

executive summary

- 1 Section 2 of the Exchequer and Audit Departments Act 1921 requires me to examine the accounts of the Inland Revenue to establish that adequate regulations and procedure have been framed to secure an effective check on the assessment, collection, and proper allocation of revenue and to examine the correctness of sums brought to account. This report sets out the results of audit examinations carried out by the National Audit Office in fulfilment of these requirements.
- 2 The Inland Revenue is managing a major change programme. Following the implementation of self assessment for income tax and corporation tax, 1999-00 saw the transfer of the Contributions Agency to the Department, along with policy responsibility for the national insurance scheme. In August 1999 the Department introduced new arrangements for collecting tax in the construction industry affecting over 1 million taxpayers and, in October 1999, implemented an important new programme of tax credits for working families and disabled people. This change programme is set to continue.
- 3 During 1999-00, we carried out examinations on both new and existing systems. New systems examined included the construction industry scheme, tax credits and income tax and corporation tax self assessment. Reviews of existing systems included inheritance tax, PAYE, petroleum revenue tax, stamp duty, and tax deducted at source by banks and building societies. Checks on the information technology operations included reviews of the Inland Revenue's main computer installations and the Department's management of the risks associated with its information technology infrastructure.
- 4 Overall, our work provided assurance that the Inland Revenue's regulations and procedure continued to provide an effective check over the assessment, collection and allocation of tax. My report on the Inland Revenue's trust statement for 1999-00 (CM 5029) records that I was also satisfied with the correctness of sums brought to account.
- 5 My report focuses both on new systems and on the impact of change on existing systems. The key points arising from these examinations were:
 - The Inland Revenue cleared the PAYE tax records of one million people without knowing whether they had paid the correct amount of tax in 1997-98 because of difficulties in processing employers' end of year returns. The Department estimates that, had it been able to process the records in the normal way, its checks would have identified some £4 million underpaid tax and £22 million overpaid tax. The Department believes that the processing difficulties have now been resolved, but will not know for sure until it has completed work on processing 1998-99 end of year returns. It is conducting a fundamental review of its systems, and this needs to be completed quickly to provide assurance on the completeness and reliability of the entire process, particularly as the systems will have to cope with additional information on tax credits and collection of student loan repayments from 2000-01. The Department should also examine the scope to alert those taxpayers affected to the risk that they may have under or over paid tax.

- In the first six months of the new tax credits scheme, the Inland Revenue paid out more than £1 billion to around one million applicants. Implementation went smoothly, and the Department is continuing to strengthen the controls necessary for the effective operation of the scheme. In particular, it should continue both to refine its approach to managing the risk of erroneous or fraudulent applications and improve the assurance it obtains about the reliability and accuracy of the substantial amounts paid out of tax revenue.
- Introduction of the new construction industry scheme in August 1999 has led to the identification of around 100,000 people not previously registered with the Department, and produced an estimated £280 million extra tax receipts in 1999-00. But there were some teething troubles, particularly with the issue of registration cards and tax certificates to over one million contractors and subcontractors in the industry and in managing the issue and receipt of returns from taxpayers. As a result, the Department has temporarily scaled back planned work to reconcile tax paid with contractors' returns. These difficulties have increased the risk of fraud and error remaining undetected in the early stages of the scheme, when procedures are settling down and systems are at their most vulnerable. The Department is working to resolve these difficulties.
- Following a Committee of Public Accounts report in 1998, the Inland Revenue has made a number of improvements to the way it checks employers' compliance with PAYE regulations. The recent transfer of the Contributions Agency will streamline the way that checks on tax and national insurance contributions are carried out. But this, and other organisational changes, have affected the level and quality of work, and there is further scope to target resources on higher-risk employers. Having completed a major reorganisation in April 2000, the Department is now in a position to address these issues.