National Audit Office

Report
by the Comptroller
and Auditor General

HM Revenue & Customs

HMRC's approach to collecting tax from high net worth individuals

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Summary

Introduction

1 HM Revenue & Customs (HMRC) is responsible for administering the tax system, including managing and reducing risks to the collection of tax revenue. One of its three objectives is to "maximise revenues due and bear down on avoidance and evasion".

2 HMRC focuses on the people and businesses it considers pose the greatest risk of not paying the correct amount of tax. One such group is high net worth individuals. These are the very wealthiest people in the UK.

3 HMRC considered there to be around 6,500 high net worth individuals at the start of 2015-16. These are people who have a net worth of more than £20 million. Net worth refers to all of the assets a persons owns – such as property, stocks, savings and interests in other entities – less any debts. The threshold at which HMRC considers someone a high net worth individual changed during 2016-17 to a net worth of more than £10 million. For the purposes of this report, where we refer to high net worth individuals we mean those who have a net worth of £20 million or more.

Scope of this report

4 This report examines the issues facing HMRC in dealing with the tax affairs of high net worth individuals. In this report we consider:

- the tax risks posed by high net worth individuals (Part One);
- how HMRC organises its work with high net worth individuals (Part Two);
- how HMRC identifies high net worth individuals and enquires into their tax affairs (Part Three); and
- how HMRC measures the impact of its work (Part Four).

5 We also examine HMRC's approach to high net worth individuals and:

- marketed tax avoidance schemes (Appendix One);
- offshore tax evasion (Appendix Two); and
- inheritance tax (Appendix Three).

These are areas of HMRC's work that have been of interest to the Committee of Public Accounts.

6 In future work, we intend to examine HMRC's response to dealing with the tax affairs of affluent individuals. These are people who have an annual income of at least £150,000, or wealth of £1 million or more.

Key points

The tax risks posed by high net worth individuals

7 The amounts of tax revenue that are at stake are significant. HMRC has identified that there are around 6,500 high net worth individuals. These are the very wealthiest people in the UK, and account for roughly 0.02% of all taxpayers. In 2014-15, high net worth individuals paid more than £4.3 billion in tax. This included £3.5 billion in income tax and national insurance, which was 1.3% of the total revenue for those taxes. They also paid £880 million in capital gains tax, which accounted for 15% of all capital gains tax in that year. HMRC does not record other types of tax that are collected, such as inheritance tax, in a way that easily allows it to identify the amounts paid on high net worth individuals' wealth (paragraphs 1.1 to 1.7).

8 High net worth individuals have complex tax affairs. Their wealth can take many forms. It typically includes assets such as property and investment income, and they may have complex business arrangements. Their assets may be located in many different countries, and they generally have more choice over how they manage their income and assets than the average taxpayer. Almost all high net worth individuals use tax agents to manage and advise on their tax affairs. It can be challenging for HMRC to understand their tax affairs and assess if there are any risks to address (paragraphs 1.7 to 1.9 and Figure 6).

9 HMRC is investigating risks from high net worth individuals with a potential value of £1.9 billion. This figure is an initial estimate of the tax that could be due at the start of 2015-16 and covers more than one tax year. Of this, £1.1 billion relates to the use of marketed avoidance schemes; around 15% of high net worth individuals have used at least one scheme. HMRC has identified that the risks from high net worth individuals relate primarily to tax avoidance and the legal interpretation of complex tax issues, rather than tax evasion. HMRC is developing its analysis of the scale and nature of the risks (paragraphs 1.10 to 1.12).

How HMRC has organised its work with high net worth individuals

10 **In 2009, HMRC established a specialist unit to manage the tax affairs of high net worth individuals.** Before this unit was set up, HMRC's approach to high net worth individuals was dispersed, with no single part of its business responsible for their tax affairs. HMRC set up the high net worth unit to give it a better understanding of the overall tax position of high net worth individuals and their behaviour. In 2009, the Organisation for Economic Co-operation and Development (OECD) recommended, following consultation with tax authorities including HMRC, that tax authorities set up appropriate structures to administer the tax affairs of high net worth individuals. In 2015, the OECD reported that one-third of countries had done so and around half of G20 countries (paragraphs 2.1 to 2.3 and 2.10).

11 **HMRC assigns a customer relationship manager to each high net worth individual.** The customer relationship managers are responsible for understanding the risks and behaviours of the people assigned to them. In practice, this means working with that person's tax agent. Customer relationship managers have a team of staff working with them. Each of the 40 customer relationship managers and their teams are responsible for around 160 taxpayers. The use of customer relationship managers for high net worth individuals is not common in other countries (paragraphs 2.4, 2.10 and Figure 10).

12 **HMRC has made organisational changes that are designed to strengthen its understanding of risk.** In October 2016, HMRC brought all of its compliance work under one area of its business, called customer compliance. These organisational changes bring together its work with businesses, individual taxpayers and bodies such as trusts. HMRC told us that it hopes they will help strengthen its understanding of high net worth individuals and the links between their personal wealth and the entities with which they are connected. High net worth individuals may have interests across different areas of tax, including businesses and trusts (paragraphs 2.15 and 2.16).

How HMRC identifies high net worth individuals and enquires into their tax affairs

13 **It is not straightforward for HMRC to identify high net worth individuals and their tax risks, as most of the information about their wealth does not need to be reported.** The UK raises tax on income rather than wealth, except for some disposals or transfers of assets. Taxpayers in the UK are required to complete self-assessment tax returns and disclose taxable income and gains, but not the sources of income or the assets they own. In 2015-16, in preparing to expand the high net worth unit, HMRC undertook an exercise to identify people with a net worth of more than £10 million. This brought an extra 1,000 people with net worth of more than £20 million into the high net worth unit, in addition to the 6,500 that HMRC already knew about (paragraphs 3.2 and 3.4).

14 HMRC is currently running a formal enquiry on around a third of high net worth taxpayers, with an average of four issues being examined per taxpayer. Where HMRC does not understand or agree with the position taken by a taxpayer it will open a formal enquiry. Customer relationship managers use the understanding of individual taxpayers they have developed over time to identify taxpayers at risk of misstating their tax affairs. They aim to resolve issues before the taxpayer submits their tax return. New information may trigger a reassessment of risks. Where customer relationship managers identify a tax risk that cannot be easily resolved, they will open a formal enquiry. These enquiries can take a long time to resolve; 6,000 issues under enquiry have been open for more than 18 months, 4,000 of which have been open for more than three years (paragraph 3.6 and Figure 17).

15 HMRC prioritises the recovery of tax where it identifies fraud and uses civil investigations in the majority of cases. Where high net worth individuals are suspected of tax fraud, their case is passed to a specialist team within HMRC which examines whether the evidence is sufficient to merit a criminal, rather than civil, investigation. In the last five years, HMRC has investigated and closed 72 cases relating to high net worth individuals. Of these, 70 were investigated with civil powers. Two cases were criminally investigated. These cases were passed to the Crown Prosecution Service, and one was taken forward and successfully convicted. At October 2016 HMRC was criminally investigating a further 10 high net worth individuals. HMRC has a target to increase to 100 the number of prosecutions of wealthy individuals and corporates made each year by 2020. There is no expectation for how many additional high net worth individuals will be prosecuted (paragraphs 3.10 to 3.12 and Figure 14).

How HMRC measures the impact of its work

16 HMRC recorded yield of £416 million in 2015-16 from the work of the high net worth unit. This is an increase from £200 million in 2011-12, and exceeds HMRC's internal target of £260 million in 2015-16. High net worth individuals are a relatively small population and the trend in yields can fluctuate due to a small number of one-off but high-value cases. In addition to the work of the high net worth unit, since 2009 HMRC has recorded yield from high net worth individuals of around £450 million. Around half of this – £230 million – has come from its work in tackling marketed avoidance schemes and around £140 million from the use of offshore disclosure facilities. A further £80 million relates to civil fraud investigations since 2011 (paragraphs 4.2 to 4.4 and 4.7).

17 HMRC has developed its approach over time. HMRC initially focused on getting a better understanding of the circumstances of high net worth individuals. This meant each taxpayer was subject to the same level of review. It has since refined its approach to become increasingly focused on the riskiest taxpayers. HMRC is also developing its understanding of the characteristics of the high net worth population. It has identified events that might happen during a person’s life that present a particular risk. It has started to bring together its internal data on high net worth individuals to improve its understanding of the population as a whole. We think it could usefully build on this analysis by considering what external data could help it to predict how the very wealthy might respond to changing economic and market conditions (paragraphs 2.12 to 2.14 and 4.11).

18 HMRC has not evaluated its approach to high net worth individuals. HMRC has taken as indicators of success the yields from its work, feedback from tax agents and indicators of changes in behaviour, such as fewer late self-assessment returns. It has not, however, looked at what works and why in its current approach. It could use such analysis to increase the impact of its work. While the OECD has recommended that tax authorities focus resources on high net worth individuals, there are choices to be made about how to do this. We outline some of these in **Figure 2** (paragraphs 4.2, 4.8 and 4.10).

Concluding comments

19 Assessing the correct amount of tax owed by high net worth individuals is a challenge for all tax authorities. The tax affairs of the wealthiest in society are complex, making it harder for tax authorities to ensure that they are paying the right amount of tax. HMRC has a dedicated team to handle the tax affairs of high net worth individuals, which is a sensible approach given the tax at stake, and follows the best-practice advice of the OECD. It has allowed HMRC to get a better understanding of the tax affairs and behaviours of these taxpayers, and the yields from HMRC’s work in this area have increased. HMRC has now aligned the work of the high net worth unit more closely with other parts of its business that focus on compliance risk. This change should help HMRC increase the expertise it brings to bear in identifying and challenging the behaviour of the wealthiest taxpayers where they do not comply with HMRC’s interpretation of tax law.

20 We see potential for HMRC to increase its effectiveness in this area by analysing its experience to date and by triangulating its knowledge of individual taxpayers with wider economic data which might indicate how this group of taxpayers could be expected to behave. HMRC is expanding the high net worth unit based on the yield it has delivered, but has not yet evaluated which approaches that are used within the unit are most effective. Such analysis could help the unit to maximise the benefit it achieves from its resources. HMRC should therefore do more to identify what works within its approach to high net worth individuals and to understand the outcomes it achieves. It should also consider whether it could usefully supplement its focus on individuals with a broader economic analysis, which would help it to predict how changes in asset values and profitability, for example, might influence the behaviour of this taxpayer group.