



National Audit Office

DEPARTMENTAL OVERVIEW

A summary of the NAO's work on HM Revenue & Customs 2011-12

OCTOBER 2012

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The National Audit Office scrutinises public spending for Parliament and is independent of government.

The Comptroller and Auditor General (C&AG), Amyas Morse, is an Officer of the House of Commons and leads the NAO, which employs some 860 staff.

The C&AG certifies the accounts of all government departments and many other public sector bodies.

He has statutory authority to examine and report to Parliament on whether departments and the bodies they fund have used their resources efficiently, effectively, and with economy.

Our studies evaluate the value for money of public spending, nationally and locally. Our recommendations and reports on good practice help government improve public services, and our work led to audited savings of more than £1 billion in 2011.



National Audit Office

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Introduction

Aim and scope of this briefing

The primary purpose of this report is to provide the Treasury Select Committee with a summary of HM Revenue & Customs' performance since September 2011 based primarily on the Department's Accounts and National Audit Office work. The content of the report has been shared with the Department to ensure that the evidence presented is factually accurate.

Part One

About the Department

The Department's responsibilities

1 HM Revenue & Customs (HMRC) is the principal UK revenue-collecting department. Its purpose is to make sure that money is available to fund the UK's public services, by collecting UK taxes. In 2011-12, HMRC collected £474.2 billion in revenue, £4.5 billion (1 per cent) more than in 2010-11 (£469.7 billion). Income tax, National Insurance contributions and VAT accounted for 74 per cent (**Figure 1**).

2 HMRC also helps families, individuals and companies with targeted financial support. In 2011-12 it incurred expenditure on:

- tax credits of £30.5 billion; and
- child benefit of £12.2 billion.

3 In addition, HMRC enforces the national minimum wage; collects student loans; collects and manages the bank levy; and supervises compliance with money laundering regulations for organisations in finance sectors that do not have a supervisory body. It is also responsible for policies and activities associated with collecting duties at the frontier and processing information about international trade.

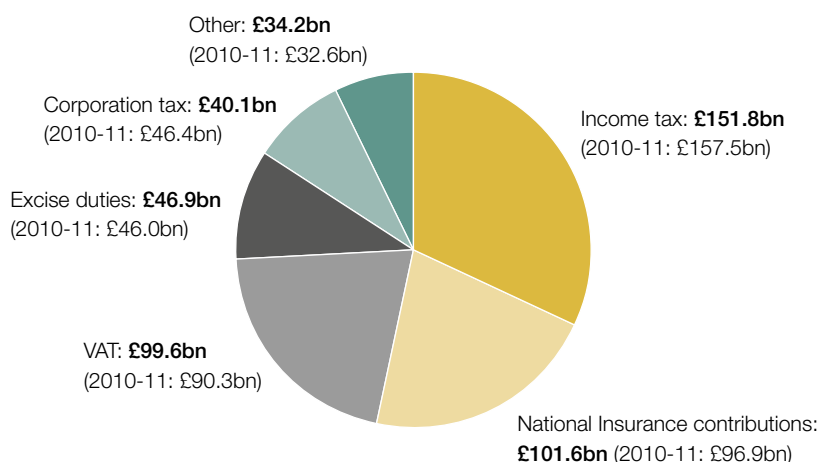
How the Department is organised

4 The chief executive is responsible for HMRC's day-to-day business, is the Permanent Secretary and accounting officer, is accountable to Parliament for the Department's expenditure and performance and chairs the executive committee of senior officials. The lead non-executive board member chairs the board, which comprises members of the executive committee and the non-executive board members. The board provides strategic leadership and is responsible for the effective governance of HMRC.

5 Significant changes in the structure of the board and executive committee, and in the individual membership have taken place in 2012. In August 2012, a Tax Assurance Commissioner was appointed to act as second permanent secretary in support of the chief executive. The Tax Assurance Commissioner is a new role, responsible for shaping tax policy and strategy, tax professionalism, and overseeing and providing assurance of tax settlements.¹ It replaces the position of the Permanent Secretary for Tax who, before the creation of the Tax Assurance Commissioner's role, had been the senior tax professional in HMRC. In addition, a new lead non-executive board member replaced the chairman of the board.

Figure 1

Main types of revenue collected by HM Revenue & Customs in 2011-12



Source: HM Revenue & Customs Annual Report and Accounts 2011-12

¹ The Tax Assurance Commissioner will have an explicit challenge role in the decision-making on large tax disputes and will have no part in the HMRC's engagement with specific taxpayers. This change is in response to NAO reports on the oversight and governance of significant tax disputes. More details on the findings are in paragraphs 60 and 61.

6 HMRC is organised into three groups (personal tax; business tax; and benefits and credits) which are responsible for tax or benefit regimes and undertake operational activities. A fourth group (enforcement and compliance) delivers a range of specified cross-HMRC operations. The groups are supported by five departmental-wide corporate services functions (**Figure 2**). The leaders of these groups and functions, together with the chief executive, form the executive committee. Four of the director generals who head HMRC's groups and sit on the executive committee will also be replaced in 2012-13, two by external appointments and two on promotion.

7 HMRC has one executive agency, the Valuation Office Agency, which provides property valuations and advice, to support the administration of taxation and benefits (Appendix One). It also provides valuation services to support the wider public sector.

8 HMRC has one arm's-length body, the Environmental Trust Scheme Regulatory Body Limited (ENTRUST). ENTRUST is a not-for-profit private sector company which acts as regulator of the Landfill Communities Fund.²

Where the Department spends its money

9 In 2011-12, HMRC had gross expenditure of £46.9 billion. This includes personal and corporation tax credits expenditure, child benefits and other payments totalling £42.9 billion, as well as gross running costs of £4.0 billion. A breakdown of expenditure by main business segments is presented in **Figure 3** on page 8. The Department employed a total of 67,004 full-time equivalent staff at a cost of £2.2 billion during 2011-12;³ this cost is included within the running cost expenditure.

Recent developments and current challenges

10 The Department is in the second year of a four-year change programme which is designed to deliver the changes and efficiencies required by the Comprehensive Spending Review 2010 settlement. The challenging settlement commits HMRC to:

- delivering efficiency savings of 25 per cent by 2014-15, resulting in reduced spending of £1.6 billion in cash cumulative terms over the four year period;
- reinvesting £917 million of savings in tackling tax evasion and avoidance to bring in additional revenue of £7 billion a year by 2014-15 on top of its existing activities; and
- stabilising and improving the customer experience.

11 The change programme also includes plans to reduce fraud and error in tax credits, the stabilisation of the National Insurance and PAYE System (NPS) and introduction of the Real Time Information (RTI) project.

12 To support the cost reductions over the four-year period, HMRC planned to reduce staff numbers by 10,000; redeploy, retrain or recruit 9,000 staff into high value enforcement and compliance work; significantly reduce the number of offices; and reorganise corporate services.⁴

13 The Department has reported that it raised £16.7 billion of additional revenue from its compliance activities in 2011-12, £1.7 billion above its target for the year and 20 per cent up from the previous year. HMRC excluded £4.3 billion of exceptional items from the reported additional revenue to avoid distorting its performance against its targets.⁵ HMRC anticipates further tax revenues following an agreement between the UK and Swiss governments to tackle offshore tax evasion which was signed on 6 October 2011. The agreement aims to settle the unpaid tax liabilities of UK individuals who hold Swiss assets through a one-off payment covering past liabilities and it will also establish a new withholding tax to collect amounts due in the future. The agreement is expected to come into force in 2013. Once this agreement has come into force, the Swiss authorities, on behalf of the Swiss paying agents, will make an up front payment of 500 million Swiss francs in anticipation of monies due once the agreement starts to operate fully.

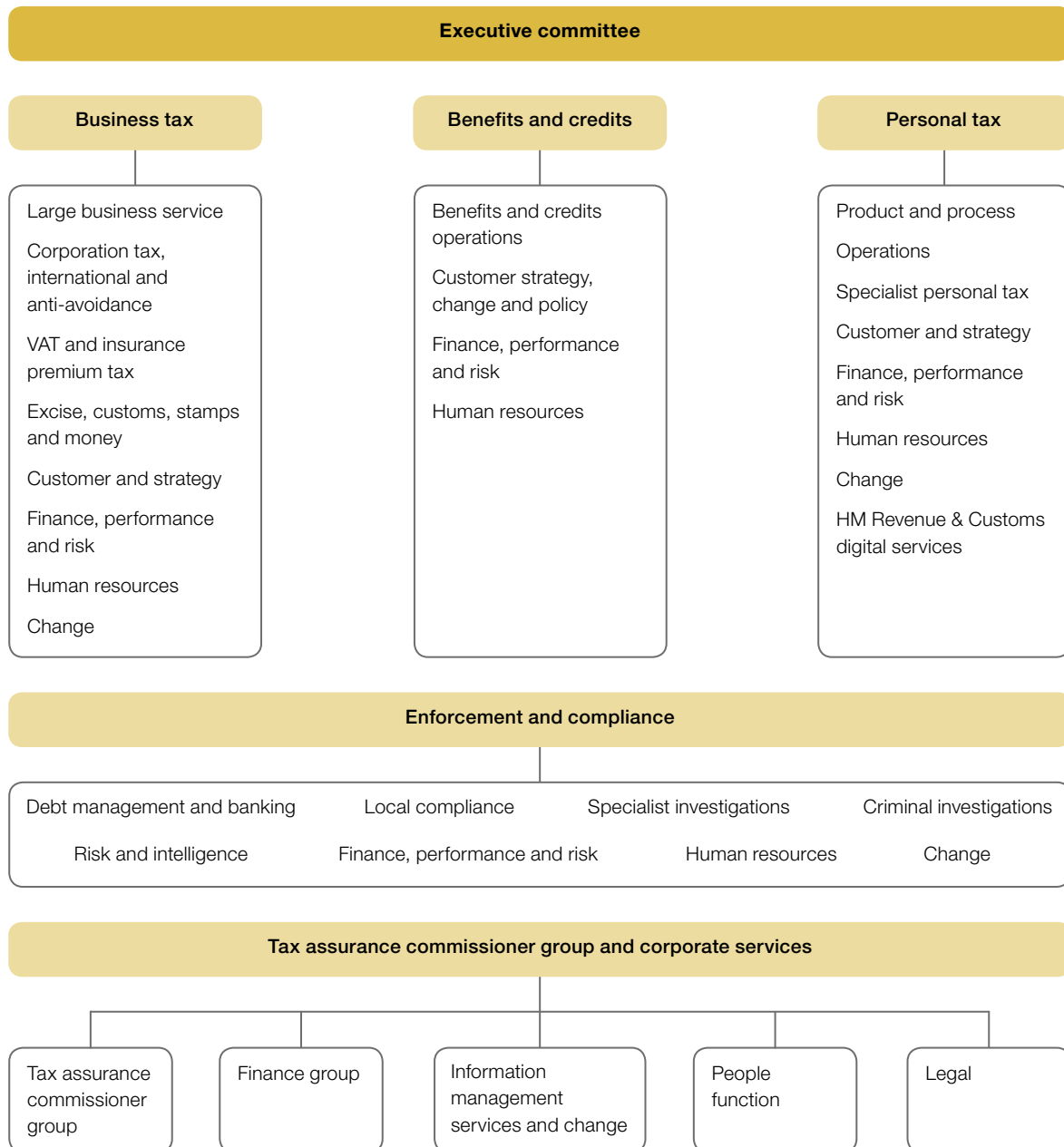
² HM Revenue & Customs, *Annual Report and Accounts 2011-12*, HC 38, June 2012, page 49. ENTRUST's accounts are not audited by the National Audit Office.

³ This is the average number of full-time equivalent staff in HMRC during 2011-12, excluding 3,600 Valuation Office Agency staff.

⁴ Comptroller and Auditor General, *Reducing costs in HM Revenue & Customs*, Session 2010-2012, HC 1278, National Audit Office, July 2011, paragraph 9.

⁵ HM Revenue & Customs, *Annual Report and Accounts 2011-12*, HC 38, June 2012. Chapter 4: How we performed, pages 9 and 11.

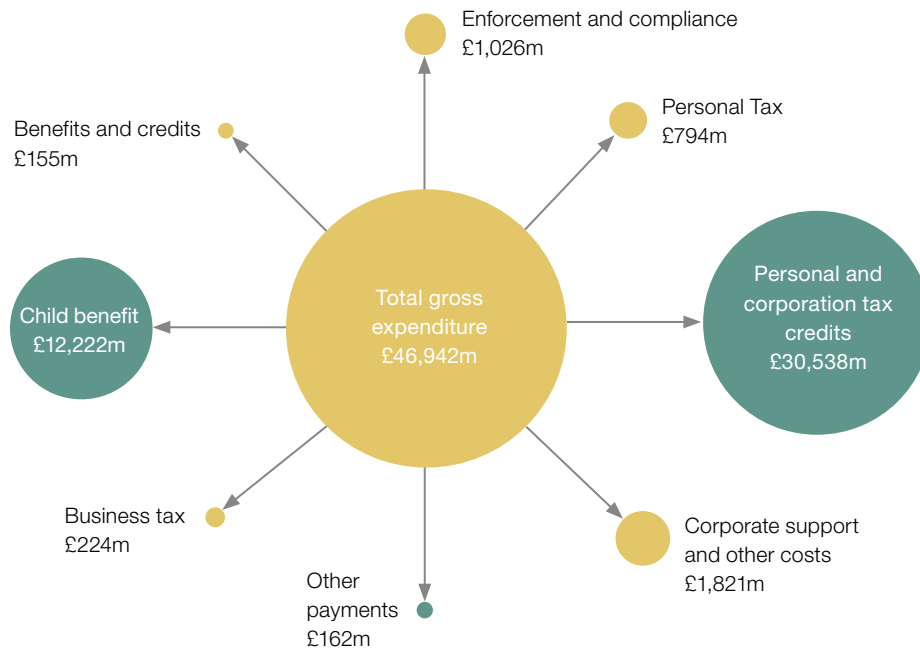
Figure 2
Summary of HM Revenue & Customs' organisational structure



Source: HM Revenue & Customs

Figure 3

Summary of HM Revenue & Customs gross expenditure in 2011-12

**NOTES**

- 1 The yellow items relate to running costs.
- 2 The green items relate to expenditure on benefits and credits and other payments.

Source: National Audit Office analysis of HM Revenue & Customs Resource Accounts 2011-12 (Notes 6 and 9)

14 We have previously reported the difficulties that the Department faced in operating PAYE after introducing its NPS system in 2009. The Department is part way through its plan to stabilise the PAYE service by March 2013. It had many key activities to complete in 2011-12 to meet its target to be operating a normal PAYE service by March 2013. The Department has met its target to process 6.7 million end-of-year reconciliations relating to the 2008-09 and 2009-10 tax years by March 2012. (The Department carries out end-of-year reconciliations on each taxpayer's record to determine whether the correct amount of tax has been paid). It is on track to reconcile the 2010-11 and 2011-12 tax years by March 2013 and also to clear the backlog of reconciliations relating to tax years 2003-04 to 2007-08 by December 2012. The Department estimates that it will cost £53.7 million to clear the backlog of open cases to March 2013, and £21.2 million to stabilise PAYE.⁶

15 The Department has still to make long-term process improvements to allow it to deal with the volume of work items created from in-year changes to taxpayer records or work automatically created by the NPS system from in-year processing (collectively called work items). Currently the NPS system creates more work items than the Department has capacity to clear. The Department is in the process of approving a project to automate and reduce the number of work items generated.

⁶ Comptroller and Auditor General, 'Report by the Comptroller and Auditor General' in HM Revenue & Customs, *Annual Report and Accounts 2011-12*, HC 38, June 2012.

16 The Department is working to introduce RTI as part of the PAYE service. RTI will require employers and pension schemes to report employees' income tax and National Insurance deductions when they are paid rather than at the year end. The timetable for full implementation is challenging and is driven by the Department for Work and Pensions' timetable for rolling out Universal Credit from October 2013.⁷ HMRC started a pilot to test the RTI system in April 2012. At 31 May 2012, 209 PAYE schemes, covering 1.5 million individual employee records, were using RTI. All employers and pension providers will be required to use RTI by October 2013. The Department has yet to decide how far it will use RTI within its in-year PAYE processing and plans to use the information gained during the pilot to inform its view.⁸

Capability and leadership

17 In 2006, the Cabinet Office launched Capability Reviews to assess departments' leadership, strategy and delivery – to improve departmental readiness for future challenges and to enable departments to act on long-term key development areas. Departments are required to conduct and publish self-assessments and resultant action plans against standard criteria set out in the Cabinet Office model of capability, which was updated in July 2009.⁹ Departments must rate their capability against ten criteria under three themes:

- **Leadership criteria** – 'set direction'; 'ignite passion, pace and drive'; and 'develop people';
- **Strategy criteria** – 'set strategy and focus on outcomes'; 'base choices on evidence and customer insight'; and 'collaborate and build common purpose'; and
- **Delivery criteria** – 'innovate and improve delivery'; 'plan, resource and prioritise'; 'develop clear roles, responsibilities and delivery models'; and 'manage performance and value for money'.

18 The Department completed its action plan in response to the Capability Review in March 2012.¹⁰ The action plan includes a self-assessment of the Department's ability to meet current and future challenges across ten criteria under three themes (**Figure 4** overleaf). Six of the criteria were assessed by the Department as amber/green and four as amber/red.

19 The Civil Service People Survey aims to provide consistent and robust metrics to help government understand the key drivers of engagement, so that it can build upon strengths and tackle weaknesses across the civil service. The survey of civil servants across all participating organisations includes a range of questions across nine themes which seek to measure their experiences at work. We present here the results of the third annual people survey for HMRC¹¹ – undertaken between mid-September 2011 and mid-October 2011 – covering the themes of leadership and managing change, and understanding of organisational objectives and purpose (**Figure 5** on page 11). The results of 17 major departments are in Appendix Two.

20 As part of the annual survey, each Department is given an engagement index, assessing the level of staff engagement determined by: the extent to which staff speak positively of the organisation, are emotionally attached and committed to it, and are motivated to do the best for the organisation. In 2011, HMRC, excluding its agency, achieved an overall engagement index of 40 per cent, the joint second lowest in the civil service and 16 percentage points below the civil service average. The overall employee index has increased from 34 per cent in the previous year, with improvements having been made across the nine themes. In absolute terms, the results are still poor and remain well below the civil service benchmark. The survey's conclusions were that although employees have a good understanding of the Department's objectives and purpose, they lack confidence in senior management and do not feel that the Department managed change well. While scores have improved, HMRC acknowledges there remains much to do. HMRC considers that a key priority is to increase its leadership and management capabilities and improve confidence in senior leadership and its management of change.

⁷ Universal Credit will be designed to bring together different forms of income-related support and provide a simple, integrated, benefit for people in or out of work. Available at: www.dwp.gov.uk/docs/universal-credit-chapter2.pdf, page 13.

⁸ Comptroller and Auditor General, 'Report by the Comptroller and Auditor General' in HM Revenue & Customs, *Annual Report and Accounts 2011-12*, HC 38, June 2012.











⁹ www.civilservice.gov.uk/about/improving/capability/background

¹⁰ HM Revenue & Customs, *Capability action plan*, www.hmrc.gov.uk/capability/capability.pdf

¹¹ www.hmrc.gov.uk/research/ps-autumn2011.pdf

Figure 4

HM Revenue & Customs Capability Action Plan Assessment

Theme	HM Revenue & Customs self-assessment	Criteria	Rating
Leadership	The Department has a clear and coherent vision for the future of HM Revenue & Customs but still has more to do to develop its people and embed the necessary leadership skills, behaviours and values, which promote pride in the organisation and vision.	Set direction	
		Ignite passion, pace and drive	
		Develop people	
Strategy	The Department's strategy allows it to make choices about how to design services and interventions that best influence customer behaviour, to maximise revenues and improve the customer experience at the lowest sustainable cost. The Department has a lot more to do to embed the strategy in the hearts and minds of its people and to use the understanding of customers to inform day-to-day decisions and choices.	Set strategy and focus on outcomes	
		Base choices on evidence and customer insight	
		Collaborate and build common purpose	
Delivery	The Department is making progress and improving its delivery but still has more to do to improve delivery for customers and staff.	Innovate and improve delivery	
		Plan, resource and prioritise	
		Develop clear roles, responsibilities and delivery models	
		Manage performance and value for money	

Source: Her Majesty's Revenue & Customs: Capability action plan

Figure 5
2011 Civil Service People Survey – HM Revenue & Customs

Theme	Theme score (% positive) ¹	Difference from 2010 survey	Difference from civil service 2011 ²
Leadership and managing change			
I feel that the Department as a whole is managed well	18	+6	-22
Senior managers in the Department are sufficiently visible	31	+7	-14
I believe the actions of senior managers are consistent with the Department's values	25	+6	-14
I believe that Excom (the departmental board) has a clear vision for the future of the Department	22	+7	-17
Overall, I have confidence in the decisions made by the Department's senior managers	17	+6	-19
I feel that change is managed well in the Department	15	+5	-12
When changes are made in the Department they are usually for the better	13	+5	-10
The Department keeps me informed about matters that affect me	39	+8	-16
I have the opportunity to contribute my views before decisions are made that affect me	18	+2	-18
I think it is safe to challenge the way things are done in the Department	27	+5	-12
Organisational objectives and purpose			
I have a clear understanding of the Department's purpose	73	+8	-11
I have a clear understanding of the Department's objectives	70	+9	-8
I understand how my work contributes to the Department's objectives	73	+8	-9

NOTES

- 1 Percentage positive measures the proportion of respondents who selected either 'agree' or 'strongly agree' for a question.
- 2 The 2011 benchmark is the median per cent positive across all organisations that participated in the 2011 Civil Service People Survey.

Source: HM Revenue & Customs People Survey Results Autumn 2011

Part Two

Financial management

21 The ability of departments to control costs and drive out waste requires professional financial management and reporting. In particular, departments need to be better at linking costs to services and benchmarking performance to determine whether costs are justified and value for money can be improved. Organisations also need to move their risk management arrangements from a process-led approach to one which supports the efficient and effective delivery of services. Improvements in these areas of management will help public bodies to deliver cost-effective services as they make difficult financial decisions over the coming years.

22 Departments are required to publish Governance Statements with their Annual Report and Accounts, which describe their arrangements for corporate governance, risk management, and oversight of locally delivered responsibilities. Governance Statements replace Statements on Internal Control which were published in previous years. They are designed to include additional discussion of how governance in the Department works, in line with the Corporate Governance Code.

Financial out-turn for 2011-12 and comparison with budget

23 We audit HMRC's two main annual accounts. The Trust Statement records revenue collected and the Resource Account reports the costs incurred by HMRC in collecting those revenues and paying tax credits and child benefit.¹² We also audit the accounts of the Valuation Office Agency, an executive agency of HMRC; the National Insurance Fund; and the Northern Ireland National Insurance Fund. HMRC collected £101 billion of National Insurance contributions in 2011-12 for payment to the National Insurance Funds and National Health Service.

24 For the year ended 31 March 2012, the Trust Statement records total revenues of £474.2 billion, compared to £469.7 billion in 2010-11. Overall, tax revenues have continued to recover from the effects of the recession in 2008-09 and 2009-10, although revenue within some individual elements has reduced:

- VAT revenue increased by £9.3 billion, largely due to the rate increase from 17.5 per cent to 20 per cent and increases in revenue from the oil, gas and business services sectors;
- revenue from corporation tax decreased by £6.3 billion as a result of turbulence in the financial sector, partly offset by increased revenue from offshore companies because of higher oil and gas prices;
- tax revenues for income tax and National Insurance have fallen by £1 billion, largely because the previous year's figure includes an overestimate of self-assessed income tax liabilities, which has been corrected in the current year; and
- other taxes and duties have risen by £2 billion as a result of rate rises for tobacco duty, alcohol duty, air passenger duty and insurance premium tax.

25 The 2011-12 Resource Accounts reported a net resource out-turn of £46.5 billion, which includes £12.2 billion programme expenditure on child benefit and £30.5 billion on tax credits. The resource out-turn was £811.6 million or 1.7 per cent below the estimate of £47.3 billion. The majority of this underspend was in respect of tax credits where payments were £719.7 million less than originally forecast. In line with revised HM Treasury guidance the reporting of tax credits has moved from the Trust Statement to the Resource Accounts this year.

26 The Valuation Office Agency seeks to break even and recover the full costs of the work it undertakes from clients. Income from fees and charges was £204.4 million in 2011-12, compared to expenditure of £202.7 million, generating a surplus of £1.7 million.

Progress on cost reduction

27 Departments remain under pressure to reduce costs. The scale of cost reduction required means that departments need to look beyond immediate short-term savings, and think more radically about how to take cost out of the business and how to sustain this longer term.

28 In our report *Cost reduction in central government: summary of progress* published in February 2012,¹³ we examined the cost reductions achieved by 12 departments. We found that departments successfully cut spending by £7.9 billion (2.3 per cent) in 2010-11 compared to 2009-10, but further cuts are needed in most departments over the next four years. We concluded that fundamental changes are needed in government to achieve sustainable reductions on the scale required – departments will achieve long-term value for money only if they identify and implement new ways of delivering their objectives, with a permanently lower cost base.

29 Under the 2010 Spending Review, covering the four-year period to March 2015, HMRC is required to reduce its annual running costs by £1.6 billion on a cumulative cash basis, a reduction of 25 per cent in real terms. HMRC will contribute to reducing the budget deficit by spending less on running costs and reducing expenditure on tax credits (and child benefit), as well as increasing tax revenues.

30 To support the cost reductions, HMRC planned to reduce staff numbers by 10,000; redeploy, retrain or recruit 9,000 staff; significantly reduce the number of offices; and reorganise corporate services. The Department has so far reduced the average number of permanently employed staff in year from 67,553 in 2010-11 to 64,483 in 2011-12 (a reduction of 3,070 full-time equivalent staff).¹⁴

31 In addition to reducing its running costs, HMRC is required to reduce expenditure on child benefit and tax credits by £8.3 billion over the spending review period. The Department did not meet its target to reduce personal tax credit error and fraud to no more than 5 per cent of the value of final awards by March 2011; its latest central estimate of the level of error and fraud for 2010-11 is 8.1 per cent. The Department reported that it identified £1.5 billion losses prevented through activity to tackle personal tax credits error and fraud to the end of March 2012, and it estimated that it was on course to achieve its target to identify a total of £1.7 billion prevented losses by July 2012.

NAO reports on financial management

32 During the last year we have not reported specifically on financial management in HMRC, but our wider examinations have identified a number of relevant issues.

33 Cost information: In our report on the *HM Revenue and Customs 2011-12 Accounts*¹⁵ we found that on tax debt management, while HMRC can identify the cost of using debt collection agencies, it does not have good information on the cost of other debt collection approaches. We also recommended that the Department should continue to prioritise its work to undertake full risk profiling and customer segmentation of its debt balance in order to tailor interventions and maximise debt collection. This work had been delayed from April 2011 to October 2012 as a result of the government's moratorium on IT projects in 2010 and the civil service recruitment freeze.

34 Measuring impact: In our report on the *HM Revenue and Customs 2011-12 Accounts*¹⁶ we found inconsistent measurement and inaccurate recording of the outcome of the Department's interventions to tackle error and fraud in personal tax credits awards. We recommended that HMRC improve the accuracy of calculating and recording these outcomes and better understand the link between these results and the levels of error and fraud in tax credits awards.

35 In our report *Reducing Costs in HM Revenue & Customs*¹⁷ we found that HMRC has comprehensive governance arrangements to deliver cost reductions, a good understanding of the administrative costs it incurs and has benchmarked accommodation and IT costs against the private sector and other government departments. We recommended that HMRC needed to develop further its understanding of the link between the cost and value of its activities, including the cost of end-to-end processes and of servicing different customer groups. We plan to follow up with further work on cost reduction.

¹³ Comptroller and Auditor General, *Cost reduction in central government: summary of progress*, Session 2010–2012, HC 1788, National Audit Office, February 2012.

¹⁴ HM Revenue & Customs, *Annual Report and Accounts 2011-12*, HC 38, June 2012 page 90 note 7; HM Revenue & Customs, *Annual Report and Accounts 2010-11*, HC 981, July 2011 page 96 note 9.

¹⁵ Comptroller and Auditor General, 'Report by the Comptroller and Auditor General' in HM Revenue & Customs, *Annual Report and Accounts 2011-12*, HC 38, June 2012.

¹⁶ Comptroller and Auditor General, 'Report by the Comptroller and Auditor General' in HM Revenue & Customs, *Annual Report and Accounts 2011-12*, HC 38, June 2012.

¹⁷ Comptroller and Auditor General, *Reducing Costs in HM Revenue & Customs*, Session 2010–2012, HC 1278, National Audit Office, July 2011.

NAO financial audit findings

36 Our financial audit work involves understanding HMRC's operations; examining its internal controls; agreeing the accounting policies; auditing its transactions, liabilities and assets; and confirming that the accounts present a true and fair view. We also consider the regularity of the transactions of the Department in accordance with Parliament's intentions.

37 The Comptroller and Auditor General has qualified his regularity opinion on the Department's 2011-12 Resource Accounts due to the material level of error and fraud in personal tax credits expenditure. HMRC published its latest estimates of personal tax error and fraud in June 2012, which showed that the estimated level of error and fraud in payments made in 2010-11 was between 7.5 per cent and 8.8 per cent of entitlements (equating to overpayments of between £2.08 billion and £2.46 billion, up from between £1.85 billion and £2.28 billion in 2009-10).¹⁸ The Department's Trust Statement, in which personal tax credits were reported in previous years, has received similar qualified audit opinions since the scheme commenced in 2002-03 because of the estimated levels of error and fraud. The Department's 2011-12 Trust Statement received an unqualified audit opinion.

Issues raised in Governance Statements

38 We work with the Department and its sponsored bodies to improve the quality and transparency of published Governance Statements. We aim to ensure that the processes by which Statements are produced are robust and that the Statements comply with Treasury guidance.

39 During 2011-12, HMRC reported on progress in tackling a range of key challenges and risks, including: the change programme; the governance of large business tax settlements; the work to prevent internal fraud and corruption; work on clearing the backlog of PAYE open cases; progress on further reducing

the number of non-matching National Insurance contribution items;¹⁹ progress on the HMRC debt strategy; responses to system failures in the Excise Movement and Control System; developments in attendance management and employee engagement initiatives; and the threat of criminal attacks against HMRC systems and responses to specific threats.

40 In addition to the levels of personal tax credit error and fraud, material control weaknesses reported in 2011-12 included:²⁰

- Levels of **personal tax credit debt** are high at £4 billion. The Department decided not to pursue any inactive remaining debt over three years old, so the Resource Accounts record total losses of £1.22 billion from over one million remitted overpayments. This has allowed HMRC to focus on more recent debts and take actions tailored to the type of debt. These include recovering tax credit debt by changing PAYE codes, revising its approach to the direct recovery of debt, and using debt collection agencies (subject to funding). HMRC aims to maintain tax credit debt levels at under £4 billion in 2012-13.
- **Limitations within legacy systems.** The Department acknowledges that some of its older tax computer systems have financial reporting limitations. It is reliant on scans of these systems to establish aggregate levels of tax debt at the year-end as the system reports were not designed to produce detailed information on transactions, losses and balances beyond the summary totals. The Department expects that new systems will provide it with the opportunity to improve system reporting, but it considers that present funding constraints may impact on whether the new systems will resolve all the weaknesses identified.

¹⁸ The Department updated the 2009-10 estimates for error and fraud using the final results after initial error and fraud statistics were published in June 2011.

¹⁹ End of year information received from employers and pension schemes can include returns which cannot be matched to the relevant individual's record. After automatic tracing these returns are placed in a suspense file until they can be matched to the correct record. HMRC analysis indicates that 91 per cent of those returns added in 2011-12 have no impact on the contributors' National Insurance benefits. HMRC will continue to work with employers and pension scheme administrators to maintain the steady fall in the annual proportion of non-matching items entering the suspense file.

²⁰ HM Revenue & Customs, *Annual Report and Accounts 2011-12*, HC 38, June 2012, Governance Statement.

Part Three

Reported performance

41 Government needs robust, timely information on its activities, costs, progress against its objectives, and the cost-effectiveness of its activities. It also needs to be able to interpret that information, by reference to trends, benchmarks and other comparisons, to identify problems and opportunities. Departments need reliable information on which to design and deliver services and monitor quality, be confident about their productivity, and drive continuous improvement.

42 The Government aims to make more government information available to the public to help improve accountability and deliver economic benefits. Our study reviewing early progress of this transparency agenda²¹ concluded that while the government has significantly increased the amount and type of public sector information released, it would not maximise the net benefits of transparency without an evaluative framework for measuring the success and value for money of its transparency initiatives.

Reporting performance: Annual Reports and business plans

43 Each government department reports its performance against the priorities and objectives set out in its business plan. A transparency section of the plan includes indicators selected by the Department to reflect its key priorities and demonstrate the cost and effectiveness of the public services it is responsible for. These indicators fall broadly into three categories:

- input indicators: a subset of the data gathered by the Department on the resources used in delivering services;
- impact indicators: designed to help the public judge whether departmental policies are having the desired effect; and
- efficiency indicators: setting out the cost of common operational areas to allow the public to compare the Department's operations to other organisations.

44 A structural reform section of the plan provides a detailed list of actions and milestones designed to show the steps the Department is taking to implement the Government's reform agenda.

45 Departmental progress against indicators is published regularly in a Quarterly Data Summary, a standardised tool for reporting selected performance metrics for each government department in a way that facilitates comparison across departments. As well as the indicators described above, the Quarterly Data Summary includes information on overall departmental budgets and workforce statistics, and a wider selection of indicators on common areas of spend such as estates, procurement and ICT. An annual version of this information has been formally laid in Parliament in departments' 2011-12 Annual Reports and Accounts.

46 The Cabinet Office has reported that the accuracy of the data for all departments needs to dramatically improve²² and that there may not be common definitions and data collection processes between departments. These caveats mean that data on common areas of spend cannot currently be used to compare performance between departments and may be of limited use to judge individual departmental performance in its own right. Recognising the need to improve use of information across government, the Cabinet Office set out in the Civil Service Reform Plan its intention for departments to provide "good, comparable, accurate and reliable" management information. The Plan sets out the intention to put in place a robust cross-government management information system by October 2012. In addition, improving the quality of data is one of the key priorities within the departmental Open Data Strategies, published in June 2012. The Cabinet Office expects that, with improvements in data quality and timeliness, the public will be able to judge the performance of each department in a meaningful and understandable manner.

²¹ Comptroller and Auditor General, *Implementing Transparency*, Session 2010–2012, HC 1833, National Audit Office, April 2012.

²² www.cabinetoffice.gov.uk/resource-library/business-plan-quarterly-data-summary

Performance reported by the Department

47 HMRC's Business Plan²³ sets out its priorities for 2012 to 2015, as well as the key commitments involved in delivering its change programme, the latest version of which was published in May 2012. The business plan sets out the indicators which HMRC considers are most useful to the public in understanding the costs and outcomes of its revenue collection and benefits administration activity. Input indicators include the unit costs of collecting the main taxes and administering credits and benefits. HMRC has also defined a number of impact indicators, which include performance measures for enforcement and compliance, debt recovery, tackling benefit fraud and customer service.

48 HMRC reported its performance against each of the indicators in its 2011-12 Annual Report and Accounts.²⁴ Key results included:

- additional revenues from compliance activities of £16.7 billion (2010-11: £13.9 billion), £1.7 billion above target;
- prevented losses as a result of error and fraud of £1.5 billion within personal tax credits to March 2012 (42 per cent more than 2010-11);
- improved customer service standards, with 74 per cent of calls attempts handled by contact centres (48 per cent in 2010-11); and
- a reduction in the number of working days lost through sickness absence of around 22 per cent from 2010-11.

49 HMRC also publishes data on its performance against the 23 actions specified in its Structural Reform Plan. These mainly relate to planned changes in tax administration and policy, including steps to improve enforcement and compliance and service. In June 2012, HMRC reported that none of the actions within the plan were overdue.²⁵

Testing the reliability of performance data across government

50 We have begun a three-year programme to examine the data systems underpinning the Departmental business plan indicators and other key management information. In August 2012, we published the results of our examination of a sample of departments' indicators and operational data systems used to report performance for the Department. This involved a detailed review of the processes and controls governing: the selection, collection, processing and analysis of data; the match between the Department's stated objectives and the indicators it has chosen; and the reporting of results.

51 Our report *Information Assurance Summary Reports: HM Revenue & Customs*²⁶ found that the input and impact indicators published in the business plan and the Quarterly Data Summary are aligned with the Department's vision and the main areas of business. We found that 13 of the 19 data systems report data accurately, and that the Department is working to improve the accuracy of the remaining six.

52 We also found areas where performance information could be improved to give better information on how the Department is performing in priority areas and making progress with the challenges it faces. HMRC aims to improve the efficiency of its operations but the published indicators measuring the unit costs of collecting tax and administering benefits are not affected by efficiency alone, which may make comparisons over time misleading. HMRC recognises that unit cost indicators can be affected by other external factors such as tax rates and economic conditions, and is therefore working to develop measures that are less vulnerable to these effects. We recommended that HMRC should consider what these indicators are intended to show, whether their construction is consistent with measuring efficiency and whether they provide a clear assessment of the Department's performance over time.

23 HM Revenue & Customs, *Business Plan 2012-15*, April 2010.

24 HM Revenue & Customs, *Annual Report and Accounts 2011-12*, HC 38 June 2012, Chapter 4: How we performed.

25 transparency.number10.gov.uk/business-plan/13

26 National Audit Office, *Information Assurance Summary Reports: HM Revenue & Customs*, August 2012.

53 HMRC's published and operational indicators focus on current year performance, which means that performance reports do not project performance beyond the end of the financial year in all areas and do not highlight all future challenges or risks. We recommended that HMRC should develop performance measures which provide it with forward-looking information and which alert it to challenges and risks ahead.

The future of information management

54 Departments released updated versions of their business plans in May 2012 which included changes to their priorities and indicators. Coalition priorities for HMRC have remained the same as those identified in 2011. Departments have aligned their input and impact indicators with the Government's priorities, so that the public can better understand how they are meant to be used for accountability. The changes are a step towards the alignment of costs and results which would allow for assessment of value for money, but they will not improve the data systems underlying published indicators, or the reliability of subsequent data.

Issues identified in NAO reports

55 In our report on the *HM Revenue and Customs 2011-12 Accounts*²⁷ we identified that there were broad themes linking recommendations made in all our work in 2011-12. In summary, we recommended that the Department should:

- improve its analysis of the costs and benefits of its interventions, such as debt campaigns, and initiatives to reduce tax credits error and fraud;
- use better understanding of risks, such as risk profiling of taxpayers, to prioritise and target its activities; and
- be clearer, before implementing significant structural changes, about what its future operating model will be. For example, it should set out how its business will be changed by the implementation of RTI and Universal Credit.

56 The Department's vision for 2015 is to create a tax administration that is more efficient, flexible in its response to customers and more effective in bringing in revenues. This will be challenging as the

Department faces a great deal of change during the period. In our report on the *HM Revenue and Customs 2011-12 Accounts*²⁸ we concluded that while HMRC had a business plan, a customer-centric strategy and a change programme seeking to coordinate delivery of major projects, the Department did not have an organisation-wide operational strategy. Such a strategy would set out how it would deliver tax administration in the future, supported by planning of resources, communications with customers and changes to working practices. It would help the Department to establish the interdependencies between projects and develop an integrated response. The strategy would also help address and mitigate some of the operational difficulties outlined in our other recent reports.

57 Below we present a selection of the most important findings from individual reports we have published since July 2011, arranged within HMRC's three core objectives: increasing revenue, providing a better service to customers, and reducing costs.

Increasing revenue

58 Reducing error and fraud: Excise duties on alcohol generated £9.5 billion of revenue in 2010-11. The Department estimated that evasion of alcohol duty could have cost the taxpayer over £1 billion in 2009-10, and that fraud was on the rise. The Department launched its Renewed Alcohol Strategy in April 2009, with implementation from April 2010. Our report *HM Revenue and Customs Renewed Alcohol Strategy: A progress report*²⁹ found that the Department achieved its key financial objective in the first year of the strategy, delivering £433 million of financial benefits against a target of £390 million. However, we found that the Department was not working successfully with industry to disrupt those who were illegally diverting duty-unpaid alcohol back into the UK market. We also found there was a low level of criminal sanctions against those committing fraud. The Department has no explicit objective in its strategy to increase the number and impact of criminal investigations and prosecutions. Our report recommended that the Department should improve the quality, depth and analysis of performance information used to support its strategy.³⁰

27 Comptroller and Auditor General, 'Report by the Comptroller and Auditor General' in HM Revenue & Customs, *Annual Report and Accounts 2011-12*, HC 38, June 2012.

28 Comptroller and Auditor General, 'Report by the Comptroller and Auditor General' in HM Revenue & Customs, *Annual Report and Accounts 2011-12*, HC 38, June 2012.

29 Comptroller and Auditor General, *HM Revenue & Customs Renewed Alcohol Strategy: A Progress Report*, Session 2010-2012, HC 1702, National Audit Office, January 2012.

30 Comptroller and Auditor General, 'Report by the Comptroller and Auditor General' in HM Revenue & Customs, *Annual Report and Accounts 2011-12*, HC 38, June 2012.

59 Ensuring tax compliance: Our report on *The compliance and enforcement programme*³¹ found that the programme had helped the Department to substantially increase tax yield, the measure of additional tax arising from compliance work, to March 2011, achieving net additional yield of £4.32 billion. Our report also found HMRC used different approaches to assess the impact of projects, which demonstrated elements of good practice but, in some cases, could have gone further to validate reported increases in yield. We recommended that the Department could better achieve value for money from its investment in compliance work by developing a fuller understanding of the impact of projects and helping people to use new technology by providing the right training at the right time.

60 Resolving tax disputes: In our report on *HM Revenue and Customs' 2010-11 Accounts*³² we examined the Department's governance arrangements for settling tax disputes with large companies. We concluded that the Department's governance processes were sound, including the High Risk Corporates Programme Board, and the substantial majority of the settlements examined complied with these governance processes. However, the Department set up specific governance arrangements in four of the largest settlements. In three of these cases, there was no, or limited, separation between the negotiation and approval of the settlements. There were also two cases where the Department did not comply with its established approval procedures and, in one of these cases, this resulted in a financial error over the charging of interest. The Committee of Public Accounts' report on tax disputes³³ made clear that it had serious concerns about how the Department handled the settlements where it bypassed or overlooked governance arrangements.

61 To address the lack of assurance over the settlements where the Department set up specific governance arrangements, or did not comply with its approval procedures, we examined five of these settlements using Sir Andrew Park, a retired tax judge, to provide expert advice. In our subsequent report *Settling large tax disputes*³⁴ we found that all five settlements were at least reasonable, and therefore provided a good overall outcome for the Exchequer. The report also confirmed our earlier findings that there was a strong case for improving the processes for reaching these settlements, particularly separation of roles in negotiating and authorising settlements. We concluded that it is not appropriate for the Department to set up specific governance arrangements, or to fail to apply processes correctly, and that there is a need for stronger assurance that the Department has applied its processes correctly. The Department has accepted our findings and is changing its governance arrangements.

Providing a better service to customers

62 Understanding the effects of changes on customer service:

In July 2011 we reported on *PaceSetter: HMRC's programme to improve business operations*,³⁵ which is aimed at improving HMRC's business processes. We found that the programme had improved productivity through new ways of working. We also found that there was limited evidence to provide assurance that PaceSetter-related reductions were achieved while maintaining or improving customer service and quality. We recommended that the Department should prioritise applying PaceSetter to the areas of greatest potential benefit and do more to integrate the programme with its wider change and cost reduction plans.

31 Comptroller and Auditor General, *HMRC The compliance and enforcement programme*, Session 2010-2012, HC 1588, National Audit Office, March 2012.

32 Comptroller and Auditor General, 'Report by the Comptroller and Auditor General' in HM Revenue & Customs, *Annual Report and Accounts 2010-11*, HC 981, July 2011.

33 HC Committee of Public Accounts, *HM Revenue & Customs 2010-11 Accounts: tax disputes*, Sixty-first Report of Session 2010-12, HC 1531, December 2011.

34 Comptroller and Auditor General, *Settling large tax disputes*, Session 2012-13, HC 188, National Audit Office, June 2012.

35 Comptroller and Auditor General, *Pacesetter: HMRC's programme to improve business operations*, Session 2010-12, HC 1280, National Audit Office, July 2011.

63 Our July 2011 report on *Reducing Costs in HM Revenue & Customs*³⁶ concluded that while the Department had established a clear vision for 2015 it had not yet sufficiently defined the business performance and customer service it intends to achieve.

64 Evaluating the customer experience: Our report on *The expansion of online filing of tax returns*³⁷ found that despite HMRC achieving an ambitious timetable with 11.5 million people now filing one or more returns online and growing customer confidence, customers' satisfaction with the assistance offered through the various helpdesks varied, and HMRC's website did not fully meet accessibility standards. In addition, HMRC used various methods to collect customer feedback but it had not benchmarked customer satisfaction with that of other online services. Our report *HMRC The compliance and enforcement programme*³⁸ found that while the programme established a series of measures to evaluate the intended improvement on customer experience, the Department did not routinely measure or report performance against these.

Reducing costs

65 Assessing the value for money of activities: HMRC needs more comprehensive cost information if it is to assess whether it is getting value for money from its activities. Our report on *Reducing Costs in HM Revenue & Customs*³⁹ found that while the Department has a clear vision for how it will look in 2015 and knows its main running costs, there were gaps in its understanding, such as on the link between costs and values. It must address these gaps to create the conditions to achieve value for money over the next four years.

66 Increasing digital and online services:

In 2007, HMRC launched its online filing expansion programme with the aim that all self-assessment, corporation tax, PAYE (in-year returns) and VAT returns would be delivered electronically by 2012. Our report on *The expansion of online filing of tax returns*⁴⁰ found that the Department was on track to deliver the programme to time and budget, and that there was evidence that the Department was achieving savings as a result. We recommended that it should collect more detailed cost information to assess whether it had maximised the benefits of using online returns.

67 Managing core skills: Staff skills are vital to HMRC achieving its business objectives and delivering its spending review commitments to reduce its running costs by 25 per cent by 2014-15 and bring in additional tax revenues of £20 billion a year, of which some £7 billion a year will arise from reinvestment. Our report *Core skills at HM Revenue & Customs*⁴¹ found that the Department could get better value for money from its £96.5 million investment in skills if it was directed more systematically at business priorities. We recommended that it should take a more strategic and informed approach to its investment, aligning skills needs and training more clearly with business objectives and holding business areas to account for performance. Our 2011 cross-government report, *Identifying and meeting central government's skills requirements*,⁴² similarly concluded that departmental skills strategies and governance arrangements across government have not been adequate to ensure that skills development is aligned with departmental business needs. We also found that data weaknesses limit departments' understanding of the skills they already have within the organisation.

36 Comptroller and Auditor General, *Reducing Costs in HM Revenue & Customs*, Session 2010–2012, HC 1278, National Audit Office, July 2011.

37 Comptroller and Auditor General, *The expansion of online filing of tax returns*, Session 2010–2012, HC 1457, National Audit Office, November 2011.

38 Comptroller and Auditor General, *HMRC The compliance and enforcement programme*, Session 2010–2012, HC 1588, National Audit Office, March 2012.

39 Comptroller and Auditor General, *Reducing Costs in HM Revenue & Customs*, Session 2010–2012, HC 1278, National Audit Office, July 2011.

40 Comptroller and Auditor General, *The expansion of online filing of tax returns*, Session 2010–2012, HC 1457, National Audit Office, November 2011.

41 Comptroller and Auditor General, *Core skills at HM Revenue & Customs*, Session 2010–2012, HC 1595, National Audit Office, December 2011.

42 Comptroller and Auditor General, *Identifying and meeting central government's skills requirements*, Session 2010–2012, HC 1276, National Audit Office, July 2011.

Appendix One

HMRC's sponsored bodies at 1 April 2012

HMRC has one executive agency, the Valuation Office Agency. The Agency provides property valuations and advice, to support the administration of taxation and benefits. The work of the Agency encompasses:⁴³

- compiling and maintaining lists of rateable values of the 1.8 million non-domestic properties in England, and the 100,000 in Wales, to support the collection of business rates;
- compiling and maintaining the lists of council tax bandings of some 23 million domestic properties in England and 1.3 million in Wales, to support the collection of council tax;
- determining local housing allowances across some 150 Broad Rental Market areas for housing benefit purposes and registering some 60,000 Rent Act 1977 fair rents in England;
- delivering a range of statutory and non-statutory valuation and surveying services to central and local government departments and the wider public sector; and
- providing valuation advice to HMRC in connection with capital gains, inheritance tax and other tax compliance work.

In addition, the Environmental Trust Scheme Regulatory Body Limited (ENTRUST) acts as regulator of the Landfill Communities Fund on behalf of HMRC.⁴⁴

43 Valuation Office Agency, *Annual Report and Accounts 2011-12*, HC 267, June 2012, page 6.

44 HM Revenue & Customs, *Annual Report and Accounts 2011-12*, HC 38, June 2012, page 49.

Appendix Two

Results of the Civil Service People Survey 2011

Question scores (% strongly agree or agree, % yes)

Civil service overall

Leadership and managing change

I feel that the department as a whole is managed well	40
Senior civil servants in the Department are sufficiently visible	46
I believe the actions of senior civil servants are consistent with the Department's values	39
I believe that the departmental board has a clear vision for the future of the Department	39
Overall, I have confidence in the decisions made by the Department's senior civil servants	36
I feel that change is managed well in the Department	27
When changes are made in the Department they are usually for the better	23
The Department keeps me informed about matters that affect me	55
I have the opportunity to contribute my views before decisions are made that affect me	36
I think it is safe to challenge the way things are done in the Department	38

Organisational objectives and purpose

I have a clear understanding of the Department's purpose	84
I have a clear understanding of the Department's objectives	79
I understand how my work contributes to the Department's objectives	81

Appendix Three

Reports by the NAO on the Department since 2009-10

Publication date	Report title	HC number	Parliamentary session
1 August 2012	Information Assurance Summary Reports: HM Revenue & Customs	www.nao.org.uk/publications/1213/review_data_systems_hmrc.aspx	
28 June 2012	HM Revenue & Customs: 2011-12 Accounts	HC 38	2012-13
14 June 2012	Settling large tax disputes	HC 188	2012-13
1 March 2012	HM Revenue & Customs, The compliance and enforcement programme	HC 1588	2010-2012
25 January 2012	HM Revenue & Customs Renewed Alcohol Strategy: A Progress Report	HC 1702	2010-2012
15 December 2011	National Insurance Fund Account 2010-11	HC 1685	2010-2012
	Northern Ireland National Insurance Fund Account 2010-11	HC 1686	2010-2012
2 December 2011	Core skills at HM Revenue & Customs	HC 1595	2010-2012
11 November 2011	The expansion of online filing of tax returns	HC 1457	2010-2012
4 October 2011	Departmental Overview: A summary of NAO's work on HM Revenue & Customs 2010-11	www.nao.org.uk/publications/1012/departmental_overview_hmrc.aspx	
20 July 2011	Reducing costs in HM Revenue & Customs	HC 1278	2010-2012
15 July 2011	PaceSetter: HM Revenue & Customs programme to improve business performance	HC 1280	2010-2012
7 July 2011	HM Revenue & Customs: 2010-11 Accounts	HC 981	2010-2012
10 January 2011	National Insurance Fund Account 2009-10	HC 679	2010-2012
	Northern Ireland National Insurance Fund Account 2009-10	HC 680	2010-2012
17 December 2010	Managing civil tax investigations	HC 677	2010-11
13 October 2010	HM Revenue & Customs: Engaging with tax agents	HC 486	2010-11
20 July 2010	HM Revenue & Customs: 2009-10 Accounts	HC 299	2010-11
20 July 2010	HM Revenue & Customs: Independent review of reported CSR07 value for money savings	HC 293	2010-11

Publication date	Report title	HC number	Parliamentary session
6 July 2010	Short guide to the NAO's work on HM Revenue & Customs	www.nao.org.uk/publications/1011/short_guide_hmrc.aspx	
30 June 2010	HM Revenue & Customs: The efficiency of National Insurance administration	HC 184	2010-11
15 January 2010	HM Revenue & Customs: Handling telephone enquiries	HC 211	2009-10
15 December 2009	National Insurance Fund Account 2008-09	HC 15	2009-10
	Northern Ireland National Insurance Fund Account 2008-09	HC 16	2009-10
3 December 2009	HM Revenue & Customs' estate private finance deal eight years on	HC 30	2009-10
23 October 2009	Dealing with the tax obligations of older people	HC 961	2008-09
20 July 2009	HM Revenue & Customs: 2008-09 Accounts	HC 464	2008-09
15 May 2009	HM Revenue & Customs: Managing variations in workload	HC 507	2008-09

Appendix Four

Recent cross-government NAO reports of relevance to HM Revenue & Customs

Publication date	Report title	HC number	Parliamentary session
25 July 2012	Governance for Agile Delivery	www.nao.org.uk/publications/1213/governance_for_agile_delivery.aspx	
20 June 2012	The effectiveness of internal audit in central government	HC 23	2012-13
2 May 2012	Assurance for major projects	HC 1698	2010–2012
18 April 2012	Implementing transparency	HC 1833	2010–2012
20 March 2012	The Government Procurement Card	HC 1828	2010–2012
15 March 2012	Managing early departures in central government	HC 1795	2010–2012
6 March 2012	Efficiency and reform in government corporate functions through shared service centres	HC 1790	2010–2012
2 March 2012	Improving the efficiency of central government office property	HC 1826	2010–2012
2 February 2012	Cost reduction in central government: summary of progress	HC 1788	2010–2012
21 December 2011	Implementing the Government ICT Strategy: six-month review of progress	HC 1594	2010–2012
9 December 2011	Digital Britain One: Shared Infrastructure and services for government online	HC 1589	2010–2012
13 July 2011	Identifying and meeting central government's skills requirements	HC 1276	2010–2012

Appendix Five

Other sources of information

Reports from the Committee of Public Accounts since 2010

Publication date	Report title	HC number	Parliamentary session
24 May 2012	HM Revenue & Customs: Compliance and Enforcement Programme	HC 1892	2010–2012
20 December 2011	HM Revenue & Customs: PAYE, tax credit debt and cost reduction	HC 1565	2010–2012
20 December 2011	HM Revenue & Customs 2010-11 Accounts: tax disputes	HC 1531	2010–2012
9 March 2011	Managing civil tax investigations	HC 765	2010-11
25 January 2011	HM Revenue & Customs' 2009-10 Accounts	HC 502	2010-11
24 March 2010	HM Revenue & Customs' estate private finance deal eight years on	HC 312	2009-10
17 March 2010	HM Revenue & Customs: Handling telephone enquiries	HC 389	2009-10
1 February 2010	HM Revenue & Customs: Dealing with the tax obligations of older people	HC 141	2009-10

Recent reports from Central Government

May 2012	HM Revenue & Customs	Business Plan 2012-15
March 2012	HM Revenue & Customs	Making tax easier, quicker and simpler for small business
February 2012	Office of Tax Simplification	Small business tax review: Final Report
February 2011	HM Revenue & Customs	Change Plan – Outline of planned programmes and projects
February 2011	Department for Work and Pensions	Welfare Reform Bill introduced to Parliament
November 2010	Department for Work and Pensions	White Paper 'Universal Credit: welfare that works'

Cabinet Office Capability Reviews of HMRC

March 2012	Capability Action Plan
December 2009	Re-review (HM Revenue & Customs: Progress and next steps)
December 2007	Original review

Where to find out more

The National Audit Office website is
www.nao.org.uk

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