WWC under flexi-furlough, HMRC used post-payment compliance data. It has made a methodological choice in analysing this data, which reduces the most likely estimate of WWC for 2020-21 by 0.4 of a percentage point. It opted to use the average overclaim as a proportion of the average total claim figure from the claims it has analysed, rather than the average proportion of the claim that is overclaimed. HMRC considers its approach more appropriate for the purposes of the calculation.

Self-Employment Income Support Scheme

2.19 HMRC's 2021-22 and revised 2020-21 estimates of error and fraud for SEISS are based on what it describes as a 'blended approach' with an assessment made and value attributed to each of the risk categories that it identified could give rise to error or fraud. This mainly involved analysing 2019-20 and 2020-21 Self Assessment tax return data to determine the extent of overpayments that may have arisen when claimants were not eligible – for instance, because they were not trading or intending to trade; or manipulating their trading results inflated their entitlement or suggested that the pandemic had had an adverse on them. HMRC's estimates also involved behavioural analysis of claimants using tax return data to assess the risk of organised crime. It also includes errors that HMRC may have made in notifying claimants of their entitlement to SEISS.

2.20 The risk categories HMRC identified which could give rise to error or fraud in SEISS payments are consistent with those applied in its 2020-21 estimates and comprise:

- **Organised crime** – deliberate illegitimate claims arising from criminal action.
- **Opportunistic fraud** – in the scenarios identified as risky HMRC sought to obtain evidence of incorrect payments from a range of data sources. This risk is further broken down into three sub-risks as follows:
  - 'Boundary Pushers' for those seeking to manipulate their income or profits to claim SEISS.
  - 'Not trading or intending to trade' for those not trading but knowingly claiming SEISS.
  - 'Not adversely affected' covering instances whereby SEISS was claimed but the more rigorous test for declaring adverse impact were not legitimately met, including those where a Financial Impact Declaration (FID) has been made by the claimant for SEISS 5, but where contradictory evidence is available from the information in Self Assessment returns.
- **Official error** – identifies errors that HMRC has made computing the grant available to claimants.

2.21 HMRC's most likely estimate of error and fraud for 2021-22 covering phases 4 and 5 of the SEISS scheme is £376 million or 4.5% of scheme payments. It's revised most likely estimate for the first three phases of the scheme was £631 million or 3.2% of scheme payments.

2.22 HMRC's estimates indicate that the value and percentage of error and fraud in relation to each of the risks it identified have changed between the first three phases of the grant (SEISS 1 to 3) and the last two phases (SEISS 4 and 5) as new controls were introduced. In the latter phases of the scheme, the eligibility criteria were tightened to introduce a 'reasonable belief test', which required positive attestation that the claimant had been adversely affected, together with a FID. HMRC's analysis suggests that this reduced the take-up of grants by claimants and, in that respect, may have deterred fraudulent or erroneous claims. HMRC's most likely estimate against each risk of error and fraud is set out below in **Figure 12**.

Figure 12

HM Revenue & Customs' (HMRC's) current assessment of the nature of error and fraud present in the Self Employment Income Support Scheme (SEISS) in 2020-21 and 2021-22

HMRC's current estimates indicate that error and fraud present in SEISS are mainly due to opportunistic fraud[1]

	Estimated rates of the causes of error and fraud – most likely estimate (%)			
	Organised crime	Opportunistic fraud[3]	Error[4]	Total
Example of risks	Compromised accounts	Claimants manipulating their income or profits to increase SEISS grant or become eligible; claimants not trading or intending to trade	Errors HMRC made in calculating grants	
Year				
2021-22	0.4	2.3	1.8	**4.5**
2020-21	1.1	1.1	1.0	**3.2**

Notes

1 Causes of error and fraud are defined as follows: organised crime – organised criminals fraudulently accessing the schemes, either directly or through other businesses or individuals; opportunistic fraud – deliberate manipulation of legitimate claims to access more funds than the recipient is entitled to or to claim when ineligible; and errors – unintentional errors by either the claimant or HMRC resulting in underpayments or overpayments.

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 full effects of post-payment compliance activity have been realised.

3 HMRC's most likely estimate of the level of opportunistic fraud assumes that there was no fraud arising from the reasonable belief test introduced in SEISS 3.

4 HMRC calculates SEISS grants for the claimant and thus there is no claimant error in its estimates. HMRC have also not identified any errors made in their own calculations.

5 HMRC's estimates of the likely levels of error and fraud in SEISS are based upon modelling using a mixture of data from Self Assessment tax returns, insights from HMRC administrative data and post-payment compliance outputs.

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

2.23 Based on our review of the methodology, input data and key judgements and assumptions HMRC has applied in producing its estimates, we consider the approach to be reasonable overall. However, there remain some limitations and areas of estimation uncertainty, notable examples of which are set out below. HMRC has sought to address this uncertainty through the upper and lower ranges it has reported in respect of the estimates.

- HMRC estimates that the error and fraud arising from claimants who were not affected by COVID-19 according to the ‘reasonable belief test’ but went on to claim support, was up to 0.5% in SEISS 3 and up to 0.7% in SEISS 4 and 5. According to the evidence available, HMRC assessed that the most likely estimate was negligible for the risk associated with the ‘reasonable belief test’. These assessments are based on a large volume of internal and external data, however, some uncertainty remains. An approach using direct evidence at the individual claim level, such as a random enquiry programme, may be more effective given that claimants were asked to retain evidence of how their business had been affected. HMRC is now pursuing this approach.

- The 2021-22 estimate relies upon the results of HMRC’s analysis of 2020-21 Self Assessment tax returns because 2021-22 returns are not yet available. The 2021-22 estimate, therefore, has to include some assumptions around claimant income and behaviour in the later tranches of the scheme. For example, the results of compliance campaigns into those who had received a SEISS grant but had either ceased trading, not submitted a 2019-20 or 2020-21 tax return, or done so without a trade page, were used to make predictions about claimant behaviour.

- Our audit identified some instances where the assumptions made by HMRC appear to be overly prudent. For example, for the ‘not trading or intending to trade’ risk, HMRC’s estimates assume that, if a claimant has incorrectly claimed one of the grants, then the other grants are also erroneous (which would not necessarily be the case because the claimant may have started a new trade in-between grants or have the intention to trade and thus be eligible for subsequent grants).

- The categories of risk and the risks themselves described in paragraph 2.20 are not mutually exclusive. As a result, HMRC has had to use the available data and apply judgement to determine the extent of the overlap between risks, to adjust for double counting of error and fraud. The overlaps identified are assessed as not material, and while there is some residual uncertainty, HMRC does not consider that this will have a material effect on the reported error and fraud estimates.

- HMRC has not made a separate estimate of the level of underpayments arising from claimant error. HMRC told us the purpose of its estimate of error and fraud is to identify the value of error and fraud that is available for post-payment compliance recovery, or that has already been recovered through compliance activity. For this reason, underpayments have not been included within the estimate. Underpayments are more likely to be a feature of SEISS 5 due to the introduction of the FID test and the two different levels of grant available in that tranche. We found that HMRC has identified some underpayments in the population of those who received SEISS 5 grants and that it has developed a mechanism to uplift the payment of those who incorrectly claimed the lower level of grant, which is indicative of the risk of underpayments. As with the 'reasonable belief test', we consider that the use of direct evidence at claim level would be a more robust method of estimating the level of residual underpayments in the claimant population.

Recovery of losses arising from error and fraud in the COVID-19 support schemes

2.24 The Committee of Public Accounts raised concerns about the level of ambition in HMRC's plans to recover error and fraud in the COVID-19 support schemes and asked it to take a number of steps to address those concerns.[16] In doing so, the Committee requested that HMRC:

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

16 Committee of Public Accounts, *Thirty-Seventh Report of Session 2021–22, HMRC Performance in 2020–21*, HC 641, February 2022.

2.25 HMRC set out its response to the Committee of Public Accounts' recommendations in a Treasury Minute in April 2022.[17] This set out its expectation that it would recover between £800 million and £1 billion up to the end of 2022-23. It confirmed that it would continue prioritising the most egregious cases of abuse but would not be actively searching for people who have made an honest mistake. It also continues to report repayments of grant made either voluntarily or through HMRC campaigns to prompt individuals to return overpayments.

2.26 HMRC's 2021-22 Trust Statement includes £73 million it recovered through assessments raised against companies liable for Corporation Tax where they had over-claimed CJRS. The Trust Statement includes a further £67 million recovered through assessments raised in relation to income tax. HMRC has not been able to identify how much of the £67 million recovered through self-assessment returns relates to each of the schemes.

2.27 HMRC has recovered a further £555 million in 2021-22 through voluntary repayments, prompts from HMRC or unprompted repayment of overpayments arising from errors made by claimants. The split by scheme is as follows:

- £526 million for CJRS;
- £28 million for SEISS; and
- £0.7 million for Eat Out to Help Out.

17 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.

Part Three

Personal Tax Credits and Corporation Tax research and development reliefs

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) expenditure and Corporation Tax research and development reliefs.

3.2 The C&AG has qualified his opinion on the regularity of HM Revenue and Custom's (HMRC's) 2021-22 financial statements due to the material level of error and fraud in tax credits expenditure and Corporation Tax research and development reliefs.

3.3 The explanation for the qualified opinion for each of these areas of expenditure is supported by:

- an overview of HMRC's estimates for tax credits and Corporation Tax research and development reliefs error and fraud;
- the causes of, and development in tackling, error and fraud in each of these areas of expenditure; and
- an update on progress on the replacement of tax credits with Universal Credit and the improvements HMRC is making to its estimates of error and fraud in Corporation Tax research and development reliefs.

Personal Tax Credits

3.4 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.

3.5 In 2021-22, HMRC spent £10.6 billion on tax credits, representing 18.4% of the total expenditure of £57.6 billion recorded in HMRC's 2021-22 Resource Accounts. Tax credits supported around 1.4 million families and around 2.7 million children.

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

3.6 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).

3.7 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 overpayment or underpayment of 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.

3.8 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 his audit opinion has been qualified on that basis.

3.9 The C&AG has considered the level of error and fraud in Child Benefit and concluded that this is not material in the context of his regularity opinion. The estimated rate of error and fraud in Child Benefit has increased to 0.9% (£105 million) of related expenditure of £11.4 billion for 2021-22 from 0.8% (£90 million) in 2020-21 (HMRC Resource Accounts). For 2021-22, the C&AG considers that this level remains immaterial with reference to the related expenditure.

Tax credits

3.10 Tax credits were introduced in 2003 and are designed to support families with children, tackle child poverty and help to make sure that work pays more than welfare. Tax credits awards are based on initial estimates and finalised 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 have been a significant challenge for HMRC, and have led to a qualified opinion every year since they were introduced. Tax credits are gradually being replaced by Universal Credit, which is administered by the Department for Work & Pensions (DWP).

3.11 Error and fraud have a real cost. Overpayments arising from error and fraud increase costs for taxpayers and reduce the public resources available for other purposes. Underpayments mean that claimants do not get the support they are entitled to.[18] Even where payment errors are later corrected, this can lead to additional administrative work and uncertainty for claimants.

Estimated level of error and fraud in tax credits

3.12 HMRC's latest estimate of the level of error and fraud in tax credits relates to 2020-21. This is because, under the normal tax credits annual cycle, awards for 2020-21 were finalised between April and July 2021 following the end of the tax year, or in January 2022 for claimants required to submit an Income Tax (Self Assessment) return. It is only after all claims are finalised that HMRC can complete the required testing to estimate the level of error and fraud.

3.13 HMRC estimates that in 2020-21, error and fraud resulted in overpayments of 5% of tax credits expenditure, the same as the overpayment rate initially reported in the previous year. The 2019-20 finalised figure has now been revised to 5.3% (**Figure 13** and note 5.1.3 to HMRC's Resource Accounts). Errors in tax credits resulting in underpayments amounted to 0.8% of expenditure, the same as the initial underpayment rate reported in the previous year, recently revised to 0.9%. These rates for 2020-21 equate to overpayments of £780 million from an estimated 400,000 claims (on average, £1,950 per claim), a reduction of £160 million compared with finalised 2019-20 estimates and underpayments of £120 million from an estimated 300,000 claims (on average, £400 per claim). HMRC revisits the estimates each year to take account of new information received after the original publication.

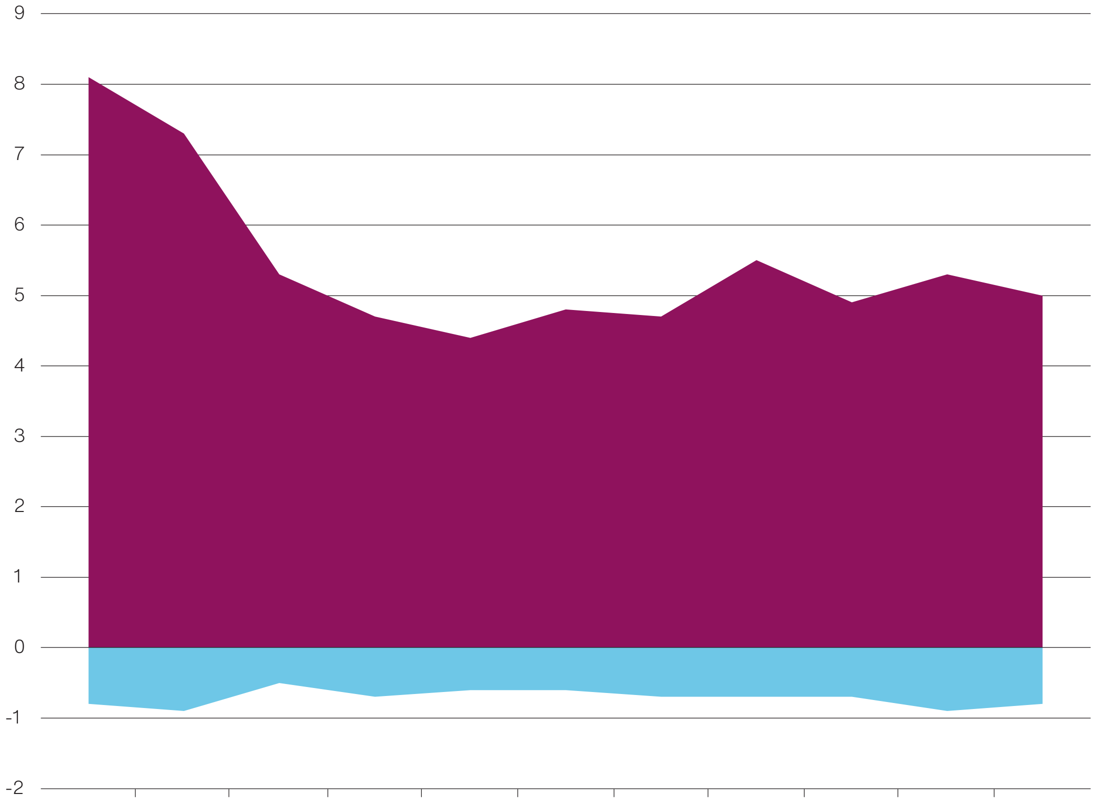
3.14 The estimated overpayment rate in 2020-21 of 5% was within HMRC's forecast range of 4.1% to 6.1%. HMRC analysis suggests that the tax credits population is becoming more stable due to the continued migration from the tax credits regime of those with frequent changes of circumstance whose claims present a higher risk of error and fraud.

3.15 In forming his opinion on the regularity of tax credits expenditure, the C&AG has considered whether the error and fraud rates for 2020-21 provide sufficient and appropriate evidence that error and fraud remain material issues in 2021-22. Based on its current forecasts, HMRC expects that the error and fraud rate will remain in the range of 4.5% to 5.5% for 2021-22, although the actual level of error and fraud will not be published until June 2023. The C&AG has, therefore, qualified his opinion based on HMRC's 2020-21 estimate and its forecast of error and fraud for 2021-22.

18 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 13
Overpayments and underpayments as a percentage of total tax credits expenditure, 2011-12 to 2020-21

HM Revenue & Customs' (HMRC's) most likely estimate of overpayments remained the same as initially reported in 2019-20 and has not been more than 5% for six of the last eight years. The 2019-20 finalised figure has now been revised to 5.3%



	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21
Overpayments (%)	8.1	7.3	5.3	4.7	4.4	4.8	4.7	5.5	4.9	5.3	5.0
Underpayments (%)	-0.8	-0.9	-0.5	-0.7	-0.6	-0.6	-0.7	-0.7	-0.7	-0.9	-0.8

Note

1 Estimates for 2020-21 are provisional. Final estimates will be published next year alongside the provisional 2021-22 estimates.

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

Causes of, and developments in tackling, error and fraud

3.16 HMRC categorises error and fraud into several different types to assess the main causes (**Figure 14**). It estimates that £200 million of overpayments are attributable to the income risk category in 2020-21, a reduction of £100 million from 2019-20. HMRC's analysis suggests that misreporting of income by claimants is now responsible for more than a quarter (26%) of overpayments, down from 35% in 2019-20. An estimated £175 million of overpayments are attributable to the undeclared partner risk category in 2020-21, the same as the revised figures for 2019-20.

3.17 COVID-19 has had a significant impact on the administration of tax credits as well as some impact on the levels of error and fraud. HMRC has identified a number of key factors relevant to its current estimate of error and fraud, including the following:

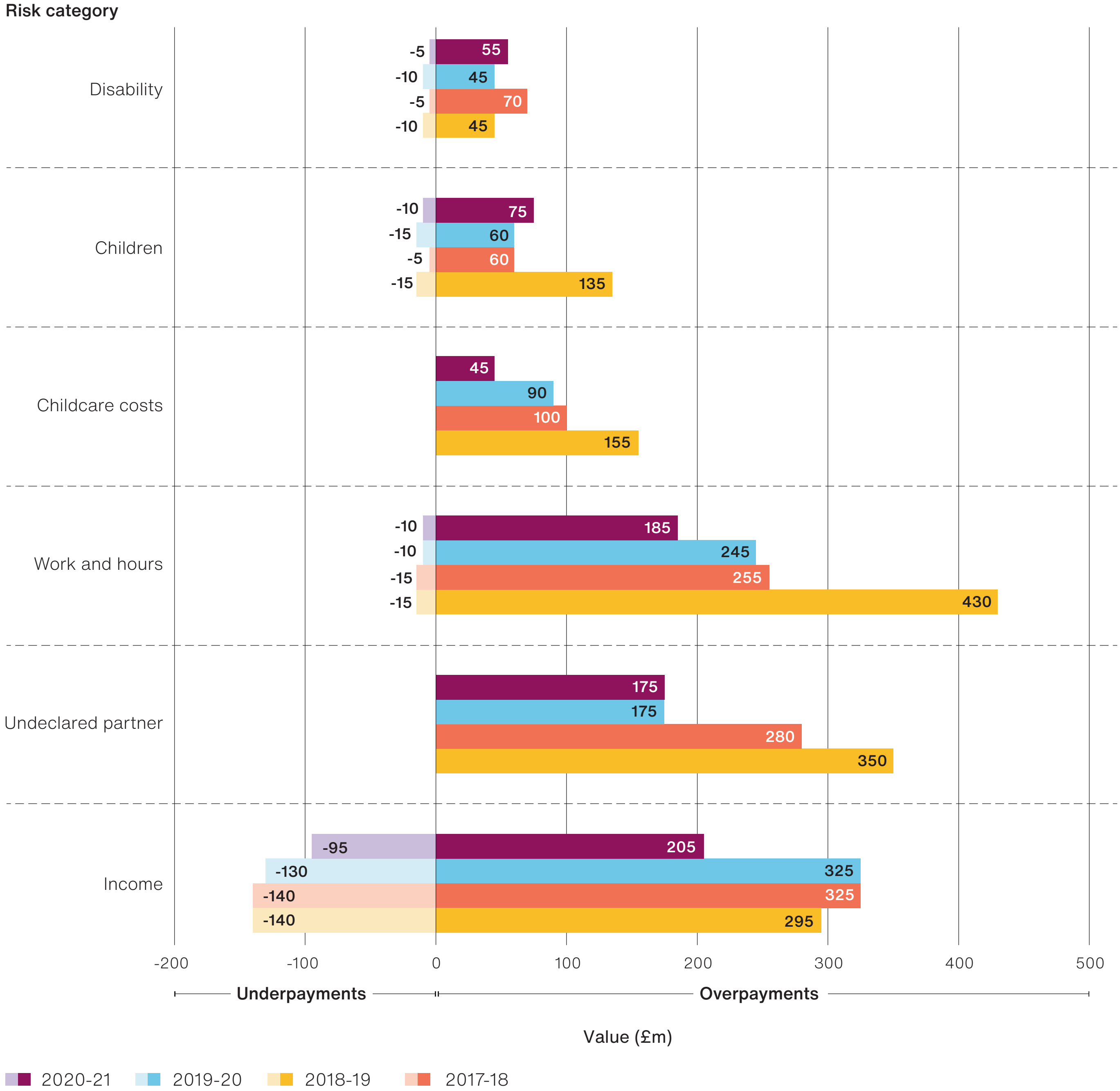
- Front-line compliance staff were redeployed to customer service work and the COVID-19 support schemes. HMRC's revised assessment of the impact this had on error and fraud in 2019-20 is £90 million.
- The decision to auto-renew all but the riskiest 35,000 claims is likely to have increased error and fraud by some £54 million in 2019-20 with some ongoing impact in 2020-21.
- HMRC introduced a legislative change to treat working tax credit claimants as being in paid employment and meeting the 'hours worked' rules when their normal work patterns changed during the pandemic. For the 2020-21 estimate reported here, this was expected to reduce reported error and fraud by some £46 million.

3.18 In 2021-22, the renewals process for tax credits returned to business as usual. HMRC used a mixture of automatic renewals for lower-risk claims and a manual process to update riskier claims where more intervention was required to update claim information. The impact of returning to business as usual on error and fraud will be reported in the 2022-23 Annual Report and Accounts when the data to measure this become available.

Figure 14

HM Revenue & Customs' (HMRC's) tax credits overpayments and underpayments by category for 2017-18 to 2020-21

The largest decrease in 2020-21, from 2019-20, was in HMRC's estimate of incorrectly disclosed income levels (£95 million reduction in overpayments), although this still remains the largest cause of error and fraud (overpayments £205 million, underpayments £95 million)



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

Future challenges

Replacement of tax credits by Universal Credit

3.19 The plans for Universal Credit to fully replace tax credits by the end of the 2024-25 financial year continue to progress (**Figure 15**). 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.

3.20 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.

3.21 The project for the migration of tax credits to Universal Credit resumed in January 2022 as the impact of the pandemic began to subside. HMRC has indicated that it remains on target to complete the transfer of all tax credits to Universal Credit by 2024-25. We will continue to monitor and report on the progress towards achieving this objective over the next three years.

Transfer of tax credits debt to DWP

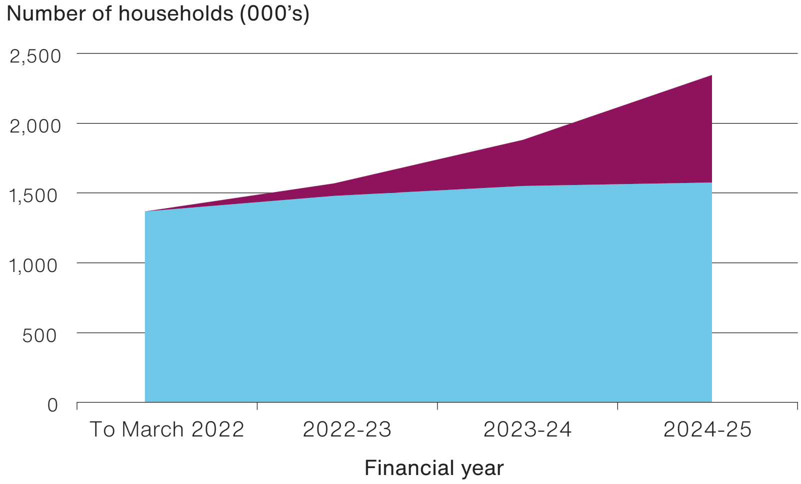
3.22 HMRC told us that it has successfully cleared the backlog of Personal Tax Credits debt transfers which arose from the joint decision with DWP to pause the transfer of tax credits debt to DWP at the start of the pandemic. HMRC restarted transfers in June 2021 and cleared the backlog of Universal Credit debt transfers within eight months.

3.23 Since tax credits debt started to transfer to DWP in 2016, a total of £3.4 billion of debt had transferred by the end of March 2022. HMRC's latest forecast suggests that a further £2.3 billion of debt is still to transfer. It is important that HMRC and DWP continue to work together to manage this process and ensure adequate records of this debt are transferred to enable recovery once the tax credit systems are shut down. HMRC expects to complete the transfer of all debts on the same timeline as the migration to Universal Credits by March 2025.

Figure 15

Planned transfer of tax credits claimants to Universal Credit (UC) by 2025

Most natural transitions have already taken place whereas most managed transitions through the Move to Universal Credit (UC) project will take place between 2022-23 and 2024-25



	To March 2022	2022-23	2023-24	2024-25
Move to Universal Credit (cumulative, 000's)	0	90	331	771
Natural Transitions (cumulative, 000's)	1,368	1,479	1,551	1,575

Notes

1 Numbers are for Great Britain only. Northern Ireland is not included.

2 Households moving from tax credits to Universal Credit may be single or joint claims.

3 Data to the end of March 2022 are actual transfers. Data from March 2022 are forecast values.

4 Values exclude 'nil awards', which will not be transferred and will be removed from HM Revenue & Customs' caseload.

5 Natural transitions to Universal Credit can occur when someone has a change of circumstances that means they would have to make a new claim for a benefit or credit (for example, their working hours fall below 16 hours a week). However, as people can, in general, no longer make a new claim for tax credits or other legacy benefits, they must make a claim for Universal Credit. Move to Universal Credit is the transfer of existing claimants of tax credits (and other legacy benefits) to Universal Credit.

6 The Department for Work & Pensions revised its methodology for forecasting transfers to Universal Credit in 2020. The new forecast incorporates more recent figures for the tax credits caseload and exits from in-payment tax credits and changes to the schedule of Move to Universal Credit transfers, accounting for the effects of the COVID-19 pandemic. This has caused a significant reduction in forecast transfers to Universal Credit since the equivalent figure was published in last year's report.

Source: National Audit Office analysis of HM Revenue & Customs, Department for Work & Pensions and Northern Ireland Department for Communities information

Corporation Tax research and development reliefs

3.24 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 seek to research or develop an advance in their field. There are two separate schemes: the SME scheme for small- or medium-sized enterprises; 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 cash tax credit paid by HMRC.

3.25 Both schemes are operated by HMRC in parallel with its administration of the Corporation Tax system, the revenues from which are reported in HMRC's Trust Statement. Expenditure on the schemes is reported in HMRC's Resource Accounts, which reflects that they, unlike most other types of tax relief, can result in cash payments (credits) to companies.

3.26 Note 5.1.4 to the Resource Accounts records expenditure incurred by HMRC on Corporation Tax research and development relief of £9.5 billion in 2021-22 (£9.3 billion in 2020-21). Of this, £3.6 billion (£3.8 billion in 2020-21) relates to the RDEC scheme and £5.9 billion (£5.5 billion in 2020-21) to the SME scheme.

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

3.27 The Corporation Tax Act 2009 specifies the eligibility criteria for research and development reliefs that can be claimed. Where error and fraud results in overpayment or underpayment of Corporation Tax research and development reliefs to large businesses and small and medium enterprises who are either not entitled to these reliefs or are paid at a different rate from that specified in the legislation, the transactions do not conform with Parliament's intention and are irregular.

3.28 Using the evidence available from existing risk-based compliance activity, HMRC has estimated the level of error and fraud present within Corporation Tax research and development reliefs as £469 million or 4.9% of related expenditure in 2021-22 (2020-21 - £336 million or 3.6% of related expenditure). The increase of £133 million and 1.3 percentage points is explained by the fact that error and fraud were identified in a higher proportion of the cases investigated; and a rise in the value of those cases confirmed as fraudulent by HMRC's Fraud Investigation Service (FIS) from £11.2 million in 2020-21 to £26.9 million in 2021-22. From our review of a sample of these compliance investigations, we found an increase in the proportion of claims that appeared to be speculative, and which were completely disallowed because the activities did not qualify as research and development.

3.29 In forming his regularity opinion, the C&AG:

- evaluated the control processes HMRC has designed and implemented to prevent and detect error and fraud in these reliefs, including how cases are risk-assessed and selected for compliance review;
- considered what evidence these controls provided about the likelihood of error and fraud occurring in the claims that have not been subject to review by HMRC; and
- evaluated the detailed input data, methodology, assumptions and judgements applied by HMRC to produce its estimate.

3.30 Based on this work, the C&AG considers the level of error and fraud present in Corporation Tax research and development reliefs to be material and has qualified his regularity opinion in that respect.

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

3.31 The C&AG has qualified his regularity opinion on Corporation Tax research and development reliefs 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 for an estimate to be produced remain relevant to the 2021-22 period 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, unexplained growth in the schemes in recent years; and
- an increase in public reporting of instances of abuse in these schemes, including through unregulated agents.

3.32 As part of its compliance processes, HMRC undertakes case reviews of individual claims under the schemes where they are assessed as at risk. These reviews can result in claims being reduced or rejected by HMRC or modified or withdrawn by the company making the claim. In establishing its estimate of the level of error and fraud in Corporation Tax research and development reliefs, HMRC analysed the results of the compliance activity it completed in 2020-21 and 2021-22.

3.33 HMRC's current estimate of error and fraud in Corporation Tax research and development reliefs is based on an assessment of observed outcomes of compliance cases, together with a series of judgements, including an assumption that unreviewed cases have a lower rate of error and fraud. This is because HMRC considers that these cases have been assessed as lower risk through risk-profiling. These judgements are limited by the quality and availability of data in respect of cases that have not been subject to review by HMRC.

3.34 Based on our analysis of HMRC data, reasonable variations in these judgements could have a significant impact on the range of estimated error and fraud. The methodology adopted by HMRC and the assumption of lower risk in unreviewed cases also means that its current estimate still does not fully consider causes of error and fraud, other than those detected by existing controls. While HMRC's best estimate of error and fraud is subject to uncertainty, the cumulative evidence suggests that the level of error and fraud is material to that expenditure stream.

3.35 An HM Treasury evaluation of Corporation Tax research and development reliefs found that UK claims could have been inflated by a wide margin.[19] It found that UK companies claimed tax relief on £47.5 billion of research and development expenditure in 2019, but the Office for National Statistics estimated that businesses only carried out £25.9 billion of privately financed research and development in the UK. It concluded that while this gap could be partly explained by companies being able to claim for activity taking place overseas, this did not account for the full difference.

3.36 HMRC temporarily paused all payments of research and development claims in April 2022, having identified a pattern of irregular claims in that month to allow it to consider and act upon potential abuse of the schemes. Claims processing and payment has now resumed, with HMRC's assessment of the issues that led to the pause in payments ongoing. HMRC's Fraud Investigation Service (FIS) continues to investigate irregular claims. In addition, HMRC told us that is has put in place additional measures in response to the irregular claims identified including: establishing a threat risk assessment process for all research and development claims; implementing additional payment identification and verification controls for all research and development payments; and accelerating the creation of its Research and Development Anti Abuse Unit, which was announced in the autumn budget.

19 HM Treasury, *R&D Tax Reliefs*, available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1037348/RD_Tax_Reliefs.pdf

Key developments during 2021-22

3.37 As part of our prior year audits, we made a series of recommendations in our Management Letters to HMRC on improving its approach to tackling and measuring error and fraud in Corporation Tax research and development reliefs. Those recommendations were accepted by HMRC and included:

- gathering sufficient evidence to perform a robust assessment of the risks that give rise to fraudulent or erroneous claims;
- assessing and improving the risk-profiling process for claims made by taxpayers; and
- introducing controls to address the risks identified, including through the development of a random enquiry programme and using that as a basis for assessing the quality of the existing compliance approach.

3.38 HMRC has made progress in addressing our recommendations, most notably in commencing the development of a mandatory random enquiry programme (MREP) for small and medium enterprises. The scope of the programme is comparable with other similar random enquiry programmes used by HMRC to inform its estimates of error and fraud. HMRC told us that random enquiries into Corporation Tax research and development relief claims typically take between 30 to 45 weeks to complete. At 31 March 2022, HMRC had closed 213 of the 500 Phase 1 random enquiry cases it opened during the year and expects to close the remainder by September 2022. HMRC considered that the number of closed cases was not yet sufficient in terms of coverage to inform the 2021-22 error and fraud estimate. HMRC expects its 2022-23 estimate to be prepared using the results of its random enquiry programme which we will evaluate and report on as part of our 2022-23 audit.

3.39 In its most recent report on HMRC performance in 2020-21, the Committee of Public Accounts made two further recommendations in respect of Corporation Tax research and development reliefs.[20] Those recommendations were accepted by HMRC and required 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.

20 HC Committee of Public Accounts, *HMRC Performance in 2020-21*, Thirty-Seventh Report of Session 2021-22, HC 641, February 2022.

3.40 HMRC's formal response to the recommendations was set out in a Treasury Minute on 26 April 2022 which outlined measures announced in the autumn Budget 2021 and other action it was taking to:

- introduce a package of research and development reform measures aimed at tackling abuse and improving compliance (by April 2023), including a cross-cutting team of around 50 staff focused on abuse in partnership with HMRC's Fraud Investigation Service; requiring all claims to be made digitally, with more detail, endorsed by a named senior officer; a programme of customer education to improve the upstream compliance programme; and enhancements to HMRC's risk-profiling.
- 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 (ONS) to gain further insight into recent trends in research and development expenditure; and
- progress its mandatory random enquiry programme, randomly checking claims to inform the 2022-23 estimate.[21]

3.41 While HMRC is taking action to address the National Audit Office and Committee of Public Accounts' recommendations, the impact of this on tackling abuse of Corporation Tax research and development reliefs will not become clear until 2022-23 and beyond. We will consider and report on any emerging insights as part of our 2022-23 audit.

Impacts of actions taken in 2020-21

3.42 Our 2020-21 report set out a series of steps HMRC had begun taking to tackle abuse of Corporation Tax research and development reliefs. We have summarised the progress made during 2021-22, together with what is known about the impact of these steps, below.

Increasing compliance team capacity

3.43 In 2021 HMRC recruited a further 100 compliance officers to support its approach to tackling abuse of Corporation Tax research and development reliefs. Overall capacity in these compliance teams will increase further through a cross-cutting team of 50 officers announced in autumn 2021. HMRC has not yet assessed the impact of this additional capacity on the level of error and fraud.

21 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.

Introduction of the small and medium enterprise scheme cap

3.44 From 1 April 2021, HMRC implemented a restriction on the tax credit payable to small and medium enterprise companies claiming Corporation Tax research and development reliefs. This Pay as You Earn (PAYE) and National Insurance Contributions cap came into effect for accounting periods beginning on or after 1 April 2021 through amendments to the Corporation Tax Act 2009.[22]

3.45 While the impact of the cap will not become clear until Corporation Tax returns for the claim period are due to be received by qualifying companies, HMRC estimates that this measure will reduce the cost of the relief by £105 million a year by 2024-25 – and that it will have a positive impact on the levels of error and fraud. HMRC has indicated that it monitors how the new cap operates in practice – both to ensure it deters abuse as expected and to identify any unintended consequences.

Improved claims checking and risk screening

3.46 In 2021, HMRC introduced a new claim checking approach, supported by standardised operating procedures to ensure consistent application by caseworkers, together with new training on risk identification, which uses a risk scoring system to ensure that HMRC is focusing its compliance activity on the areas of greatest risk. HMRC also established a revised risk screening process for claims submitted by companies and developed a mechanism to ensure findings from compliance work are reflected in future risk assessments. These initiatives have resulted in:

- new mechanisms being introduced including a Risk Assurance Board which uses project and risk dashboards to better target areas of risk within the relief schemes;
- use of analysis and evaluation of updated risk indicators and types of inaccuracy identified through compliance casework to better target the riskiest cases; and
- use of closed compliance cases to assess the types of errors being found and the proportion of such cases with errors to better inform future compliance work.

3.47 These initiatives have been introduced over the last six to nine months and HMRC has not yet measured how these are affecting the levels of error and fraud recorded.

22 The amendments were introduced in the Corporation Tax Act 2009, Chapter 13, Part 2, Section 1058.

Appendix One

Our audit approach

Methods

1 This report is our factual commentary on HM Revenue & Customs' (HMRC's) performance during 2021-22. We prepared our commentary using evidence collected between April and July 2022.

Scope

2 This report covers:

- HMRC's performance against its 2021-22 objective of collecting revenue and managing compliance, and looks at the main components of the £731.1 billion raised during 2021-22 (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 the COVID-19 support schemes (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 Personal Tax Credits (tax credits) and error and fraud in Corporation Tax research and development reliefs (Part Three).

3 In producing this report, we drew on a variety of evidence sources.

Part One

Document review and data analysis

4 For Part One, we reviewed the supporting information for HMRC's Trust Statement and Resource Accounts, as part of our financial audit. 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, the Knowledge, Analysis and Intelligence directorate and the Debt Management and Banking unit. This included a review of:

- board meeting minutes;
- internally commissioned research papers;

- risk assessments; and
- performance monitoring dashboards.

5 Our review focussed on information in those documents relevant to the period between 1 April 2021 and 31 March 2022.

6 Our analytical review 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. We reviewed the following documents published by HMRC: *Tax relief statistics* (published in May 2022); its *Outcome Delivery Plan for 2021-22* (published in July 2021); and *Measuring Tax Gaps 2022* (published in June 2022). We also reviewed the following document published by the Office for Budget Responsibility: *Economic and fiscal outlook* (March 2022).

7 We also relied on evidence from our value-for-money reports relevant to the work of HMRC. These are listed in Appendix Two.

Interviews with departmental staff

8 We interviewed staff from HMRC's business groups responsible for a range of areas including compliance, customer services, finance and debt management. We undertook these interviews to corroborate the evidence collected from our document review and to understand better, in relation to the team's area of responsibility:

- the role of each team;
- HMRC's objectives;
- HMRC's views on current issues;
- the risks to achieving HMRC's objectives; and
- the impact of COVID-19 on its operations.

Parts Two and Three

9 Parts Two and Three rely principally on evidence collected as part of our financial audit work on the employment support schemes, 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 analysis of the impacts of COVID-19 on error and fraud, and an update on HMRC's strategy for tax credits.

Appendix Two

Our value-for-money and wider work

1 Since April 2021, we have published several reports relevant to the work of HM Revenue & Customs (HMRC):

- Comptroller and Auditor General, *Initial learning from the government's response to the COVID-19 pandemic*, Session 2021-22, HC 66, National Audit Office, May 2021.

  This report draws out learning from the reports that we have published to date, as well as other work we have published that covered the COVID-19 pandemic.

- Comptroller and Auditor General, *Efficiency in government*, Session 2021-22, HC 303, National Audit Office, July 2021.

  The first in a series of National Audit Office reports about efficiency in government.

- Comptroller and Auditor General, *HM Revenue & Customs 2020-21 Accounts*, November 2021.

  The Comptroller and Auditor General's report on the 2020-21 accounts of HMRC.

- Comptroller and Auditor General, *The UK border: Post UK-EU transition period*, Session 2021-22, HC 736, National Audit Office, November 2021.

  Examines the government's progress in managing the border and implementing the Northern Ireland Protocol since the end of the transition period.

- Comptroller and Auditor General, *Managing tax debt through the pandemic*, Session 2021-22, HC 799, National Audit Office, November 2021.

  Considers how well HMRC has managed tax debt through the pandemic – in particular, whether it has adapted sufficiently to the changing nature and scale of that debt and the wider circumstances that affect taxpayers' ability to repay tax.

- Comptroller and Auditor General, *Administration of Scottish income tax 2020-21*, Session 2021-22, HC 1011, National Audit Office, January 2022.

  Examines HMRC's administration of Scottish income tax.

- Comptroller and Auditor General, *Administration of Welsh rates of income tax 2020-21*, Session 2021-22, HC 1014, National Audit Office, January 2022.

  Examines HMRC's administration of Welsh income tax.

- Comptroller and Auditor General, *Financial modelling in government*, Session 2021-22, HC 1015, National Audit Office, January 2022.

  Examines the use of financial models across government.

- Comptroller and Auditor General, *Investigation into the implementation of IR35 tax reforms*, Session 2021-22, HC 1103, National Audit Office, February 2022.

  Examines lessons from the implementation of 2017 reforms to tax rules for off-payroll working in the public sector.

- National Audit Office, *Evaluating government spending: an audit framework*, April 2022.

  Provides the National Audit Office's perspective on what we look for in terms of evaluation in the different stages of the policy cycle.

Appendix Three

Historical fraud and error rates in Personal Tax Credits

Figure 16
Historical fraud and error rates in tax credits

Error and fraud as a percentage of finalised entitlement

	Year of error and fraud analysis programme	Lower Bound	Central Estimate	Upper Bound
		(%)	(%)	(%)
Overpayments	2010-11	7.5	8.1	8.8
	2011-12	6.6	7.3	7.9
	2012-13	4.7	5.3	6.0
	2013-14	4.2	4.7	5.2
	2014-15	4.0	4.4	4.8
	2015-16	4.3	4.8	5.2
	2016-17	4.3	4.7	5.1
	2017-18	5.0	5.5	6.1
	2018-19	4.4	4.9	5.3
	2019-20[1]	4.8	5.3	5.9
	2020-21	4.4	5.0	5.7
Underpayments	2010-11	0.6	0.8	1.0
	2011-12	0.6	0.9	1.2
	2012-13	0.2	0.5	0.7
	2013-14	0.6	0.7	0.9
	2014-15	0.5	0.6	0.7
	2015-16	0.5	0.6	0.7
	2016-17	0.6	0.7	0.9
	2017-18	0.6	0.7	0.8
	2018-19	0.6	0.7	0.9
	2019-20[1]	0.8	0.9	1.1
	2020-21	0.6	0.8	0.9

Note
1 2019-20 estimates have been revised by HMRC.

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