



House of Commons
Committee of Public Accounts

Filing of income tax self assessment returns

Twenty-third Report of
Session 2005–06

*Report, together with formal minutes,
oral and written evidence*

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The Committee of Public Accounts

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Summary

HM Revenue and Customs collects £16 billion a year from Income Tax Self Assessment and sends Income Tax Self Assessment forms to around 10 million taxpayers. The Department achieved its Public Service Agreement target of 90.6% of 2003–04 tax returns filed on time by the 31 January 2005 deadline. It has a target to increase this to 93% by January 2008.

As at July 2004 some £1.1 billion of income tax was outstanding from 1.1 million overdue returns. Similarly in July 2005 around 1.1 million returns were overdue, some 240,000 taxpayers had two or more tax returns outstanding, and 10,000 had six returns outstanding.

The Committee last examined Income Tax Self Assessment in 2002.¹ It recommended improvements in the way the Department uses, and assesses the effectiveness of, its sanctions to encourage filing on time. The Committee also recommended that the Department should complete its research into the scale of non-compliance and the amounts of tax lost. The Department accepts that it still needs better information to assess the effectiveness of penalties in changing taxpayer behaviour.

Tax returns are sent out in April, before most taxpayers can complete them, and they are increasingly filing the returns later each year despite the Department's advertising campaigns. The Department has removed the need to file a return for around a million taxpayers. It has also simplified the format of the main return and introduced a shorter tax return for around a million taxpayers with simpler financial affairs. But 60% of those that file late each year have no tax to pay or are due a repayment.

Around 30% of completed tax returns contain errors and around £2.8 billion of revenue may be lost through inaccurate returns. The Department has provided guidance and advice on its website and through help lines but its staff often lack the knowledge to deal with enquiries. Callers have also experienced difficulties in getting through to the Department's help lines at peak times.

The Department made errors in processing nearly 500,000 returns, leading to £65 million of undercharges and £30 million overcharges of taxpayers. It also made two million Pay As You Earn coding errors with an accuracy rate of 73% in setting codes. It wrongfully imposed automatic penalties for late filing on 30,000 taxpayers, 3% of the 950,000 penalties issued, but does not try to detect such errors or identify those affected. The Department is developing better IT which it expects to remove a third of its coding errors; improving the management of its processes to reduce its error rate; improving systems to log in returns; and clearing taxpayers from its database who are no longer self employed. However, the Department does not know how much compensation it has paid to those affected by its errors and cannot provide any estimate of this figure.

1 33rd Report from the Committee of Public Accounts, *Income Tax Self Assessment* (HC 296, Session 2001–02)

Operating the Income Tax Self Assessment filing process costs £220 million a year. Some 8,000 staff years are needed to process self assessment tax returns and a further 1,800 staff years to chase returns and for debt management. The Department expects to achieve efficiency savings of between 200–300 staff years from 2005–06 by applying the practices of the most efficient offices.

Processing can be made more efficient by encouraging greater use of e-filing. In 2004–05, over 1.6 million taxpayers filed online or by an electronic service used by their agents. But the service did not operate properly in January 2005 when a large number of people tried to file online. Although the Department has improved the capacity of its e-service, it may still not be sufficient at peak times.

Taxpayers are increasingly filing tax returns later each year which causes a major peak in workload at the Department and higher risks of official error. Getting returns in earlier could spread the workload and give the Department more time to set tax codes for the following tax year. The ongoing Lord Carter review of e-filing is considering the options for increasing e-filing and changing filing dates.

On the basis of a report by the Comptroller and Auditor General,² the Committee examined HM Revenue and Customs on getting accurate tax returns in on time, reducing the errors made by the Department and improving efficiency in dealing with tax returns.

2 C&AG's Report, *HM Revenue and Customs: Filing of Income Tax Self Assessment Returns* (HC 74, Session 2005–06)

Conclusions and recommendations

- 1. Taxpayers are taking longer to file their returns and therefore the Department has less time to process them and makes more errors.** It sends out the returns in April each year before most employed taxpayers have received their P60 form and other financial information they need to complete the returns. The Department should therefore send out returns in late May. In time, it could then include on returns information that it has already received, which should help taxpayers to complete the form accurately.
- 2. Errors by taxpayers in completing their returns cost £2.8 billion in lost tax and result in additional costs for the Department in carrying out enquiries to correct them.** Some of the errors are due to genuine mistakes or misunderstandings by the taxpayer. The Department should provide clear information to taxpayers on the most common mistakes and how to avoid them. In particular it should target the groups such as partnerships and sole traders who are most prone to filing inaccurate returns.
- 3. Some errors made by taxpayers are because they do not have access to appropriate advice from the Department.** Telephone helpline staff often lack the detailed knowledge to respond consistently and accurately to enquiries and taxpayers have experienced difficulties in contacting them at peak times. The Department should improve the training for call centre staff and the access to specialist advice for complex enquiries. It should also extend the hours of service at peak periods of the year.
- 4. The Department makes errors in processing 5% of tax returns resulting in £65 million undercharges and £30 million in overcharges of tax.** The Department has also incorrectly imposed penalties for late filing on some 30,000 taxpayers who actually filed on time. The Department should improve its training of staff, the logging of returns and its quality control arrangements, for example by undertaking real time quality control checks as the returns are being processed to prevent errors and stop them recurring.
- 5. The Department makes errors in calculating at least a quarter of taxpayers' PAYE codes so employers then deduct the wrong amount of tax.** Taxpayers without professional advisers are less likely to challenge the Department's errors in tax assessments, codes and penalties. The Department should accept more responsibility for its mistakes. It should advise taxpayers who are most likely to be subject to coding and other errors, such as those with income from more than one source, to check the accuracy of the data it has used.
- 6. The Department recognises it needs better information to manage its business effectively.** As a minimum it should have systems that can track errors in processing and coding and the imposition of penalties and their enforcement. It should monitor the consequences for taxpayers and tax loss. It should set a target to improve the accuracy in setting tax codes from 73% to well over 90%.

7. **It costs the Department £220 million a year to process tax returns.** The Department has targets for improving efficiency and expects to achieve these by reducing the number of processing centres. Further efficiencies could be achieved by comparing with the processing costs of other taxes and benefit payments to identify and apply good practice, such as not duplicating the input of data and developing the main tax return so that the information on it can be scanned.
8. **E-filing is cheaper and more accurate than filing a paper return but only 17% of returns are filed electronically.** Other countries have higher rates of electronic filing, for example 44% in the United States of America and 83% in Australia. The Department should encourage more use of e-filing by making it more user friendly, for example by pre-completing parts of the on-line tax return forms with data it already holds. It should make on-line filing of returns by professional agents mandatory.
9. **There are major peaks in workload around the September and January filing deadlines.** These cause problems for the Department in processing large numbers of returns accurately. Smoothing the peaks would improve accuracy and efficiency. Taxpayers in other countries have only three to four months to file compared to ten months in the UK. Subject to Lord Carter's recommendations, the Department should consider bringing forward the filing dates and/or have differential filing dates for various groups of taxpayers to spread the workload.

1 Getting accurate tax returns in on time

1. HM Revenue and Customs collects net receipts of around £118 billion a year in Income Tax from 35 million taxpayers.³ Most of the tax is collected through the Pay as You Earn (PAYE) scheme whereby employers deduct and pay over to the Department each month the Income Tax due on their employees' salaries and wages, taking into account the individual's tax code as notified by the Department.

2. The Department collects around £16 billion through the Self Assessment scheme, chiefly from those who are self-employed, business partners, company directors, landlords and people with more complex financial affairs, who are required to complete a tax return and pay over any additional tax owing by 31 January following the end of the tax year. If a person submits the tax return by the end of the previous September the Department undertakes to assess the tax liability. Where possible, the Department seeks to collect any tax owing or arrange any refunds to employees and pensioners through adjustments to individual's PAYE tax code for the following tax year. Until the 2004–05 tax year, around 10 million taxpayers were required to complete Self Assessment returns. The average additional amount of Income Tax assessed as due, beyond that deducted at source, is around £1,600 per return.⁴

3. For the 2004–05 tax year, the Department simplified the Self Assessment system by removing the need to file a return for around 1.1 million people whose tax affairs were sufficiently simple that they could be dealt with through PAYE. The Department reviews such people each year in case their circumstances change.⁵

4. Around 90% of tax payers file their returns by the 31 January deadline each year and 97.8% within 12 months. The Department achieved its Public Service Agreement target of 90.6% of 2003–04 tax returns filed on time by the 31 January 2005 deadline.⁶ The Department has a target to increase this to 93% by January 2008. Achieving this higher target will be a challenge from 2004–05 because the one million taxpayers who were no longer required to file a return in 2004–05 were among also those most likely to file on time.⁷

5. In July 2005 some £1.1 billion of income tax was outstanding from 1.1 million overdue tax returns.⁸ 240,000 of these taxpayers had two or more returns outstanding and over 11,000 taxpayers had six or more returns outstanding.⁹ The Department has identified the causes of late filing and the groups of taxpayers involved and developed an action plan to meet its higher target. Taxpayers most likely to file late include young males, those new to

3 C&AG's Report, para 1.15

4 *ibid*, para 1.15

5 Q 40

6 Q 58

7 C&AG's Report, para 2.10

8 *ibid*, para 2.3

9 Ev 13

filing a return, those in the Construction Industry Scheme, taxpayers in parts of London, and those with no further tax to pay.¹⁰

6. 60% of people who file late have already paid enough tax or are owed a refund by the Department, which raises questions about the burden of completing a tax return.¹¹ The Department sends out tax returns in April each year. Before completing them most people wait to receive their P60s and other financial information from their banks and accounts which they often receive later in the summer.¹² This enforced lull allows taxpayers more time to lose returns and for some to forget to file their returns.¹³ The Department might achieve more timely filing of returns if it sent them out later when people are better placed to complete them.¹⁴

7. Despite the Department spending £46 million on three media campaigns to encourage taxpayers to file on time there has been a trend to file later. 44.8% of returns were filed by September 2004 for the 2003–04 tax year compared with 52% by September 1997 for the 1996–97 tax year. The Department considers, however that its most recent campaign is succeeding.¹⁵

8. Of the 240,000 taxpayers with returns outstanding in July 2005, 34,000 were insolvent or living abroad, the Department was attempting to trace 85,000 others and was pursuing the remaining 121,000 to obtain their returns and recover the tax due.¹⁶ In November 2002, our predecessor's Report on the collection of fines and fees in the magistrate courts¹⁷ made recommendations on the need to assess the effectiveness of different enforcement techniques and that government agencies such as the former Inland Revenue should cooperate to trace defaulters. And in their Report, *Recovery of debt by the Inland Revenue* in November 2004, they recommended that the Department should make maximum use of other departments' records to find taxpayers it cannot trace and seek a legal power to require taxpayers to provide up to date contact details.¹⁸ In 2004 the Department began to use the mutual assistance of recovery of debt provisions in the European Union to pursue through other member States longer standing cases where the taxpayer was living abroad.¹⁹

9. When taxpayers do not file their tax returns by the deadline, the Department can make determinations of the tax due, charge interest, and take court action. It can also issue automatic penalties of up to £100 but these penalties are limited to the amount of tax owed which reduces their effectiveness when little or no further tax is payable.²⁰ In some

10 C&AG's Report, para 2.6

11 Q 14

12 C&AG's Report, para 4.11

13 *ibid*, para 4.11

14 Q 17

15 Q 58

16 Ev 13

17 68th Report from the Committee of Public Accounts, *Collection of fines and other financial penalties in the Criminal Justice System* (HC 999, Session 2001–02)

18 49th Report from the Committee of Public Accounts, *Recovery of debt by the Inland Revenue* (HC 584, Session 2003–04)

19 C&AG's Report, para 2.20

20 *ibid*, Executive Summary, para 9

countries penalties for late filing are related to the taxpayer's net income. If imposing automatic penalties does not secure a tax return, the Department can seek directions from the General Commissioners to apply daily penalties of up to £60. But only one third of taxpayers are aware of these penalties.²¹

10. Under a 'Spend to Save' initiative, the Department received additional funding to increase its use of daily penalties to persuade recalcitrant taxpayers to file their returns. In about a quarter of cases the threat of daily penalties has been sufficient to bring in the outstanding returns. But the Department now expects the additional tax yield over the three years to March 2006 to be less than its estimate of £470 million.²² The Department accepts it does not have the information it needs on the number and value of the penalties it has imposed and the amounts actually paid, to determine which of its sanctions are most cost effective in getting taxpayers to file returns.²³ The Department expects that a new debt management system for Self Assessment debts will provide better management information.²⁴

Reducing errors made on returns

11. Taxpayers make errors in around 32% of tax returns. The Department estimates that around £2.8 billion of tax may be lost from inaccurate returns, equivalent to 18% of net receipts from Income Tax Self Assessment.²⁵ Some £2 billion of this is accounted for by just 5% of returns²⁶ — around 400,000 people owing on average £5,000.²⁷ These figures underestimate the true extent of underpaid tax because the Department's estimates do not identify all non-disclosed income and do not include people working in the shadow economy. Since April 2002 the Department has identified 89,000 people who are not registered for Self Assessment who should be filing tax returns.²⁸ Errors also increase the cost of processing tax returns. The Department estimates that if all self assessment forms were correctly filed it would save £9 of the £22 it costs to process a return or £90 million a year.²⁹

12. Some errors by taxpayers are simple or genuine mistakes, whereas others are due to more deliberate non-compliance such as fraudulent under or non-declaration of income.³⁰ Only half of sole traders and partnerships file accurate returns. The Department undertakes risk-based enquiries targeted on particular trades where the risk of non-compliance is higher, such as the construction industry, high volume cash-based industries, the retail and entertainment sectors, clubs and licensed premises. It also draws

21 C&AG's Report, Figure 9, paras 2.23–2.24

22 *ibid*, para 2.17

23 Q 5

24 Q 6

25 C&AG's Report, para 3.2

26 *ibid*, para 3.5

27 Q 106

28 C&AG's Report, Executive Summary, para 10

29 Qq 25–26

30 C&AG's Report, para 3.2

on its local office knowledge of compliance patterns and taxpayers' previous filing behaviour.³¹

13. The Department carries out checks during processing of filed returns to identify and correct simple mistakes made by taxpayers. It has provided guidance to tax advisers and other representative groups on common mistakes and particular areas of error. In 2005 it wrote to some 180,000 people, whom it judged most likely to make errors, to alert them to common mistakes such as in their pension contributions and capital allowance.³²

14. Simple or genuine mistakes by taxpayers in completing their returns may in part be due to the complexity of the self assessment system.³³ Simpler forms and procedures reduce compliance costs for taxpayers as well as helping them comply with their obligations. HM Revenue and Customs' tax forms compare well with those of other countries in terms of clarity and ease of use for the non-professional.³⁴ But until recently much of the main tax form did not apply to a significant number of those involved. The Department has therefore sought to simplify the forms by introducing a short tax return for a million taxpayers with simpler financial affairs³⁵ which saves the taxpayer one hour compared to completing the full tax return. It is also simplifying the format of the main return, which it plans to test in 2007 with a view to using a new return from January 2008.³⁶ But it has had less success in simplifying the accompanying guidance mainly because of the need to reflect the legal requirements of the tax. Nevertheless it plans to improve the clarity of its guidance leaflets on its website. It has obtained feedback from tax advisers and accountants, and runs schemes to educate new businesses about their tax obligations.^{37 38}

15. At present some telephone helpline staff often lack the detailed knowledge to respond consistently and accurately to enquiries and taxpayers have experienced difficulties in contacting them at peak times. The Department has a target by 2007–08 to increase to at least 90% the accuracy and completeness of information and the advice given in contacts and to 80% in taxpayers achieving success in their first point of contact.³⁹ It is improving training for its call centre staff, while supporting them with specialist staff to deal with the more detailed enquiries and sifting out more complex questions to be transferred to the most knowledgeable staff. It is also looking at ways of switching staff from other tax streams to handle peaks. The Department accepts there are pressures on the call centres in the lead up to the 31 January filing deadline as people need last-minute advice.⁴⁰ The

31 Q 35

32 Qq 27–29, 106

33 Qq 4, 20, 37

34 C&AG's Report, para 4.14

35 Qq 4, 49

36 Q 14

37 Q 4

38 Q 57

39 C&AG's Report, para 3.7

40 Q 43

helplines are open from eight am to eight pm.⁴¹ The Department does not believe there is large demand for longer opening hours.⁴²

41 C&AG's Report, paras 3.7, 4.9; Qq 20, 41, 43, 83

42 Qq 84–87

2 Reducing errors made by the Department

16. HM Revenue and Customs processed 95% of returns accurately in 2004–05, in line with its target. Nearly 500,000 returns were processed with some errors, leading to incorrect charging of tax – £65 million in undercharges and £30 million in overcharges.⁴³ In 2003–04 12% of over charging errors found exceeded £500.⁴⁴ Undercharges may be written-off.⁴⁵ A survey by Association of Chartered Certified Accounts of its members in 2004 found that 80% had to spend extra time on their clients' Self Assessment returns due to Departmental errors.⁴⁶ Unrepresented taxpayers are less likely to identify the Department's errors or to know how to get these corrected.⁴⁷ The Department is seeking to minimise the mistakes it makes in processing of returns. It considers it corrects about two-thirds of the errors it makes and seeks to identify the main causes of error. It plans to improve its quality management systems in local offices to identify and correct errors earlier.⁴⁸

17. The Department achieved an accuracy rate of 71% in 2003–04 and 73% in 2004–05 in setting taxpayer PAYE codes. It made around two million errors which led to errors in the tax codes of 1.4 million people.⁴⁹ Setting the tax code correctly is important in ensuring the right amount of tax is deducted at source for employed and pensioner taxpayers, especially when they are not required to make a return. With more taxpayers not needing to file a return, it is even more important to get tax codes right.⁵⁰ The Department depends on taxpayers to check that their tax code is right.⁵¹

18. Around one third of the Department's errors were due to a failure to update the taxpayer's code with information provided by the taxpayer. Taxpayers with income from more than one source were more likely to experience coding errors.⁵² The Department expects to remove a third of tax coding errors by improving the management of its processes and by developing better IT and an automated tax coding system.^{53 54}

19. Errors by the Department in logging tax returns and updating taxpayer records have also resulted in late filing penalties being imposed on people who have actually filed their returns on time. The Department estimates that it imposed incorrect penalties on some

43 Ev 13

44 C&AG's Report, Executive Summary, para 16

45 Q 107

46 C&AG's Report, para 3.22

47 *ibid*, para 3.12, 3.14, 3.18

48 Qq 52–53

49 Ev 13

50 C&AG's Report, para 3.13

51 Qq 91–92

52 C&AG's Report, para 3.14

53 Q 49

54 Q 54

30,000 taxpayers in 2004 — 3% of the 950,000 taxpayers with penalties imposed.⁵⁵ The Department recognises the need to improve this aspect of its work and it had reduced the proportion of wrongful penalties to an estimated 1% in 2005. It was correcting its databases to remove duplicate records and details of taxpayers who were no longer self employed and it was improving its systems for logging tax returns.⁵⁶

20. The Department is unable to identify individual taxpayers who have been penalised incorrectly and therefore relies on taxpayers to spot its errors. Nor does it know what compensation it has paid to people as a result of its errors.⁵⁷ Taxpayers without professional advisers may be less well placed to identify or respond to these or other mistakes in calculating their tax and or in setting their tax codes.⁵⁸

55 C&AG's Report, para 3.16

56 Q 39

57 Qq 92–105

58 C&AG's Report, paras 3.12, 3.14, 3.18

3 Improving efficiency in dealing with tax returns

21. Operating the Income Tax Self Assessment filing process costs £220 million a year in staff costs or some £22 per return issued, excluding overhead costs such as IT.⁵⁹ Chasing overdue tax returns and carrying out enquiries to confirm whether the right amount of tax is being declared incurs further costs. The cost of processing an accurate paper-based return is around £13.⁶⁰ By comparison, the cost of processing benefits applications ranges from £17 for Social Fund applications to £60 for Income Support applications.⁶¹

22. The Department has an overall target to make efficiency savings of over £500 million and reduce staff numbers by 12,500 posts by March 2008.⁶² Some 8,000 staff years are used to process self assessment tax returns and a further 1,800 staff years to chase returns and manage debt.⁶³ The Department processed returns at 74 offices in the UK. Two offices process around 500,000 returns, while almost half the offices handle less than 100,000 and some process only a handful (**Figure 1**). The Department intends to concentrate processing at about five centres by 2008 to achieve efficiency gains.⁶⁴

23. The Department also expects to make efficiency savings of between 200–300 staff years from 2005–06 by applying more widely the practices of the more efficient offices. Further opportunities to improve efficiency arise by increasing the extent of automatic data capture from tax returns. The Department is carrying out trials to improve its processing of tax returns by introducing standardised, quicker and more accurate procedures. Although it has not yet compared the costs of processing with other taxes, it intends to benchmark cost and quality with other taxes to identify good practice.⁶⁵

59 Q 21

60 Q 26

61 C&AG's Report, para 4.2

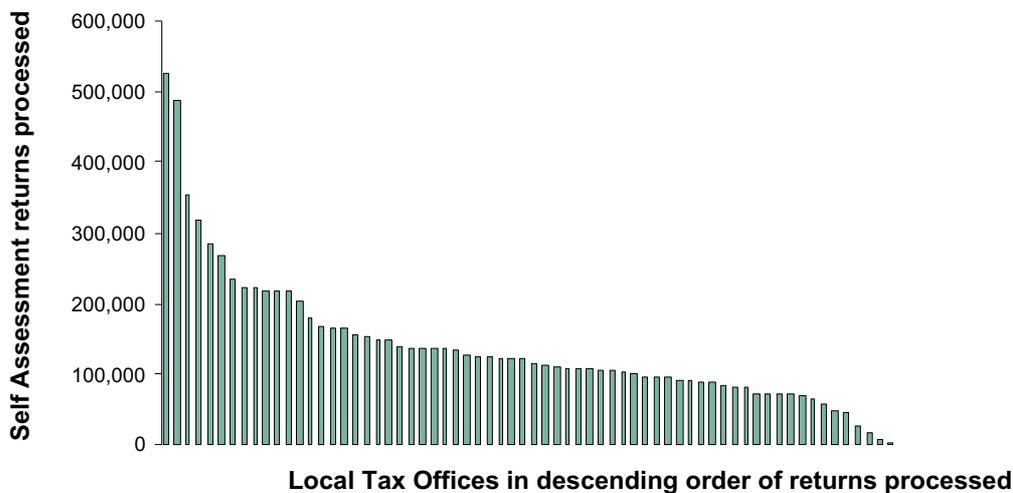
62 *ibid*, para 1.16

63 Qq 79–82

64 C&AG's Report, paras 4.6–4.7

65 Qq 76–78

Figure 1: Self Assessment returns processed by HM Revenue and Customs local offices in 2003–04



Source: C&AG's Report, HM Revenue and Customs: Filing of Income Tax Self Assessment Returns (HC 74, Session 2005–06)

Filing returns electronically

24. The Department encourages all taxpayers to file their returns electronically. Electronic filing reduces costs both for taxpayers and the Department and improves accuracy by identifying simple errors through validation checks on the return. The Department considers the cost of processing a tax return excluding overhead costs is reduced from £22 to £13 if the return is filed electronically, by eliminating the costs of data entry and of rectifying simple errors made by taxpayers in completing the form.⁶⁶

25. The Department has a target to obtain 35% of Self Assessment returns electronically by 2007–08, with an interim target of 25% by 2005–06. It achieved 12% in 2003–04 and met its forecast of 17% in 2004–05 –just over 1.6 million returns submitted electronically. Electronic filing in the UK is lower than in some other countries, for example the United States has achieved 44% and Australia 83%. To increase take up of online services the Department is targeting groups with high potential to file electronically through e-marketing campaigns.⁶⁷ It has offered limited incentives, such as performing the tax calculation on behalf of the taxpayer irrespective of when they file their return, to encourage self assessment filing on-line, whereas it has used financial incentives to encourage small sized businesses to file their employer returns electronically.⁶⁸ It has a mandatory regime for employers with 250 and more employees to have filed PAYE returns online.⁶⁹ The review by Lord Carter⁷⁰ of e-filing is expected to suggest ways in which the Department can increase e-filing.⁷¹

66 Qq 22–23

67 C&AG's Report, para 1.10

68 Q 12; C&AG's Report, Figure 15

69 Qq 109–110

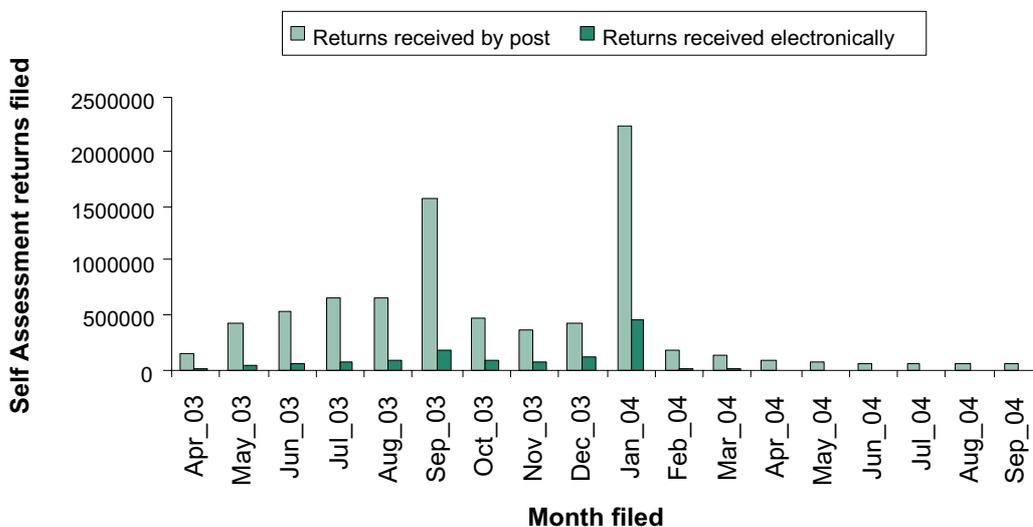
70 Ev 14

71 Q 10

26. The Department acknowledges that taxpayers want a reliable service. But over the weekend of 29 and 30 January 2005, when large numbers of people were seeking to file by the 31 January deadline, the online filing service did not operate properly. Around 80,000 people did not get a message to confirm they had submitted their completed return and they were therefore unsure whether their return had been successfully filed. HM Revenue and Customs gave those affected a two week extension to file their returns. It has reviewed the problems experienced to identify the causes and prevent a recurrence. While it has increased the scale of its web-based technology, the Department cannot provide an assurance that similar problems will not occur in the future given the high number of returns that are filed on the 31 January deadline.⁷²

27. There are major peaks in the workload for the Department around the two filing deadlines of September and January each year (**Figure 2**), which increases the Department's costs. Taxpayers are increasingly filing tax returns later each year – around 25% within two weeks of the January 31 deadline.⁷³ This brings a higher risk of errors in processing as the Department seeks to process these returns by the end of March so that it can take account of the information in sending out the following year's tax returns and in issuing tax codings for the start of next tax year. The Department encourages people to file by the end of September with the incentive that the taxpayer will not have to calculate the tax and if the taxpayer files on-line this facility is extended to the end of December.⁷⁴

Figure 2: The flow of Self Assessment returns for 2002–03 filed during 2003 and 2004



Source: C&AG's Report, *HM Revenue and Customs: Filing of Income Tax Self Assessment Returns (HC 74, Session 2005–06)*

28. Experience of other tax authorities suggests that HM Revenue and Customs might consider more fundamental changes to the filing deadlines to reduce costs and errors. Taxpayers in the United Kingdom have 10 months to file their returns whereas overseas tax authorities typically allow taxpayers only three to four months.⁷⁵ Some tax authorities

72 Qq 7, 43

73 C&AG's Report, Executive Summary, para 16

74 Qq 33, 43

75 C&AG's Report, para 2.4

tend to collect during the year a level of tax that is likely to be higher than the final assessment and therefore taxpayers have a greater incentive to submit returns promptly to obtain the refunds owed.⁷⁶ Getting returns in earlier by bringing forward the January deadline to the autumn, or setting differential filing deadlines for different groups could smooth the peaks in workload and help to reduce errors in processing and setting tax codes.⁷⁷

29. Sending out the returns later would also ease some of the pressure on the Department to finish processing the previous year's returns by the end of March, and the forms would also reach people when they are in a better position to complete them.⁷⁸ Lord Carter's review is considering a range of options for changing the dates when returns are sent out and the time allowed for taxpayers to return them^{79 80} and the findings of the National Audit Office's Report. The Department considers that any change in filing dates would need to reflect the differing circumstances of taxpayers, some of whom have more complicated financial affairs. It had not undertaken a cost benefit analysis of the various alternatives, but it intends to develop the management information needed for such analysis.⁸¹

30. Differential filing dates for paper and electronic returns are in place in ten of the 30 Organisation for Economic Co-operation and Development (OECD) member countries (Australia, Austria, Canada, France, Greece, Iceland, Ireland, Italy, Netherlands and Norway). In addition the United Kingdom has the most generous return filing dates for self calculating personal taxpayers of any OECD country. The Department has provided evidence to Lord Carter to inform his review. This outlines several options for differential filing dates such as moving the Self Assessment filing deadline from 31 January to 30 November of the preceding year; proposals for introducing a paper filing charge which would apply after a certain date while still retaining a late filing penalty; and changing the cut off date when the taxpayer does not have to calculate the tax. The Department considers that differential filing would increase the take up of online filing to 57% in the first year.⁸²

76 Q 9

77 Q 8; C&AG's Report, para 4.8

78 Qq 16 –17

79 Qq 10, 17

80 Qq 44, 46

81 Qq 18, 30, 61–66

82 Ev 15

Formal minutes

Wednesday 18 January 2006

Members present:

Mr Edward Leigh, in the Chair

Mr Richard Bacon
Greg Clark
Mr David Curry
Mr Ian Davidson
Helen Goodman

Sarah McCarthy-Fry
Mr Austin Mitchell
Jon Trickett
Kitty Ussher

Draft Report (Filing of income tax self assessment returns), proposed by the Chairman, brought up and read.

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

Paragraphs 1 to 30 read and agreed to.

Conclusions and recommendations read and agreed to.

Summary read and agreed to.

Resolved, That the Report be the Twenty-third Report of the Committee to the House.

Ordered, That the Chairman do make the Report to the House.

Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

[Adjourned until Monday 23 January at 4.30 pm]

Witnesses

Monday 14 November 2005

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Mr David Varney, Mr Gabs Makhoulf, and Mr Roy Massingale, HM Revenue and Customs

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Oral evidence

Taken before the Committee of Public Accounts

on Monday 14 November 2005

Members present:

Mr Edward Leigh, in the Chair

Mr Richard Bacon
Greg Clark
Helen Goodman

Mr Sadiq Khan
Kitty Ussher
Mr Alan Williams

Sir John Bourn, Comptroller and Auditor General, National Audit Office, was in attendance.

Ms Paula Diggle, Second Treasury Officer of Accounts, HM Treasury, was in attendance.

Report by the Comptroller and Auditor General, Filing of Income Tax Self Assessment Returns (HC 74)

Witnesses: **Mr David Varney**, Chairman, **Mr Gabs Makhlouf**, Director, Debt Management and Banking and **Mr Roy Massingale**, Self Assessment Product and Process Group, HM Revenue and Customs, examined.

Q1 Chairman: Good afternoon and welcome to the Committee of Public Accounts. We welcome Mr Seeder who is Chairman of the Committee of Public Accounts of the Estonian Parliament, our equivalent, and Mr Saar who is the Director of the State Audit Office; we are having a word with them at the end of this Committee meeting. Thank you very much for coming. Our hearing today is on *Filing of Income Tax Self Assessment Returns* and we are joined once again by Mr David Varney, who is Chairman of the HM Revenue and Customs. Would you like to introduce your team Mr Varney?

Mr Varney: On my left-hand side is Mr Roy Massingale who is Director for Self Assessment in HMRC and on my right-hand side is Gabs Makhlouf who is Director for Debt Management and Banking in HM Revenue and Customs.

Q2 Chairman: Could you please have a look at page 26, figure 10, where it says “Over 260,000 taxpayers had more than one tax return outstanding at July 2004” and I understand that it is now about 240,000 taxpayers; still a lot. I wonder whether you are doing enough about these 240,000 taxpayers who persistently fail to get their returns in on time.

Mr Varney: One of our central jobs is to allocate resources to the many challenges we face and in this particular case some of those individuals will have low tax obligations to collect; others we are trying to pursue. As it says in the Report, we have recently done a spend-to-save initiative with the Treasury, which is using rather more aggressively some of the penalties that we can impose. That has had an impact on increasing the collection.

Q3 Chairman: Is it right that what we are talking about here is around 1.1 million tax returns outstanding, £1 billion not realised? Is that right?

Mr Varney: In total, if you look at self assessment as a whole, because at any stage you take a snapshot, if you take the last 12 months, 90% of the people who were on self assessment filed on time. Within 12

months, we had increased that to 97.8% and of the tax brought to charge through self assessment, we eventually collect about 99.5%. The position over time is that it is a big source of tax collection, so there will be an outstanding amount at any time, but if you look over the whole of the regime, we actually collect 99.5% of the money which is outstanding.

Q4 Chairman: Let us still look at the people who do have difficulties. If you look at figure 14, which you can find on page 34, that figure deals with the most common mistakes that taxpayers make in completing a tax return. I just wonder whether you are doing enough to help these people put in accurate tax returns.

Mr Varney: I would not be complacent. We have redesigned the form, we have taken a million people out of self assessment and tried to take people out where their affairs are sufficiently simple that they can be dealt with by Pay As You Earn. We have redesigned the form and we have put out this short return, which has been well received. We do try to look at the causes of error and then see whether we can trace that back either to our form or our guidance and then, if that is the case, we consult about how we might amend the form or amend the guidance. We are not complacent, but we are trying to see what we can do to improve the accuracy of the returns and also trying to minimise the mistakes that we make internally in processing the return, because another source of error is that we get the right data but we do not record it correctly.

Q5 Chairman: Let us now look at the sanctions you can use to get people to file on time. If you look at page 28, paragraph 2.21, it says: “The Department has not yet developed management information which enables it to monitor the value of sanctions applied against the amount of tax assessed as due”. Do you think you have got the penalties right?

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Mr Varney: There are two issues. Very helpfully, the NAO draw attention to the need to have a better management information system and I think that is a fair comment and that is something we are taking away to work on. The penalties are a judgment call in the end; there is no exact science. It is a decision on what impact you can have and some of the things which we are doing in terms of the daily penalties illuminate that debate. In the end, it is a choice for Government as to what regime they want to put in place and then for us to work it to the best of our abilities.

Q6 Chairman: Do you have the right information to assess the impact of penalties?

Mr Varney: We are doing more work on it, but it could be better. We are going to move self assessment debt management into a new system, which will give us better intelligence, which will help build a better management information system, for which the NAO have rightly called.

Q7 Chairman: Let us look at filing returns electronically now which is dealt with on page 15, paragraph 1.11. It says there "Some taxpayers encountered problems with the online service over the weekend of 29 and 30 January 2005". For 2004–05 17% were filing electronically and you have a 25% target for 2005–06. Do you think you can avoid these problems in the future?

Mr Varney: I hope so and I regret the problems. May I explain what they were and maybe look at the reasons why they emerged and some of the challenges we face? Over the period, 29 and 30 January we successfully processed 139,000 filings, but 80,000 filings did not get a message back saying "We have processed your account and everything is satisfactory". We were able to send them that message on 31 January, but if it was not satisfactory, if their input was wrong, they did not get a chance to correct the error. So we gave them a two-week period in which they could then correct the error and file it. We have looked at the reason why we had a problem and we have tried to re-size the web-based technology we are using. This is probably the busiest piece of the e-government infrastructure and one of the issues which we have to face is the density of traffic in a particular period. Because the filing has to be done by 31 January, what tends to happen rather late on 31 January is that we get a large number of filings and therefore have to collate them.

Q8 Chairman: Let us look straight at that, which is covered in figure 22 on page 42. This shows graphically those peaks which you are encountering. I just wonder whether you should consider changing your filing deadline so that you can avoid some of those peaks in your work.

Mr Varney: That is one of the things being looked at by Lord Carter in his review. He will be making recommendations to Ministers later this year for Ministers to think about. Clearly, from an administrative viewpoint there is benefit if you can smooth the peaks, but that is just the administrative consideration.

Q9 Chairman: It seems that other countries may be organising this better.

Mr Varney: I think other countries organise it differently. The reason that the United States and Australia, which are the two often cited, get such early returns from their taxpayers is that they take rather more money from their taxpayers than it turns out the taxpayer needs to pay. So they have high levels of taxpayers claiming back tax which has been paid. That is a rather neat judgment and not one for me to make I suspect.

Q10 Chairman: I am cautious in this Committee about suggesting that you should impose greater penalties on people, because if I say that, I get angry letters from taxpayers. So what about more of a carrot-and-stick policy then? Why do you not, for instance, give people incentives to file electronically?

Mr Varney: I think that is something Lord Carter is looking at.

Q11 Chairman: What is your opinion of that idea?

Mr Varney: I think it is an appropriate topic for Ministers to consider.

Q12 Chairman: That is very illuminating.

Mr Varney: I was trying to keep your mailbox down. We have used incentives to go electronic with small and medium-sized enterprises. It is a finely judged matter. If you make the incentive too high, you get all sorts of unwanted behaviour; people who would have filed as a single company now file as 10 because they can get 10 rewards for doing so. I think there is a debate to be had about what is right.

Q13 Chairman: Surely not. We are not talking about massive incentives.

Mr Varney: When we do the market research, the thing that most people want is a reliable service and they want the functionality that we could tell them that their return had been accepted by us; that seems to be the biggest attraction. Whilst that is the biggest attraction and given that the amount of filing online is growing, we should stick with that.

Q14 Helen Goodman: My understanding is that 61% of the people who are late with their tax returns have either already paid enough tax or are owed money by the Revenue. That suggests that people are not delaying filing their tax returns in order to avoid tax but simply because they find it difficult to comply with the Revenue's bureaucratic systems. As a general proposition, do you agree with that?

Mr Varney: I think we have gone quite some way to make the systems as user-friendly as we can.

Mr Massingale: The introduction of our short tax return this year, which is four pages as opposed to a minimum of 10 on the main tax return, has been very well received. Our next major move in that course, and we are working on it now and are going to pilot it from next year, is to do similar work on the main tax return to improve the guidance related to that with a view to getting that going by January 2008.

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Q15 Helen Goodman: You have also taken some people out of self assessment, which is a similar sensible step.

Mr Massingale: Indeed, about 1.1 million on a risk base and the NAO have approved that and asked us to look at that further.

Q16 Helen Goodman: Strictly speaking we are not supposed to draw on our own experience, but I will draw on my own experience of filling in my tax form, which is that you receive the papers in May, you put them down in some safe place and you subsequently forget where that safe place is. About two months later you get your P60 and you put that in another safe place, probably not the same safe place. You then realise that you are supposed to fill it all in by September and, interestingly, I see in table 27 that you get a reminder letter on 23 December. Do you think 23 December is a good day for sending out a reminder letter to people?

Mr Varney: Which one would you suggest? Maybe 23 December is not the best chosen, but then 22 December probably would not be well chosen either. We have a process where we are trying to give people enough notice. To make a tax system work you need to get the taxpayer to provide you with information. We are trying to do that and to make it as easy as possible.

Q17 Helen Goodman: Of course I understand that, but when you send out the tax form two months before people have the information that they need to fill in the tax return, that does make it more difficult for people. Bringing those two timetables together would be something that I should like you to comment on. It is all very well to say you have given it over to Lord Carter but you, the Revenue, must surely have some control over what these systems are?

Mr Varney: We have obviously put to Lord Carter some of the considerations which we have encountered in operating the system. He will make recommendations but then it will be for Ministers to decide. On the issue of timing and frequency, there are some comments in the National Audit Office's Report about the fact that our system appears to give more time than some of the other countries with which we compare the tax system.

Q18 Helen Goodman: Quite. The further point in this timetable which makes it tricky for people is that the final deadline is not until the end of January. Possibly bringing the timetable forward to late summer or early autumn might actually make it easier for people to keep in their head that they need to do this.

Mr Varney: We do need to look at that with Lord Carter. That is what he is there for. There are some practical issues around when we can get the information from the companies, when we alert them. I suspect some people have much more economically chaotic lives than you lead, so they will have changed employers and have more bits of

paper. We try to advertise as well for a high level of awareness. What we are trying to do is get as much voluntary compliance as we can.

Q19 Helen Goodman: I appreciate that. I am just trying to suggest that looking at the timetabling would be particularly fertile.

Mr Varney: I shall pass that on to Lord Carter.

Q20 Helen Goodman: One of the problems that the NAO found was that there was insufficient capacity at the call centres during the peak times and that is in paragraph 3.7 on page 33. Another issue, which I think is related to this and relates also to the complexity of the tax return, is the lack of face-to-face advice now for people when they are making their tax returns. Is the Revenue going completely away from face-to-face advice for people on filling in their tax returns?

Mr Varney: No, I do not think so.

Mr Massingale: Not at all, in fact we are proposing to improve the quality of our face-to-face advice, in part by introducing an appointment system so that people can plan their time to receive advice. We have worked hard on our website; it does not suit everyone, but there is some very good helpful advice there. We constantly look at our leaflets and guidance notes to try to keep them up to date and write them as clearly as we possibly can.

Q21 Kitty Ussher: When the Report was written, it suggested that it cost about £22 to process each self assessment tax return. Is that figure still valid?

Mr Massingale: That is broadly right. That is mainly a staff cost and I think that cost does not include the overhead costs of our buildings and, in part, our IT system.

Q22 Kitty Ussher: Is that a cost which you think you can realistically reduce with efficiency savings and the programmes you have in hand?

Mr Massingale: A major way of reducing that cost, and we need to of course, is to increase the level of online filing. Quite clearly our costs are reduced with an effective online system because the costs of data entry are removed and indeed some of the costs of exceptions in the system, because the protocols within the software system can take that difficulty out of it.

Q23 Kitty Ussher: How much is it on average if it is an online application? How much would it cost you?

Mr Massingale: We believe that overall, the cost of an online form at the present time is about £9 less than the cost of the paper form.

Q24 Kitty Ussher: Are you incentivised through PSA targets and that type of thing to achieve those potential savings?

Mr Varney: Yes. We get a remit letter from the Chancellor once a year and part of that is efficiency. The other thing we are doing is looking at the efficiency and accuracy of our own processes and in the report you will find reference to the use of a quality management regime to improve the

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performance. However, there will always be a group of people who will want to use post and paper, so we have to have effective processes for them as well.

Q25 Kitty Ussher: Just to get a sense of the order of magnitude, if self assessment forms were filled in correctly 100% of the time, which of course never happens, how much would the cost per form reduce because you did not have to go and chase people? Is that a small proportion of the total?

Mr Varney: It would be a guess, but it is probably of the same order. It is the electronic gain if we have done it. The great thing about filing online is that a reconciler is put in the form which tells the taxpayer that the information has been accepted; we get clean electronic data, so we get clean addresses. It is hard to get a precise number because we have not been there.

Q26 Kitty Ussher: But if someone completes a manual one perfectly it is roughly the same effect as completing one electronically.

Mr Massingale: I think so, broadly, although even with a perfect paper return we are of course still left with the cost of data entry which we have to do manually.

Q27 Kitty Ussher: Staff costs; of course. For the paper returns, which make up the bulk of your returns and, as you say, there will always be people who prefer to submit by paper, I am certainly one them unfortunately, what efforts have you taken to minimise the mistakes that are routinely made? There is an interesting table in the Report which highlights that people often get their pension contributions wrong and various capital allowances and so on; certainly it is inherently confusing. Do you have an action plan to address each of those particular issues?

Mr Varney: We wrote letters to 180,000 people who were most likely to make errors. Inevitably, when you are dealing with large populations like we are, 40 million, you are always trying to find segments at which you can target your interventions so they can be effective and that is what we have tried to do. We also look at what we think are the errors in the system and try to see whether we can work out where the fundamental cause is coming from.

Q28 Kitty Ussher: Do you work with the private sector as well? For example, do you work with private pension companies to make sure their yearly tax returns are absolutely clear about which bit you should put in?

Mr Varney: We have a thing called Closer Working, which is an engagement basically with advisers. They reflect back to us problems and issues, plus we have what we get from our own internal management information; we work together. If anybody has ideas, they tend to come to us pretty quickly. We tend not to be short of advice about how we can change the system.

Q29 Kitty Ussher: Do you have another comment?

Mr Massingale: The major piece of engagement that we are involved with is through third party software vendors who support not only individuals who want to return online but also agents and various intermediaries, tax accountants and the like, who want to use their products. We work very closely with that community to ensure that their products meet the requirements of the system and so on and so forth and provide them with test facilities to ensure that what they generate on their machines is a proper replication of our system and the rules and regulations.

Q30 Kitty Ussher: I am sure that is useful, but I was thinking more of Helen Goodman's example of piling up bits of paper during the year and wondering what to do with them. You have several different bits of paper, potentially from your bank, from a private pension, potentially all sorts of different bits and pieces and it is not often clear which should go in which box if you do not want to employ an accountant or have a piece of software. Have you thought about perhaps ensuring that the private sector writes clearly on the bank statement when you have the interest coming in, that this is what you should put in box 16.24 or whatever it is? Is that something that you would consider doing?

Mr Varney: What we have tried to do is to take out of the system those people whose affairs are simple, that is the million we have already done. The shorter tax return is meant to address those people whose affairs are still sufficiently simple that they can fill in the form and get an accurate return. As people's affairs get more complicated, it then becomes correspondingly more challenging and that is why we have the full tax return and we are going to pilot a redesign of it and see whether that produces a better outcome.

Q31 Kitty Ussher: Could you explain how much it costs the public purse for someone who files in September as compared to filing in January for both electronic and manual? Does it make a difference to you?

Mr Varney: There is a small cost advantage from early filing. We should prefer that people filed as early as they could and we try to encourage that. It is not easy to persuade people to do that.

Q32 Kitty Ussher: Are you able to quantify the effect on the public purse?

Mr Varney: It is a quite small timing effect. We have not quantified that, but it is quite small. What we do is encourage people to file and pay as early as possible. We get about 80% of the money in by the end of January.

Mr Makhlouf: We do. I think your question was whether the cost of processing was different between the end of September and the end of January and I think the answer is that the differences are too small. It is more the consequences of people filing late or filing too close to the deadline which has been some of the discussion that we have just had. The earlier people file, the easier it is for us to avoid peaks which

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create costs. I do not think we can actually see a material difference in the costs. If it is the £22 figure that you are interested in, I am not sure we can actually see a big difference between the £22 figure, whether it is September or January; not at this stage.

Q33 Kitty Ussher: You are trying to encourage people to file by September by using various incentives such as not having to calculate the tax, so that is simply to get it in?

Mr Makhlof: Yes; to get the return in, that is right. You can actually get the return in online by the end of December and have the facility which is offered for returns on paper by the end of September, which is a fact which is not very well known.

Q34 Mr Bacon: Mr Varney, in paragraph 3.4 on page 32 it refers to the random enquiries and the risk based enquiries which are undertaken for both corporate and personal returns. It says at the bottom of that paragraph that 78% of such enquiries detected non-compliance, which sounds quite high I suppose. Nonetheless, out of 200,000 it means that around 22%, 40,000 have nothing wrong at all. Do you think you could do something to improve the targeting? Plainly, not only is it a huge hassle for those 40,000 people, but it also turns out to be a waste of your inspectors' time, does it not?

Mr Varney: The random enquiries show roughly a 30% yield and those targeted over 70%. So those are partly the fruits of being more accurate in terms of targeting. Our challenge is that about 5% of cases account for 70% of lost money which we are trying to get to, so we need to find and hit the highest yielding part of that 5%.

Q35 Mr Bacon: What criteria do you use to come up with the 200,000 that you have come up with which are risk based?

Mr Varney: We go through and look at their experience of filing in the past.

Mr Massingale: In our local offices, we have put a lot of effort recently into more systematic risk-based programmes. We have national programmes focusing on particular trades where we think there might be high levels of risk and we also allow our local compliance teams to develop locally based programmes of work based on their experience of the local area and where they think the risks lie. We do quite a lot of work researching the internet, researching local newspapers and so on and so forth.

Q36 Mr Bacon: What are the particular trades that stand out as being high risk?

Mr Massingale: The construction industry has been a long-term high risk trade; obviously anything with a high volume of cash in the business, cash retail, the entertainment sector around clubs, licensed premises and the like.

Q37 Mr Bacon: The previous line talks about just 5% of returns accounting for around three quarters of the total tax at risk. The problem may be deliberate

non-compliance by sole traders, but might it not also be complexity on your part making life more difficult for them?

Mr Varney: When we get involved, often the case is that something has not been seen as needing to be reported or there is a trial. There is an element of that. We have tried to simplify this. We have a dilemma which is that we try to simplify the forms. The guidance, which becomes the subject of legal action when we are litigated against, has to be comprehensive. So we are continually between trying to keep the forms as simple and as clear as we can but making the guidance as comprehensive and proof against legal attack which says we did not provide the right guidance. It is a dilemma.

Q38 Mr Bacon: When you said you look at previous history of filing, I take it you were talking about behaviour rather than whether they filed on time or not.

Mr Varney: Yes; whether we had found something before. At my first appearance in front of the Committee of Public Accounts, I was explaining that we also believe that some element of random checking has a deterrent effect and it is unfair perhaps on the individual who is selected if we do not find anything, but it does deter people.

Q39 Mr Bacon: May I ask you to turn to paragraph 3.22 which is on page 37? "The Association of Chartered Certified Accountants has carried out annual surveys since 1997 . . . In their February 2004 survey they found that 61% of respondents had experienced cases of penalty or reminder letters issued to their client where the return had been submitted on time". In other words, it was not because they were not doing anything right, yet they were still getting penalty notices or reminders where they should not have done. It goes on to say "80% of respondents reported having to spend extra time on their client's Self Assessment returns due to errors on the part of HM Revenue and Customs". That is not really good enough is it?

Mr Varney: No.

Mr Massingale: This is something we have been very concerned about and we have regularly surveyed the number of wrong penalties we have sent out. I think we find that there are three reasons for them and I think we have action in place to try to reduce the levels and indeed have reduced the levels to something around the 1% mark now. One of them is duplicates in our databases and we are looking permanently to clean up our database, in fact we have a structural clean-up there. The fact that we simply do not log the returns in is slightly unforgivably on our part and we have introduced a better system of control around that, batching particular numbers and checking then that those batches have been fully logged and that there is a match there and the final main cause—there are three—is people who have ceased to be self-employed or ceased to be within the self assessment system who have not been cleared from our records. We have been working very hard on the work list that illustrates that. It is something where we do not

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have a very good record, but we have improved greatly. We think we understand what those main reasons are and have programmes of work to cover each of them.

Q40 Mr Bacon: What about those people who are no longer required to complete a return, who drop out of the regime as it were? What are you doing to ensure that you are notified if their circumstances change, making sure that they do not necessarily drop out for ever? It is plainly the case that some of them will have dropped out forever, but equally it is obvious that many will or ought to come back in. What are you doing to make sure they do not drop out and drop off the map forever?

Mr Massingale: We have removed 1.1 million systematically from our system, but in fact if we think about it, the system is fluid in any case. People will come up to our criteria and move away from our criteria quite regularly anyway. We have systems which recognise the factors which bring people in and out of self assessment and, each year run those factors against our databases to correct the situation. The criteria are public criteria. They are on the internet and people know or can see what they are.

Q41 Mr Bacon: You have a target, according to paragraph 3.7, for increasing by 2007–08 the accuracy and completeness of information and advice given when there is contact with members of your staff to at least 90%. What steps are you taking to make sure that you reach that target?

Mr Massingale: We have, as you know, gone very heavily into call centres on the grounds we believe they are giving a better and more consistent service as well as on cost. We have put a lot of energy into training. Some of the things we have found are that people we have recruited newly for this work in fact can provide a better service because they are not encumbered with perhaps the fables of the past. We do put a lot of very systematic training into that territory. We have our frontline, our first-line staff supported by more specialist staff who can take the more detailed enquiries which lie behind the more obvious ones.

Q42 Mr Bacon: Paragraph 3.7 of the NAO Report about call centres is telling. “All stakeholders commented on the difficulties of getting through at peak filing times”. So long as you have a system where you have peaks and troughs caused by deadlines, that is inherent is it not? Is there a limit to how much you could do through training, if you are going to have to get extra staff in for dealing with peak times?

Mr Varney: There is a point at which, no matter how much money we have, providing the facilities to answer calls would just be almost impossible because of training.

Q43 Mr Bacon: If there is an inherent problem there, which I think there is, is your strategy to move away from having created deadlines?

Mr Varney: Our strategy is to take people out if they do not need to do the system, to go for e-filing, to encourage early filing if we can and offer benefits and inducements to file early. So it will calculate your tax liability for you if you give us a paper return in September. That is the service, in return for which we get, hopefully, more people giving us the data. We are also putting our telephone answering capability into tiers, so that the most difficult questions which come in can go to the most knowledgeable and not clog up the system. Given that we operate a range of tax regimes, they are going to have different peaks so we can move the resources from one tax regime to another to help some of these peaks. However, there will always be an issue if you have a filing day. If people wanting to file at the very last minute want to ring up, they will want to ring up on the 31 January and our system is going to be under huge, huge pressure.

Q44 Mr Khan: Helen Goodman gave you the hypothetical example of a disorganised Member of Parliament who, for various reasons, does not get the return in on time. What are your opinions on having an eight-month period within which to file tax returns for the previous financial year?

Mr Varney: That is something Lord Carter is looking at.

Chairman: We are going to have a very boring hearing, if we are constantly referring to Lord Carter.

Q45 Mr Khan: I deliberately changed my question to ask you for your opinion as I did realise you would say that.

Mr Varney: It is one of the features, if you do ask somebody to look at something, to listen to what he has to say.

Q46 Mr Khan: Without prejudice as to what Lord Carter may find, what are your views on having an eight-month period, bearing in mind other countries have a much shorter period? Would that help you?

Mr Varney: Yes. We are going to give the NAO Report to Lord Carter—in fact he has got it—so that he can see what the comparison is with other countries.

Q47 Chairman: You are not prejudicing what Lord Carter is going to say by giving your own opinion now.

Mr Varney: No, and he will make that very clear. It is a balance in the end. It is not that if you made it seven months rather than eight, you would immediately get people giving it their attention. It is a judgment call as to when people have the information, how they are organised and we know that people have got used to the current situation. What we are trying to do is persuade them voluntarily to bring forward their return. If the Government desires to make a move, then we shall make that work to the best of our ability.

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Q48 Mr Khan: May I say, it is a criticism, that I am no clearer as to your views two minutes after you began answering the question? If, for example, the date for returning this were nearer to when people receive their P60, what would your views be on that?

Mr Varney: The issue is that you have to pull together. It depends on the complexity of the case, the individual's circumstances. If you have a large number of bits of paper, you have to work out the critical path, the last date and I suspect moving it forward will have some benefits to us in terms of the administration, but it will also lead to a new set of issues which we will have to deal with as people think about their work. A lot of people are dependent on specialist advice and those specialist advisers do not only do income tax, they do other forms of tax. We would look, if you were to move the date, at what it would do to other tax regimes and other peaks. It is not a straightforward question. I am not trying to be obscure; I am just saying that there are various trade-offs.

Q49 Mr Khan: May I just ask you about this? We see from the Report that last year approximately 5% of mistakes were made in processing returns, the year before it was 6%. Bearing in mind that some of the poorer people who will fill in returns will not have an agent or expert to advise them, do you think you are doing enough to identify and alert taxpayers who may have had their tax return incorrectly processed?

Mr Varney: We have done some more work. We have an automatic coding, a piece of IT which is going in, to remove about a third of the coding errors; so we have made an improvement there. What we are doing is trying to bring as much management quality into this process as we can. We are trying to take out of the system people whose circumstances are relatively straightforward or make sure that they do a short return, which we try to make as straightforward as possible. We have not designed the system so it needs an agent. We have designed it so that it can be worked by the taxpayer.

Q50 Mr Khan: My point, Mr Varney, is this. If somebody has an agent, it is more likely, is it not that he or she will be aware of the mistake that you have made. It is somebody without an agent who will be unaware of the mistake made and, for example, we see 50 million people have been overcharged due to mistakes made by your team.

Mr Varney: We have a rolling process in this and we try to see what the errors are. We try to spot them and we try to encourage people, if they do not think it is right, to come back and challenge it, then we look at it again. That is what we try to do. We are trying to reduce the number of errors which we generate on our side, making it easy for the people to fill in their forms, because that is the best way of making the system work.

Q51 Mr Khan: Just before I move onto the next topic, how do you encourage people to challenge you?

Mr Varney: We have explained that this is what we think is their assessment, this is how we have arrived at it and then it is up to them to come back.

Q52 Mr Khan: Okay. As far as tax codes are concerned, I see from the memorandum that last year your Department was 73% accurate and the year before 71%. What sort of figure should we expect in accuracy?

Mr Massingale: We are not at all complacent about these figures; we are not at all happy about them. Perhaps I might just elaborate a little more on what our chairman has said and what we are doing about them. First of all, we do manage to track and correct about two thirds of our errors and are constantly working in our management chain to identify common causes of error and feed them into our management systems.

Q53 Mr Khan: Is this tax codes or processing?

Mr Massingale: This is both. Tax codes are a major source of error.

Q54 Mr Khan: The question I asked was: what sort of percentage of accuracy for tax codes should we expect? It was 73% last year and 71% the year before. What figure is acceptable?

Mr Massingale: I should say that we should expect it to be much higher than that.

Q55 Mr Khan: Right. So what figures can we expect to see for the current year?

Mr Massingale: I cannot give you a prediction of what would happen for this year. I can tell you the sorts of things we are doing to try to improve these matters. We have recognised that one of the issues for us has been that our quality management systems have tended to be too lagged. We have examined our quality too far away from the event and we are trying to bring quality management much more into real time in our local offices.

Q56 Mr Khan: So the graph will go upward 71, 73, this way would it?

Mr Massingale: We would expect the graph to go up quite considerably.

Q57 Mr Khan: I have already explained my concern that those who have no agents are not being made aware of errors that you make in processing the claims. I also read that only half of sole traders and partnerships file accurate returns; I suspect because they tend to be smaller partnerships and clearly sole traders by definition are small. What more help do you think you can give to improve their compliance?

Mr Varney: We do run education schemes, which are meetings for people starting up businesses, trying to explain to them what the tax system is and what their obligations are coming into the system. In terms of the information we put out, we try to make it customer friendly and we do answer questions but we approach this in a sort of multi-layered way, trying to help people with the information that they have the capacity to absorb and to use.

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Q58 Mr Khan: I see from page 23 of the NAO Report that after spending £25 million on Hector the Inspector, the conclusion was that it should be withdrawn because it was a stereotypical and inaccurate image of HMRC. We then spent £6 million on Mrs Doyle, which was withdrawn because it did not meet the objective of increasing filing by the end of September. We have now spent £15 million on an advertising campaign which seems at this stage to have been unsuccessful because there was a continuing deterioration in the percentage of taxpayers filing by end September. I am assuming you have changed the advertising agencies in those three examples, have you?

Mr Varney: I do not know, to be honest. For the last one, the ongoing latest results are 90.6% for the year to January 2005 and 44.8% for September 2004. So it has gone up and we have seen e-filing up by 400%. We think this last campaign is still working and still producing results. Our media tracking says the campaign researches very well. It is in the nature of what we do that we shall be changing our advertising presentation to reflect the impact it has.

Q59 Mr Khan: It says in the Report that you are unable to trace 85,000 taxpayers with outstanding returns. What are your views on an amnesty?

Mr Varney: If we are unable to trace, we have various schemes now across Europe to enable the exchange of information. I am not really in favour of an amnesty. If those people do not want to be found, then they are trying to avoid and evade tax and we shall treat them accordingly. Encouraging them to come forward is not a particularly useful way. I have seen other revenues have tried something like that, but that is primarily to bring money from overseas into the country. I am thinking about the Belgians and the Americans who gave tax breaks to do that.

Q60 Greg Clark: Will you be giving evidence to Lord Carter?

Mr Varney: Yes.

Q61 Greg Clark: What will you be saying on the question of whether an earlier deadline might be appropriate?

Mr Varney: I shall be saying the same thing as I have said to the Committee.

Q62 Chairman: That will be a very boring conversation.

Mr Varney: It will be very boring. I shall explain to him that in any network you are obviously interested in whether you can move the peak down into the valley so that you make it more even. The difficulty and challenge in this is very much the political judgment, how much change, whether it will actually achieve the results and where self-assessment fits against other tax regimes. I shall be giving him that. What I cannot give him and which I should like to give him, but I do not have the information, is the cost benefit analysis of various alternatives. We just do not have the information for that.

Q63 Greg Clark: Why not? Is that not important? You are the expert in the subject. You are the man who is in charge of the Revenue. Surely he must depend on that information. I do not understand the great secrecy around it.

Mr Varney: There is no great secrecy; it is not there. We are in the process of building a management information system and I have been saying pretty frequently since I arrived that one of the needs is to get in a quality management information system which can answer these sorts of questions.

Q64 Greg Clark: You can give him no information which will enable him to come to a judgment as to the costs for you to have an earlier deadline.

Mr Varney: I can give him information, but it does not lead quickly to an answer. We can illuminate a lot of these issues with some research, we can give particular pictures, but if you asked me for the cost advantage of this date as against that date, we should give some impressionistic information but we just do not have that quality of research.

Q65 Greg Clark: So you are not going to give him your view as to whether it would be desirable or not to have another deadline.

Mr Varney: I shall tell him what we think the tradeoffs are, what we think will be the response from consumers to various ideas which he has.

Q66 Greg Clark: What do you think the response from consumers will be to an earlier date, say a November deadline?

Mr Varney: It will take a bit of time to bed in and there will be some transition issues along the lines mentioned by Helen Goodman. The people who get the letter are likely to put it to one side and think it is the same thing as last year, so there would need to be quite an advertising campaign. I suspect the accountants would have quite strong views about whether this was a good idea, because it will affect them. One of the frequent comments they make is that the reason they file at the last minute generally is the workload they have among their customers of filling in their tax forms for them.

Q67 Greg Clark: When do you get to give your evidence to Lord Carter?

Mr Varney: Shortly.

Q68 Greg Clark: Within the next few weeks, the next few months?

Mr Varney: I have had a dialogue on and off with Lord Carter from time to time and also we are interested in what the IT implications will be.

Q69 Greg Clark: May I ask you to write to the Chairman of the Committee with a copy of your evidence to Lord Carter?¹ We can joke about this, but this is seriously frustrating. We have an NAO Report here entitled *Filing of Income Tax Self Assessment Returns*, which presumably entailed considerable expense, we have seven Members of the

¹ Ev 13-19

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Committee, three members of the NAO, a representative of the Treasury, meeting here in order to guide public policy on how best this should be in the future and we seem to have responses which are vague. We are all in it in order to improve value for money and it would be helpful if some of this information which you are about to discuss were shared with this Committee before we make our report, which will entail some expenditure of resources. Do you think that a reasonable request?

Mr Varney: I think it is reasonable. I have reached a situation where by and large I have been talking to Lord Carter as his thoughts have been developing and I have been trying to ensure that we provide him with as much information as we can to illuminate the sort of choices that he wants.

Q70 Greg Clark: Could you provide the Committee with that sort of information?

Mr Varney: I shall be happy to provide that to the Committee.

Q71 Chairman: There is no reason why you should not want to provide us with information and illuminate us just as much as you want to provide information and illuminate Lord Carter.

Mr Varney: I am trying to.

Q72 Greg Clark: Specifically we should all be grateful to see the written information you give Lord Carter.

Mr Varney: Whatever written information there is I am happy to share.

Q73 Greg Clark: Paragraph 4.2 of the Report suggests that the average cost of filing a tax return is £22 and compares it with £60 for a typical income support claim. Do you have an understanding of how much an average tax credit application costs to process?

Mr Varney: No, not at my fingertips.

Q74 Greg Clark: Do you think it is more than income support or less than income support.

Mr Varney: I have a feeling that it is less than income support. I just do not have the numbers at my fingertips.

Q75 Greg Clark: Will you write to the Committee?

Mr Varney: Yes; certainly².

Q76 Greg Clark: That would be helpful. Do you make comparisons between different types of benefits to see what best practice is and if some system is particularly efficient, do you learn from them?

Mr Varney: It is a bit more complicated than that. You can look at the costs of various tax heads and we are trying to do more of that. There is a limit to how much value you can get out of a comparison between different taxes, because they often illuminate the regime. They have different environments, they apply to different populations.

What we are also trying to do is to see what benchmarking can be done with other revenues to see whether there is any information there which is useful. The problem is that the way it tends to be done is that we receive rather dense documents from OECD, which is where we all exchange this information. Often you then have to go into definitional issues.

Q77 Greg Clark: Presumably one of the advantages of having this great new department which has every benefit, every tax conceivably levied there, is that you can compare and contrast and get to some view of best practice.

Mr Varney: Where we do want to get to best practice is on quality and the costs, as we get better information, will help, but quite a lot of the work we are doing is focusing on the quality of our processes, learning about common issues.

Q78 Greg Clark: Not on costs. Are you not going to take any lessons from the cost of processing one set of benefits, for example tax credits and apply those lessons, good or ill, to other benefits?

Mr Varney: We are talking two sides of the coin. I am talking about the management intervention which produces the outcome which is cost. I just do not think that looking at cost of itself is the issue. What we are trying to do is get behind that look at quality. That is what we are trying to do.

Q79 Greg Clark: I would hope that costs are part of it as well as quality. On costs, paragraph 4.7 of the report lays out some of the differences in processing capacity which some of your centres have. You make a commitment to more centralised processing and suggest that will save some costs. You give a figure of 200 to 300 staff years, which I assume is a full-time equivalent to 200 to 300 people. Is that a big saving? How many people work in the filing of income tax self assessment returns?

Mr Varney: We have about 8,000 full-time equivalent staff members on the processing side and on the debt management side something like 1,800.

Q80 Greg Clark: So 8,000 plus 1,800 and the best estimate of the savings from this great efficiency review of centralising processing is 200 to 300 staff, according to paragraph 4.7. That does not seem very much.

Mr Varney: That is based on lifting the performance of the processing centres. We are making a whole series of interventions to try to see what we can do to lift the overall standard beyond the three best.

Q81 Greg Clark: Is that right? Are you making 200 to 300 staff years of savings or is there a higher figure?

Mr Varney: No, we have at the moment 200 to 300 which are in our plans so far.

Q82 Greg Clark: So this great review of centralising administration is just going to lose 200 to 300 people out of the thousands you have working for you.

² Ev 21

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Mr Varney: I am trying to talk about two different things. What that paragraph says is correct, if we rise to the standard of the three most efficient offices. Are we comfortable with their efficiency levels? No. We have a programme which is talked about in here which is seeking much greater efficiency savings. That will come from the quality of training, redesign of process, involving the people who do it and a big investment in frontline management capabilities.

Q83 Greg Clark: I just find it very mysterious that there is such a great disparity of efficiency and bringing the bottom up to the top is only going to make a nugatory difference to staffing levels, but that now seems to be it. On guidance with filling in forms, one of the problems which means there is more work for you is that you get incomplete or incorrect forms which you then have to reprocess. You have helplines. At what times are they available? Are they open for 24 hours?

Mr Massingale: Our main helplines are available from eight o'clock in the morning to eight o'clock in the evening.

Q84 Greg Clark: Is there a reason why they need to finish at eight o'clock in the evening?

Mr Varney: Just cost; it is a cost efficiency argument of whether you think people are going to ring in the early hours of the morning to do their tax return.

Q85 Greg Clark: Have you made an assessment and determined that they do not do them after eight o'clock in the evening?

Mr Varney: We have not come under a great deal of pressure to do that.

Q86 Greg Clark: When you say "a great deal of pressure", how would you detect this pressure?

Mr Varney: You talk to customers, you talk to intermediaries. This is a public process in which we get a lot of feedback.

Q87 Greg Clark: I should be surprised if you were to do a survey if you did not find quite a lot of people, particularly the people Mr Khan mentioned who perhaps do not have professional advisers, might fill in their tax returns after work, in other words between eight and 10 in the evening. Do you find that a surprising suggestion?

Mr Varney: We do not see that pressure. I think it is more a tribute to your imagination than reality. I do not think there is a large demand.

Q88 Mr Williams: Following on the figure Mr Bacon used of 80% of chartered accountants saying that they spend extra time rectifying your errors, does that imply that for those who do not employ accountants, but try to do these things themselves, these errors probably go largely undetected?

Mr Varney: We hope not.

Mr Massingale: We are trying to improve our internal performance.

Q89 Mr Williams: That was not the question I asked you. I know you are trying to improve. All I am asking is whether it means, for those who do not employ accountants, that the probability is that they go undetected.

Mr Massingale: To the extent that we do not detect errors we have made ourselves, they are in large part detected by our customers.

Q90 Mr Williams: Do you know how many people in the vulnerable areas do not use accountants? I suppose the majority do in fact.

Mr Varney: We are trying to take those people with simple affairs out of the tax system.

Q91 Mr Williams: We understand that. I see that you failed to update tax codes for over 600,000 people and you made two million tax coding errors, which are very large numbers. You and I have been exchanging correspondence in relation to a constituent of mine in such a situation and you imposed the duty entirely on the taxpayer to identify your failures as far as the coding was concerned. You seem to accept no responsibility for getting it wrong.

Mr Varney: We have invested in some IT to try to improve the accuracy. We have accepted that we do need to improve it.

Q92 Mr Williams: That is not my point. I am asking about imposing the duty on the taxpayer. Though I do not know how many around here bother to check their tax codes, I must admit that I am terribly remiss and do not and I suspect an awful lot of people do not check their tax code and many people may not even be aware of what their tax code entitlements may be. Errors on this scale and the imposition of a duty on the taxpayer seem grossly unjust.

Mr Varney: The taxpayer is in command of the information on which the assessment is based. We try to make as transparent as we can why we have reached the decision we have on the coding and then, if we have made an error, they come back and we correct it.³

Q93 Mr Williams: If they spot it. When they come back later I was fascinated to find that you are so conscious of the money which is coming in and yet we are told that apparently you do not know how much compensation you pay out as a result of the Department's errors. That is in paragraph 3.19. Why is that?

Mr Varney: I think that was correct information⁴.

Q94 Mr Williams: I did not ask whether it was accurate. I asked you why. We assume it is accurate because we know you have cleared these figures with the National Audit Office and we are not here to argue about the figures. I am asking you why you cannot tell us what compensation you have paid out.

³ Note by witness: Self Assessment operates on an annual cycle and any coding errors in one year are corrected in the following year.

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Do you not keep any track of it? How can you be sure that the money which has flown out is properly accounted for?

Mr Varney: It is properly accounted for.

Q95 Mr Williams: You say it is probably accounted for but can you say that it is certainly accounted for?

Mr Varney: I said that it is properly accounted for.

Q96 Mr Williams: Probably accounted for is less than certain it is accounted for. We actually expect you of all people to be in control of your figures and yet you sit there, the Revenue, saying you do not know how much your people are paying out in compensation. I find that staggering.

Mr Varney: When the NAO came in that was one of the things they uncovered in the report and we think this report is very helpful and illuminates areas.

Q97 Mr Williams: It could be £1 million, £2 million, £3 million, £10 million, £20 million. You do not know.

Mr Varney: No, I do not.

Q98 Mr Williams: You just do not know. This gets rather worrying when we look at the cost of some of your errors. We are told that errors led to £70 million being undercharged and £50 million overcharged; you have detected errors of £120 million. These are large sums of money where you have gone wrong. First of all, how do you determine compensation? Whoever receives a letter does not just say they will drop the taxpayer a note and give them £10 compensation. There must be a system. There must be some accounting process for it. Why are these figures not aggregated?

Mr Varney: They were not aggregated.

Q99 Mr Williams: If one of the people whose tax return you are dealing with were to say they had not bothered to add up the figures, you would not be very impressed by that, would you?

Mr Varney: No, but—

Q100 Mr Williams: We are entitled not to be very impressed by you.

Mr Varney: You are entitled to have your views.

Q101 Mr Williams: Yes, I am entitled to my views, but I am also entitled to know what has happened to the money, that is what this Committee is about. Where is it? How much is it?

Mr Varney: I am telling you that at this stage, when this Report was done, we did not know and that is regrettable and that is something which the NAO has drawn to our attention and we need to improve the management information. That is what we will do now.

Q102 Mr Williams: You know that you incorrectly imposed late filing penalties on 30,000 taxpayers. You know what you imposed on them. How many people then got compensation? Do you know in how many cases compensation was paid?

Mr Varney: Do we? We do not. If they wrote back and said they thought it was unfair, which they do, they say “You say we late filed, but we did file on time”, we realise that we need to improve the logging system of collecting the data, which is what we are doing.

Q103 Mr Williams: Who makes the decision? Let us get back to that first of all. Who decides whether someone is entitled to compensation? At which level in your system is it decided that compensation is due?

Mr Varney: That would probably be within the distributed processing organisation and there would be guidelines and those guidelines would say—

Q104 Mr Williams: How would you know whether the guidelines were being observed, if you did not know how much was being paid or for what?

Mr Varney: In trying to control this, the question is whether it was properly authorised.

Q105 Mr Williams: How can you try to control something when you have no idea what it is?

Mr Varney: We do not know what the sums of money are in total, but that is not to say the individual items will not have been properly authorised in accordance with the policy for giving compensation.

Q106 Mr Williams: We are getting nowhere on that. I hope that by the time you come here next time you will have tried to address this problem, because we should probably like to return to it. I see that three quarters of the tax loss, which is £2.8 billion, is accounted for by 5% of returns, which is around 400,000 people. That works out at about £5,000 each. We are told that half the inaccurate returns are from partnerships and sole traders; half of them are coming from the same place every time and it is £5,000 per year on average. Does that mean that the same people are year after year making similar mistakes? Are you sure a lot of them are not getting away with it?

Mr Varney: If we find that there is a mistake, we try to provide advice, if we can identify who the people are. There is some degree of fluidity in this. Obviously what we try to do is to provide those who are making errors with the information and the explanation to encourage them not to make those errors. We have been able to mop up returns over a number of years in some of the areas where we have been using the daily penalty regime.

Q107 Mr Williams: Let us come back to the people who have been undercharged. Do you sometimes write that off? We know you do in fact.

Mr Varney: Yes.

Q108 Mr Williams: Do you know what that comes to, because that is different from compensation, or is it counted within the compensation figures?

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Mr Varney: Undercharging is more difficult. If they are undercharged and they still have an ongoing relationship and we become aware that they have been undercharged, then, as long as it is not outside the statute of limitation, we can collect it.

Q109 Mr Bacon: I have a couple of questions about e-filing. I understand that for the corporate sector e-filing is more advanced than for personal taxpayers and indeed companies above a certain size must file online. Is that correct?

Mr Varney: Yes.

Q110 Mr Bacon: What is the threshold above which you must file online?

Mr Massingale: The new mandatory regime for Pay As You Earn employers' filing requires employers with 250 and more employees to have filed online this year. The requirement moves to employers with 50 or more from next year.

Q111 Mr Bacon: There were stories in the press, though you cannot always believe something just because it was in the press, about people being unable to file their corporate returns on line because the system was not working properly. Is it correct that processing was stopped?

Mr Massingale: I do not believe there was any serious problem about filing online.

Q112 Mr Bacon: Is it correct that processing was stopped? Yes or no. Was processing stopped?

Mr Massingale: I do not think the question is capable of a binary answer.

Q113 Mr Bacon: By "not capable of a binary answer", do you mean you are not capable of saying yes or no to the question? Was processing which should have been taking place not taking place because the system was jammed?

Mr Massingale: There was some delay in some of our back-end processing but we had no problem about receiving employers' returns.

Q114 Mr Bacon: There was delay.

Mr Massingale: No.

Q115 Mr Bacon: Was any money involved? Was there money which should have been collected which was not collected?

Mr Massingale: No.

Mr Varney: The information which was collected was held in a stockpile so that it could then be fed through to the processing.

Q116 Mr Bacon: And has the stockpile now been cleared?

Mr Varney: Pretty substantially; yes.

Q117 Mr Bacon: Is it possible you could send us a note about that?⁵

Mr Varney: Yes.

Q118 Mr Bacon: And will you?

Mr Varney: I shall, of course.

Chairman: Thank you very much, Mr Varney; that concludes our hearing. We look forward to receiving a full note on your evidence for Lord Carter. Thank you very much.

⁵ Ev 22

**Letter from Mr David Varney, Chairman, HM Revenue and Customs to Chairman,
Committee of Public Accounts**

In anticipation of the Committee's scheduled oral evidence session on 14 November 2005 in respect of the Comptroller and Auditor General's Report on Filing of Income Tax Self Assessment Returns please find attached information updating some of the statistics within the Report.

UPDATES TO FILING STATISTICS

- At July 2005, there were around 1.1 million overdue returns (all previous Self Assessment tax years).

[Report reference: Executive Summary 6, paragraph 2.3 and footnote 6.]

- At July 2005, there were around 240,000 taxpayers with two or more returns outstanding, and 11,000 with 6 or more returns outstanding.

[Report reference: Executive Summary 10 and paragraph 2.14.]

- At July 2005, there were around 85,000 taxpayers subject to tracing action by the Department.

[Report reference: Executive Summary 10, paragraph 2.18 and figure 11.]

- At July 2005, there were around 34,000 taxpayers with two or more returns outstanding who were insolvent or living abroad.

[Report reference: Executive Summary 10, paragraph 2.18 and figure 11.]

- The 2004–05 level of accuracy in processing returns and value of undercharging and overcharging errors were:
 - 2004–05 processing accuracy was 95%;
 - 2005 undercharging errors totalled £64.8 million;
 - 2005 overcharging errors totalled £30.2 million;
 - 2005 total tax effect was £95 million;
 - 2005 PAYE coding accuracy was 73.3% which equates to 2,046,976 errors.
 (The number of coding errors is the estimated number of errors and not the number of taxpayers affected. We estimate the number of Self Assessment taxpayers in 2004–05 with coding errors was 1.4 million.)
- [Report reference: Executive Summary 16 and paragraph 3.11.]
- Around 500,000 returns due on 31 January 2005 for the 2003-04 tax year were still outstanding at 31 July 2005.
 - [Report reference: paragraph 2.3 and footnote 6]

30 September filing figures

- The Department estimates that the number of 2004–05 returns filed by 30 September 2005 was 3,713,322, which includes 641,000 (585,000 last year) filed online. The management information supporting this figure will be verified in the next few weeks.

The number of returns filed by 30 September is 720,000 less than the same period as last year. This can be substantially attributed to the change in criteria for filing a tax return and the consequent removal of about 1.1 million of our most compliant customers.

Supplementary memorandum submitted by HM Revenue and Customs

Question 69 (Mr Greg Clark): Information provided by HMRC to Lord Carter

DIFFERENTIATED FILING: SELF ASSESSMENT

1. PROPOSAL

This proposal is to bring forward the paper filing deadline for Self Assessment returns from individuals (SA100 and SA 200), Trusts (SA900) and Partnerships (SA800), leaving the online filing deadline as 31 January.

To take effect for returns for the 2006/07 tax year, i.e. returns and notices to file issued in April 2007.

This would increase take-up of online filing, reduce the work caused by processing paper returns, and bring forward the reduced peak in paper returns, allowing more time for them to be processed.

We don't favour extending the SA filing deadline for online filers. The filing date for SA is already generous (at 10 months after the end of the tax year) and longer than the time provided to file equivalent forms in other tax regimes. We understand that this view will be supported in the NAO "Study on Filing of Income Tax Self Assessment returns" due to be published in Spring 2005).

We also do not intend any changes to the payment due date. We are advised that to vary the payment due date may leave us open to challenge under the Human Rights Act (HRA), whereas the differentiated filing proposal does not run the same risk.

A possible variation on the earlier paper filing deadline, which might be presentationally more attractive, would be to leave the filing deadline at 31 January for both online and paper returns, but charge a paper filing fee for paper returns received after a certain date.

2. SA DIFFERENTIATED FILING: SPECIFIC AREAS FOR CONSULTATION

We would consult on:

- (i) What additional help, reminders, would be needed to ensure un-represented taxpayers understood the new requirements?
- (ii) What help that might be needed for represented taxpayers and their agents? How best can we work with agents to minimise the impact of the change?
- (iii) What special arrangements might we consider in the first year(s) to ensure soft landing?
- (iv) What are the appropriate penalties/compliance action for filing paper after the deadline [or appropriate level of filing fee] with cross reference to consultation paper on HMRC powers?

3. SA DIFFERENTIATED FILING: SUMMARY IMPACTS

The summary impacts set out in this section are applicable irrespective of the date or penalty approach. More detailed benefits and costs/risks for the different options are set out in the options analysis that follows.

The revised paper deadline is anticipated to be end October or end November. With either a late penalty or a paper filing fee payable by those who file by paper after these dates.

4. SA DIFFERENTIATED FILING: CUSTOMER IMPACT

This proposal will impact the whole of the SA population: represented and un-represented alike, both employed and self-employed.

The change would be unpopular and thorough consultation will be vital to understanding and mitigating the impact.

Customer benefits

- (i) We know from customer research that those who use our online services find them beneficial. While some customers may not previously have transferred, they may find benefits once they adopt. After enrolment, customers will have access to their Self Assessment details and status any time they choose. They will be able to contact the Department and submit changes at their convenience.
- (ii) Most un-represented taxpayers have the information needed to complete their tax returns by mid-July at the latest.
- (iii) These proposals do not, in fact, impose any real additional burden or risk of exclusion on customers, as we would continue to offer a choice between online and paper channels. The behavioural impact stems from altering the balance of that choice, not removing it.

Customer costs/risks

- (i) This would be a material change to the existing Self Assessment system, and is therefore likely to attract negative comment from both press and accounting representative bodies. We can also anticipate complaints about disadvantaging the non-e-literate taxpayers and some agents.
- (ii) Our research indicates that agents would not welcome a shorter paper-filing window. Indeed representative bodies have in the past expressed strong opposition to measures bringing forward the SA filing deadline, although they find it difficult to justify the need for the current 10 month window (which is long in comparison to other fiscal regimes that operate similar schemes).
- (iii) There may be some confusion in customers' minds as this proposal amends and or introduces a new date to the Self Assessment calendar (depending on preferred the option). This will add complication and will call for focused and directed marketing and communication to ensure a clear message for customers.
- (iv) A paper filing penalty or a paper processing fee may be seen as an increased tax burden on small businesses and will attract a degree of negative press comment. With the paper processing fee, we would be following a route established by Companies House who have moved to a differential filing fee starting in February 2005.
- (v) The short tax return is currently not available online or as a paper substitute. Tax agents have complained that this causes problems for them serving their clients. The online return is constructed in such a way as to display to customers only those items of the return that are relevant to the individual customer and therefore, in a sense, falls in between the main return and the short return. However, we believe that the development of an online short return will smooth the path with agents for the removal of substitutes. The development of an online short tax return is dependent on some redevelopment of the SA processing system (CESA). We hope to have this in place by the time the substitutes are withdrawn.
- (vi) Any delays to the planned revision of the SA Return and replacement of the CESA system may impact our ability to have the necessary changes in place for an April 2007 start.

5. SA DIFFERENTIATED FILING: DEPARTMENT IMPACT

Departmental benefits

- (i) We anticipate that differentiated filing will bring about a further conversion of 10–20% of those agents who would otherwise still paper file after the removal of paper substitutes in 2007–08, bring us to a total of 70% of Self Assessment returns from agents filed online. We expect a more modest

impact on un-represented taxpayers of around 5% over and above our target for voluntary take-up of 35%. When combined with the removal of paper substitutes, we expect that this proposal would give us online take-up of 57% in the first year. This would be a challenging target but we think it would be achievable, especially taking cognisance of increasing Internet penetration.¹

- (ii) Differentiated filing would send a clear message on the Government preferred approach and helps us achieve our current target of 35% in 2007–08, boosting individual take-up to 45% and supporting our achievement of the overall 57%.
- (iii) Besides its potential to drive online take-up, differentiated filing dates would reduce the amount of paper handling in local offices and bring forward the SA paper peak from the last quarter to the third quarter and hence help spread work. Bringing forward the deadline to Quarter 3 will also reduce the demands on IT capacity in Quarter 4.
- (iv) Differentiated filing dates between paper and electronic are now in place in 10 of the 30 OECD member countries (Australia, Austria, Canada, France, Greece, Iceland, Ireland, Italy, Netherlands and Norway). In particular, Ireland has successfully increased filing for their Self Assessment equivalent from limited take-up to over 40%, through the introduction of a three week differential.
- (v) Supports achievement of the December deadline for IR to code out liability under PAYE in following year. Has additional benefit of reducing in year coding changes that are expensive for both the department and employers.
- (vi) Cashflow to the Exchequer: we are not proposing any changes to the payment deadlines under Self Assessment, but a number of taxpayers do make their balancing payment at the same time as filing their return, whether on paper or electronically.

Departmental costs/risks

- (i) We would require primary legislation in Finance Bill 2006. We think that this would be approximately half a page in length.
- (ii) Legislation would need to be in place before the statutory notices (Self Assessment returns or Notices to File) with revised filing deadlines were issued in April 2007.
- (iii) This proposal may result in an increase in electronic submissions at the end of the filing period (ie near the January deadline) and may therefore result in increased infrastructure capacity dependencies. We are already building substantially increased capacity to support the first phase of mandatory electronic PAYE end of year filing, and will increase this for subsequent years. We plan to continue to invest in infrastructure to support our projected take-up.
- (iv) Non compliance. Differentiated filing may cause an increase in the number of late filing penalties that would create negative publicity.
 - Some people who habitually file paper returns after the new paper deadline won't absorb the message and are likely to file late by paper. We could mitigate against this through additional advertising and an operational "soft touch" in early years.
 - Some people who find that they have missed the new paper filing date are unable to file electronically will also file late.

The potential impact in early years will be mitigated by targeted marketing and pre-registration for online services for those who have not yet filed on paper. Some of the marketing budget would be allowed for this activity.

- (v) Will require some re-profiling of work and resource in processing offices
- (vi) System and administration changes would need to be made. These might include adjustment to the reminders cycle and content, identification of penalties, and their presentation on statements and accounts, and the collection of these penalties. These changes would need to be resourced and scheduled against other priority departmental and ministerial initiatives and ASPIRE capacity constraints. Costs are not dependent on the year or month we eventually decide to use. However, if October is chosen, rather than November, an additional reminder run at a cost of around 20p per reminder (distribution and postage costs) might be desirable rather than simply changing the existing December run. If additional reminders were to be sent to all who haven't paper filed we may be looking at an increased operational costs of around £2 million in earlier years.
- (vii) There would be additional marketing costs, particularly in earlier years to promote awareness and communicate the rules surrounding the new deadlines and penalty. While we would hope to maximise the use of existing spend, we estimate the need for an additional £1 million in each of the first three years. This would include a sum for pre-registering selected groups of SA taxpayers to reduce the Government Gateway and Self Assessment enrolment lead times.

¹ Gartner and Forrester research indicates that usage of online banking services continues to grow. Latest figures from the Office for National Statistics show that internet use continues to grow: all adult use has grown from 53% in 2001 to 66% in October 2004; 70% of those aged between 16–64 have accessed the internet.

- (viii) Potential negative impact on our PSA target for filing on time in the year to 31 March 2008 due to customers not complying with the paper deadline.
- (ix) Support arrangements for online customers would need to be put in place at a potential increased costs in earlier years of approximately £1 million.
- (x) There is potentially an impact on the Inland Revenue Receivables Management Service collection of payments as a result of the paper processing fee or penalty.

6. SA DIFFERENTIATED FILING: OPTIONS

A number of options exist in terms of how differentiated filing could be implemented. These are laid out in the following sections. There are three key dates in the *existing* Self Assessment timetables.

- **30 September:** cut off date for paper returns to ensure IR calculation and notification of liabilities and the guaranteed influencing of the coding for the following year. Online submissions are automatically calculated.
- **31 December:** deadline for online returns to ensure IR coding out of liability for PAYE in the following year.
- **31 January:** paper and electronic SA filing deadline and payment due date. Late filing penalty applies beyond this date.

In determining options there are three key parameters:

- (i) Paper filing deadline: We have considered moving this to end of September, October, November or December.
- (ii) Financial charge: We have considered two options:
 - Penalty: A fixed penalty already exists for returns received after statutory filing date. This penalty would apply if a paper return were submitted at any time after the new paper filing deadline.

Note that in any event, it would not be practical to issue penalty notices until after the online filing deadline (31 January), as, until that date, it would not be possible to identify all taxpayers who had missed the relevant deadline.

- Paper filing fee: a single fee would apply after a certain date. A late filing penalty fee would still apply for returns received after the 31 January (paper returns received after 31 January would get the penalty and the paper filing fee).

The proposed paper filing fee would apply if the return were submitted on paper after a certain date. Precedent already exists for applying a higher charge paper handling with paper submissions to Companies House attracting a filing charge of £30 for paper submissions against a £15 for online filing. Companies House will be introducing this new charging regime from February 2005. There are two choices for charging a paper processing fee. These are:

- Fee on a sliding scale from August onwards increasing at monthly intervals,
- Flat fee, which applies after a cut off date.

We believe that the operational and communication complexities and costs of a sliding scale would outweigh the benefits. A flat fee which would apply after a cut off date would be straightforward to communicate and simpler to administrate.

- (iii) Other date changes, in particular, the cut off date for IR calculation and notification of liabilities for paper returns.

In considering these parameters, four potential viable options have been identified:

Option 1a:	<ul style="list-style-type: none"> — Move paper SA filing deadline to 30 November from 31 January — Late filing penalty for paper returns filed after 30 November. — No change to any other dates. — <i>Note:</i> this is the option recommended to the PMG in previous submissions
Option 1b:	<ul style="list-style-type: none"> — As Option 1a but with a paper processing fee rather than late filing penalty.
Option 2a:	<ul style="list-style-type: none"> — Move paper SA filing deadline to 31 October from 31 January. — Late filing penalty for paper returns filed after 31 October. — Move cut off date for IR calculation and notification of liabilities for paper returns to 31 October from 30 September to coincide with the revised paper date.
Option 2b:	<ul style="list-style-type: none"> — As Option 2a but with a paper processing fee rather than late filing penalty.

The key benefits and costs/risks of these options are set out below. Note that the summary impacts set out in section 3 apply to all options.

Options 1a/1b: November

Benefits:

- (i) The November date means that gap between the paper filing deadline and the date from which penalty charges would be applied (31 January) is kept relatively small.
- (ii) Preserves the 30 September cut off date, which has significant recognition by taxpayers.
- (iii) Avoids tax credits renewal peaks whilst offering a material differential in dates.
- (iv) November is one of the Department's Contact Centres' quietest months; this maximises the Department's ability to support SA customers with questions about completing their return.
- (v) We understand that this date is likely to be suggested (as a possible revised deadline for *all* Self Assessment returns) in the NAO "Study on Filing of Income Tax Self Assessment returns" due to be published in Spring 2005.
- (vi) Option 1b provides a softer landing for taxpayers and may, therefore, be more palatable, may have a smaller impact on increasing electronic take-up.
- (vii) Pulls workload forward and reduces the peak levels normally seen in January. This supports the NAO view that the Department should be more proactive in evening out workload across the year.

Costs/Risks:

- (i) This option introduces an additional cut-off date into the SA timetable and would need careful communication to taxpayers to avoid confusion.
- (ii) Will require a re-profiling of work and resource in processing offices; may give rise to some tricky operational workload balances in November spilling into December which will need to be carefully managed.
- (iii) It will be necessary to send a warning message in December to those SA customers to whom a paper form had been sent and who had not yet filed by the new deadline for paper. This may be an adaptation of the existing reminder rather than an additional one. This would advise the customer that a paper return will attract a penalty (or fee), and that they have until the end of January to file electronically.
- (iv) Risk that the paper filing fee may be ineffective with represented Self Assessment taxpayers whose returns are filed by agents. We would hope the removal of substitutes will counter this risk.

Option 2a/2b: October

Benefits:

- (i) Whilst it amends an existing date it doesn't introduce an additional date into the SA timetable and therefore should be more straightforward to communicate and understand.
- (ii) Still a substantial differential between paper and electronic deadline, so likely to impact more people.
- (iii) The deferral of the September deadline would allow taxpayers more time to prepare their return—a useful concession in terms of getting through those who object to pulling paper away from 31 January.
- (iv) We would then have a single paper filing date—as opposed to the two we have now (September and January)
- (v) It moves the current September SA filing peak away from the Tax Credit renewals peak. A single filing date in October will take away from the tax credit renewals peak that will involve some agents.
- (vi) Would allow us to issue a reminder immediately after October telling people that they must now file by e—giving them considerable notice to put the appropriate arrangements in place to allow them to do this.
- (vi) This is one of the quietest periods for the Department's Contact Centres; maximises the Department's ability to support SA customers with questions about completing their return.
- (viii) Option 2b provides a softer landing for taxpayers and may, therefore, be more palatable, albeit may have a smaller impact on increasing electronic take-up.

Costs/Risks:

- (i) Amends the 30 September cut off date, which may cause confusion.
- (ii) Date brought further forward than November option so likely to result in greater pushback, especially from agents. Previous consultation with agents elicited strong opposition to November, so this resistance is likely to be stronger for the October proposal.
- (ii) Clashes with the tail end of tax credits renewal.
- (iv) The filing deadline is even further from the date at which we would issue the penalty notice and we would have to send a reminder notice to file electronically to avoid the penalty/fee.
- (v) May put at risk the guarantee to calculate the taxpayer liability and notify them in time to make their January payment.
- (vi) May put at risk the ability to process returns in time to influence the following year PAYE coding notices to individuals and employers.
- (vii) Risk that the paper filing fee may be ineffective with represented Self Assessment taxpayers whose returns are filed by agents. We would hope the removal of substitutes will counter this risk.

7. SA DIFFERENTIATED FILING: DEPENDENCIES AND TIMING

Timing considerations are as follows:

- (i) We would require primary legislation to be in place before the statutory notices with revised filing deadlines were issued. So, for example, to take effect for returns for the 2006–07 tax year would need to be in within the Finance Bill 2006 ahead of notices going out in April 2007. The changes needed to the primary legislation would be fairly minor and we estimate take no than half a page.
- (ii) *IT Considerations:* System changes need to be scoped and implemented.
- (iii) *Processes:* changes to communications and procedures are designed to make the transition as clear and smooth as possible for both taxpayers and staff.
- (iv) More effective marketing and communication campaign required.

8. SA DIFFERENTIATED FILING: OPTIONS CONSIDERED AND REJECTED

September

Move the paper filing deadline to 30 September. This would coincide with the cut off date for IR calculation and notification of liabilities for paper returns.

Whilst this would provide a single combined date that already has currency for SA taxpayers, it would create an un-manageable paper filing peak in September as well as clashing with the tax credits renewal peak.

December

Move the paper filing deadline to 30 December. This would coincide with deadline for IR to code out liability for PAYE in the following year.

Whilst this would be attractive in so far as it is less of a differential and keeps the filing deadline close the payment due date, it is rejected given likely objections resulting from the closeness to Christmas holiday period. Staff leave around this time would impact the Department's ability to process the paper returns promptly.

Agents will be put under similar pressures during the Christmas period and are likely to strongly object to such proposals.

We wouldn't be able to process these returns in time to influence PAYE coding. We will continue to have to send PAYE in year coding changes to individuals, their agents and employers; expensive for us and the employer; September or October dates would reduce the impact and costs of these.

Question 75 (Mr Greg Clark): Cost of processing an average Tax Credits application form

Mr Clark referred to figures in paragraph 4.2 of the Comptroller and Auditor General's Report on the Filing of Income Tax Self Assessment returns, citing the cost of processing an ITSA return as £22 per return, compared with an average staff cost of £60 of processing an Income Support application.

The differences between the Tax Credit system and benefits such as Income Support Incapacity Benefit and Jobseekers Allowance, mean that we are unable to provide an exact comparison. However, we have calculated what we believe to be a similar figure using staff costs and application volume where

- Staff costs, have been interpreted to mean salaries and salary related costs.
- Application volume, has been interpreted to mean the number of new claims and the number of renewals.

<i>Tax Credits</i>	<i>2004–05</i>
Staff cost (£m)	205
Application volume (m)	5.88
Staff cost/application (£)	35

We have provided figures for 2004–05, as these are the most recent ones available and they reflect the first year of Tax Credits which had both new claims and renewals

Question 93 (Mr Alan Williams): Compensation paid following HMRC errors

Mr Williams referred to paragraph 3.19 of the C&AG’s Report on the filing of Self Assessment tax returns which comments that “although HM Revenue and Customs has information on complaints referring to penalties and compensation it has paid, it has no specific information on the number of taxpayers who claimed compensation for being wrongly subject to a penalty; the number of claims for compensation agreed, and the amount paid out as a result of its errors.”

The Department holds statistics for the total number of complaints about penalty notices (1,037 in 2004–05) and the total compensation paid for all types of complaint, but, our IT system does not currently provide statistics that give a break down of the compensation paid for different types of complaint. We are looking at ways to enhance the system so that compensation figures for different types of complaint are obtainable.

In the year to 31 March 2005 the offices that are responsible for codings paid out a total of £608,552 in compensation in respect of 21,919 complaints, but this covered the whole range of processing and compliance work.

The payments were made under Code of Practice 1 and covered costs, worry and distress and poor complaints handling, as appropriate to each case. Most payments have to be approved at Director level and all are fully recorded and subject to audit. Thus, it would be possible, though time-consuming, to draw up a list showing every case, the amount paid, and the reason for the complaint (though there will often be more than one reason). The difficulty continues to be devising a manageable system that records the data centrally and that can be easily accessed. We are working on this.

Complaints teams that pay out compensation are also subject to Quality Assessment and Quality Control by the relevant management team to ensure that the guidelines on paying financial redress are being adhered to.

Question 117 (Mr Richard Bacon): Processing of the 2004–05 employer’s annual PAYE returns

Large employers, those with 250 or more employees, were mandated to file their 2004–05 Employer’s Annual Return online. Small employers, those with fewer than 50 employees, who voluntarily filed online for 2004–05 are entitled to a tax-free incentive payment of £250.

IR (now HMRC) was “open for business” on 6 April 2005 and agents and employers of all sizes were able to file online. 935,000 online Employer Returns have been received. There were some initial minor problems on the start days but subsequently filing went ahead unhindered, even on the peak submission days. To avoid overloading our online systems, we advised users to file outside peak times, to give them a smoother filing experience.

There were delays in the delivery of the IT supporting processes, particularly our new computer system “ERIC” which lead to an inability to validate Returns on receipt. All online Returns were stored. Processing of Returns submitted by Electronic Data Interchange started on 5 June. We began processing, out of the temporary store, Returns sent via the Internet on 10 August and that work was completed at the end of September.

The processing of Returns involved validation routines to ensure that the Return was of an adequate quality as specified in the published Quality Standard. All “good” online employer Returns (with no errors in them) have all been processed to HMRC’s back end systems.

The £250 tax-free incentive payment, given to small employers who successfully filed online, is made when the Return details are posted to HMRC's accounting systems. The delay in processing Returns has led to considerable delay in making the payment. Payments in respect of all "good" Returns started on 18 July and the issue of letters to submitters confirming the payment was completed on 10 November 2005. As remaining "poor" quality Returns are corrected and processed the payment will be credited to the relevant payment record.

Letter from the Director of the OECD to the Chairman of HM Revenue and Customs on the review of HMRC's online services

It has been brought to our attention that there is a review underway of HMR's online services. As this is an area that has been the subject of recent study by the OECD Committee on Fiscal Affairs Forum on Tax Administration (FTA), we thought it useful to bring the findings of this (and some related) work to your attention, and to provide some additional observations based on Richard Highfield's experience in this area with the Australian Taxation Office. This is all set out in the attached brief note prepared by Richard who can be contacted if you or your officials require additional information or clarification.

TRENDS IN TAXPAYER SERVICES USING NEW TECHNOLOGIES

In early 2005, the OECD released a report prepared by the FTA entitled "*Survey of Trends in Taxpayer Services Using New Technologies*". The report—electronic version attached—describes in some detail the findings of an OECD-wide survey to gauge the level of progress of national revenue authorities in member countries in their use of modern online services to assist taxpayers meet their tax obligations. It provides benchmark data on the take up rates being achieved for electronic filing of tax returns for the major taxes and describes the strategies being employed to improve success in this area.

The report also covers progress with other aspects of a modern online service for tax purposes (eg, electronic payments and refunds, email, use of the internet for information provision), and makes reference to some major process redesign initiatives in a number of countries as part of their enhanced taxpayer service arrangements (eg systems of pre-populated tax returns used by Nordic countries, Australia's "business activity statements"—an integrated means for business to report all of their periodic tax obligations as a single information stream).

TAX ADMINISTRATION IN OECD COUNTRIES: COMPARATIVE INFORMATION SERIES

The OECD also released a report in late 2004 entitled "*Tax Administration in OECD Countries: Comparative Information Series*" (2004). This report, the first in what is intended to be a regular series, describes selected features of the tax administration arrangements in OECD member countries. The series was established to fill a void in the availability of such information, and thereby facilitate and encourage dialogue on important tax administration matters. An electronic version is attached.

Among other things, the report describes tax return filing and payment obligations for the major taxes—refer pages 14 *et seq* and Tables 7 and 8—and from the country data it will be seen that the UK has the most generous return filing dates (for self-calculating personal taxpayers and the corporation tax) of any OECD country. Among other things, this severely limits in my view the scope to use extended return filing arrangements to encourage electronic filing, as other countries have done, and unnecessarily lags the collection of tax revenues. More is said on this later.

THE AUSTRALIAN EXPERIENCE

Electronic filing of tax returns commenced in Australia in 1990, following a successful pilot test in two states. I was in charge of the operational division in the Australian Taxation Office (ATO) responsible for the systems administration. The initial focus of the system was personal tax returns which in Australia must be filed annually by all taxpayers. Given the level of tax system complexity, the majority of these returns were, and still are, prepared by tax professionals. (The costs of tax return preparation are tax deductible.) In its first two to three years of operation, the system achieved considerable success which I attribute to three factors:

- (i) the forging of strong working relationships with software producers and the tax profession;
- (ii) streamlining tax return information requirements to make the system as user-friendly as possible; and
- (iii) establishing an attractive regime of incentives to encourage wide use of the system.

Concerning (i), it is axiomatic that as significant players in the building and operation of electronic filing arrangements, software producers and tax professionals need to be given a central role in their planning and development. In the Australian context, considerable emphasis was placed on achieving this outcome in a variety of ways (eg systems design, early advice of changes, testing and certification procedures).

At the time of its implementation, Australia had recently moved from a regime of assessment of tax returns, involving scrutiny of all returns and accompanying information by technical staff, to one based on self-assessment principles. As such, there remained within the design of tax returns some fairly detailed information requirements which imposed onerous reporting obligations on some taxpayers. With the development of electronic filing, steps were taken to rationalize tax return information requirements so as to simplify use of the system by tax return preparers. This was particularly relevant when contemplating the extension of electronic filing to business returns (including corporation tax) in the ensuing years. Today, Australia's corporation return is akin to a data input schedule of summary information, which has led to a very high take-up rate being achieved (ie over 90%).

From the outset of the system, it was recognised that taxpayers and tax professionals would need to be given strong incentives to use the new arrangements. In the case of personal tax returns, two major incentives were established:

- (i) accelerated refunds of overpaid taxes; and
- (ii) extended periods of time for tax professionals to file returns that are to be submitted electronically.

So far as (i) is concerned, refunds of overpaid tax, which are very common for employee taxpayers, typically took some six to 10 weeks to process when filed on paper returns in peak periods. To encourage electronic filing, a corporate objective of 10 working days (for 80% of electronically-filed returns) in the form of a public commitment was established and widely promoted. Over-achievement of the objective in the first two years of operation encouraged greater take-up in the ensuing years. For tax professionals, an extended filing period of one month was provided over and above the then existing arrangements that require tax professionals to file returns on a staggered basis for a period of up nine months. Typically, all returns are required to be filed within four months after the end of the fiscal year. Special arrangements exist for tax professionals. Today, over 80 percent of all personal tax returns are filed electronically.

SUGGESTIONS IN THE UK CONTEXT

The report referred to at the outset provides a range of ideas to encourage use of online services. As you would be aware, a number of countries have established mandatory reporting and filing obligations, if not for the bulk of their taxpayers then certainly for the largest ones. Given a possible reluctance to contemplate mandatory requirements for the bulk of UK taxpayers, one is left to contemplate incentives that might be crafted to encourage taxpayers into the electronic filing net.

As mentioned earlier, return filing dates for UK self-calculating taxpayers are excessively generous by OECD country standards. It has occurred to me that a revision of these dates might be undertaken so as to require paper returns much earlier (eg, within four months of the close of the fiscal year as in many other countries), but with provision made to give longer periods, perhaps on a staggered basis, for electronic filers. This, in conjunction with any streamlining of return information requirements that may be feasible, could be attractive to return preparers.

So far as business taxpayers are concerned, I recommend that you examine the idea of integrating the regular tax payment and reporting obligations that businesses are confronted with as a medium/longer term proposition. With the increasing trend of revenue bodies to organize and design their processes around taxpayers', as opposed to a "tax by tax type" approach, I believe that integration of businesses' regular reporting and payment obligations is the future direction for tax administration. Such an approach is already being pursued to varying degrees by a number of Nordic region countries and as mentioned earlier, a more complete model, known as 'business activity statements' has recently (2000) been introduced in Australia.

Jeffrey Owens
Director, OECD

2 September 2005