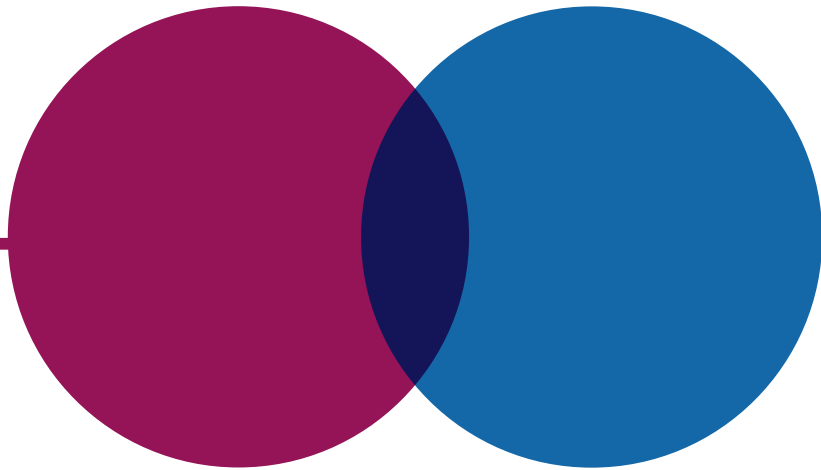




National Audit Office




REPORT

# Administration of Welsh rates of income tax 2022-23

HM Revenue & Customs

SESSION 2023-24  
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HC 389



We are the UK's independent public spending watchdog.

We support Parliament in holding government to account and we help improve public services through our high-quality audits.

The National Audit Office (NAO) scrutinises public spending for Parliament and is independent of government and the civil service. We help Parliament hold government to account and we use our insights to help people who manage and govern public bodies improve public services.

The Comptroller and Auditor General (C&AG), Gareth Davies, is an Officer of the House of Commons and leads the NAO. We audit the financial accounts of departments and other public bodies. We also examine and report on the value for money of how public money has been spent.

In 2022, the NAO's work led to a positive financial impact through reduced costs, improved service delivery, or other benefits to citizens, of £572 million.

## Key facts

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**1.4mn**

Welsh taxpayers  
in 2021-22

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**£2.4bn**

Welsh income tax revenue  
in 2021-22

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**£2.6bn**

HM Revenue & Customs'  
estimate of Welsh income  
tax revenue in 2022-23

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**£0.4 million** costs of administering Welsh income tax in 2022-23

# Summary

## Introduction

**1** The Wales Act 2014 gave the Senedd (Welsh Parliament) power to determine the rates (excluding the personal allowance) paid by Welsh taxpayers on all non-savings, non-dividend income, from 6 April 2017. The Welsh Government receives all income tax revenue generated from non-savings, non-dividend income under Welsh income tax policy.

**2** Since April 2019, the UK government has reduced the UK basic, higher and additional income tax rates by 10 percentage points for Welsh taxpayers and the Senedd has had the power to apply Welsh rates in addition. For each tax band, the rate of income tax paid is the sum of the reduced UK rate and the Welsh rate set for the year (**Figure 1** overleaf). As in previous years, for 2022-23 the Senedd set the Welsh rates of income tax at 10% across all bands, which meant that the total rates for taxpayers in Wales matched the UK rates at 20% (basic rate), 40% (higher rate) and 45% (additional rate).

### Roles and responsibilities

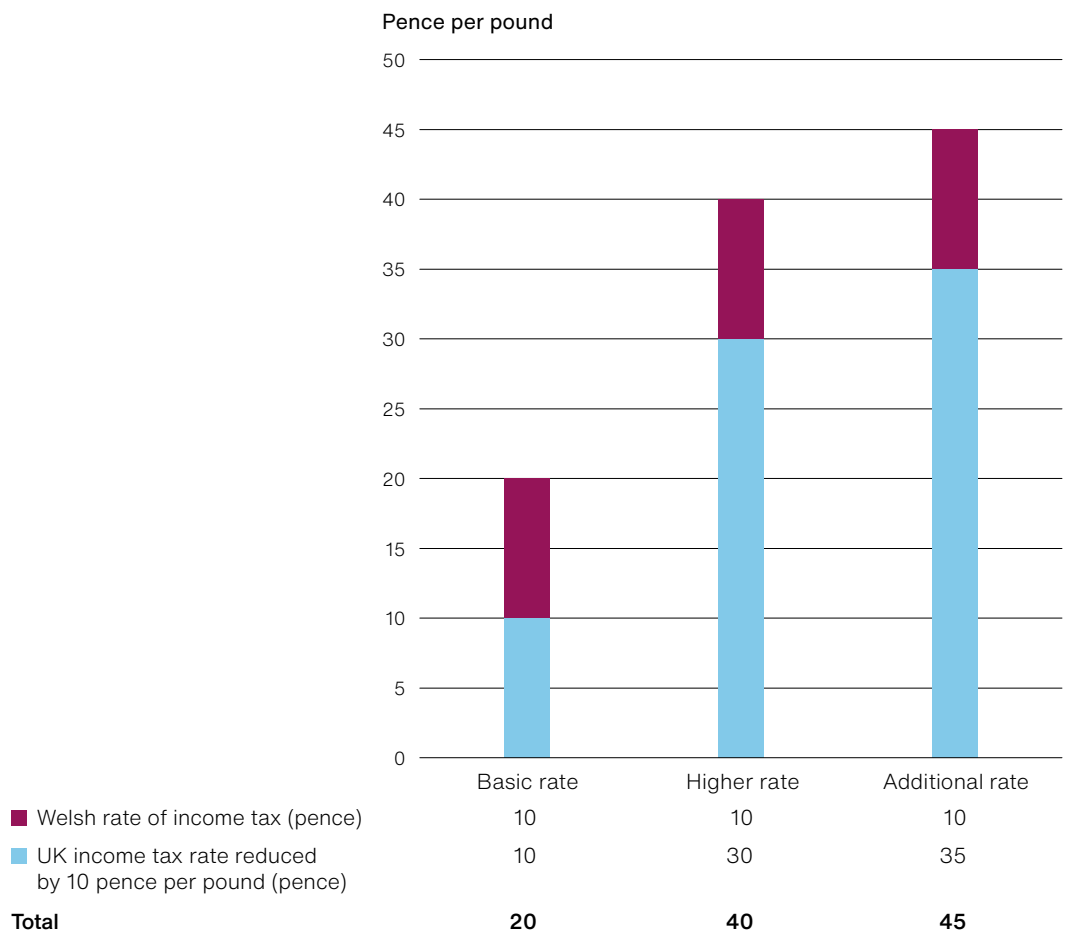
**3** HM Treasury is responsible for paying Welsh income tax to the Welsh Government. HM Revenue & Customs (HMRC) administers and collects Welsh income tax as part of the UK tax system. HMRC identifies taxpayers living in Wales by applying a 'flag' in its systems that indicates they are subject to Welsh income tax rates. HMRC has calculated that there were 1.4 million Welsh taxpayers in 2021-22.

**4** Following the end of each tax year, HMRC produces a provisional estimate of Welsh income tax revenue for that year. It calculates the final outturn the following year once it has received further information from taxpayers and employers. This report covers the final outturn for 2021-22 and the provisional estimate for 2022-23. HMRC expects to publish the outturn for 2022-23 in its 2023-24 Annual Report and Accounts.

**Figure 1**

Welsh rates of income tax for 2022-23

The UK rates of income tax are reduced by 10 pence per pound and replaced with the Welsh rates of income tax



**Notes**

- 1 For each tax band (basic, higher and additional), the UK government reduces the amount of tax it will collect by 10 pence per pound and the Senedd (Welsh Parliament) sets the Welsh rate of income tax to be added to the UK rates of tax.
- 2 For 2022-23, the Senedd set each Welsh rate of income tax at 10 pence, meaning that Welsh taxpayers pay an amount of tax equivalent to the UK rate for each tax band.

Source: National Audit Office analysis of data from the Welsh Government

**5** The Government of Wales Act 2006, as amended by the Wales Act 2014, requires the Comptroller and Auditor General (C&AG) to prepare a report for each financial year on:

- the adequacy of HMRC's rules and procedures, in consequence of the Welsh rate provisions, to ensure the proper assessment and collection of income tax charged at rates determined by those provisions;
- whether HMRC is complying with these rules and procedures;
- the correctness of the sums brought to account by HMRC which relate to income tax that is attributable to a Welsh rate resolution; and
- the accuracy and fairness of amounts reimbursed to HMRC as administrative expenses.

**6** This report assesses:

- HMRC's calculation of the 2021-22 income tax revenue for Wales (the 'outturn') and assurance on the correctness of amounts brought to account (Part One);
- HMRC's estimate of the 2022-23 income tax revenue for Wales and our view on the estimate methodology (Part One);
- key controls operated by HMRC to assess and collect income tax (Part Two);
- HMRC's approach to assessing and mitigating the risk of non-compliance with Welsh tax requirements (Part Two); and
- the cost of administering Welsh income tax. We provide assurance on the accuracy and fairness of these amounts in agreement between HMRC and the Welsh Government (Part Three).

**7** Appendix One sets out our audit evidence base.

## Key findings

### Welsh income tax 2021-22 final outturn and 2022-23 estimate

**8 HMRC calculated the final outturn for 2021-22 as £2,384 million, representing amounts collected under Welsh income tax policy.** HMRC's estimate of 2021-22 Welsh income tax revenue, published in July 2022, was £2,356 million, meaning the actual outturn was £28 million (1.2%) higher than HMRC had originally estimated. We examined HMRC's methodology for calculating the actual outturn, which necessarily includes some remaining areas of estimation, for instance where HMRC had not yet received returns from taxpayers. In these areas, we have evaluated the basis of HMRC's estimate, including the relevant assumptions and available data. Based on that audit work, we have concluded that the Welsh income tax revenue outturn for 2021-22 is fairly stated (paragraphs 1.2 to 1.15).

**9 HMRC has estimated Welsh income tax revenue for 2022-23 as £2,589 million.** This represents an increase of £205 million (8.6%) compared with the 2021-22 outturn. Income tax for the whole of the UK increased by 8.9% in 2022-23. The increases in UK and estimated Welsh income tax revenues reflect inflationary rises in earnings and the freezing of income tax bands and thresholds. This increased the size of the taxpayer population and moved some taxpayers into higher tax brackets. HMRC expects to calculate the finalised 2022-23 income tax outturn attributable to Wales in 2024. The estimate HMRC produces is solely for financial reporting purposes in its annual accounts and does not affect the amount of revenue that the Welsh Government ultimately receives (paragraphs 1.16 to 1.19).

**10 External factors have increased the level of uncertainty in HMRC's estimate of Welsh income tax revenue in 2022-23.** HMRC identified the key source of uncertainty as the accuracy with which it can estimate Wales's share of UK income tax liabilities, particularly since its estimate for 2022-23 relies on survey data from 2019-20. HMRC has highlighted high interest rates and inflation, wage growth and high and volatile energy prices as external factors causing increased uncertainty in 2022-23. We consider the approach adopted by HMRC to estimating the impact of these areas of uncertainty on Welsh income tax revenue in 2022-23 to be reasonable (paragraph 1.20).

### Administration of Welsh rates of income tax

**11 HMRC has adequate rules and procedures in place to ensure the proper assessment and collection of Welsh income tax and it is complying with those rules.** Our work on Welsh income tax matters builds on our wider assessment of HMRC's rules and procedures, completed as part of our annual audit of HMRC. As part of that audit, we concluded that HMRC had framed adequate regulations and procedures to secure an effective check on the assessment, collection and proper allocation of revenue, and that these regulations and procedures are being duly carried out (paragraphs 2.2 to 2.14).

**12 Maintaining an accurate and complete record of the addresses of Welsh taxpayers remains HMRC’s key challenge in administering the system.**

HMRC relies on taxpayers notifying it of a change of address, although there is no legal requirement for them to do so. We found that there had been a decrease in the number of Welsh postcodes identified by HMRC’s address-cleansing work as either missing or invalid, with 4% (52,319) of the overall taxpayer population identified as either missing or invalid in its 2022-23 scan in November 2022. This was lower than the 6% (81,716) in June 2021. HMRC has investigated and updated those cases with taxable income during the year (paragraphs 2.15 to 2.24).

**13 HMRC continues to assess the risk of non-compliance in relation to Welsh income tax as low because there is no divergence between Welsh tax rates and the rest of the UK.** In 2022-23, HMRC produced a Strategic Picture of Risk (SPR) for Welsh rates of income tax. It considers the main areas of risk to Welsh income tax to be the same as those compliance risks which it assesses at the whole-of-UK level. There are no risks that HMRC identifies in this SPR which are specific to Wales as HMRC assesses that compliance risk in Wales is consistent with the rest of the UK (paragraphs 2.26 and 2.27).

**14 HMRC calculated a compliance yield of £120 million relating to Wales for 2021-22, the most recent data available.** HMRC measures the effectiveness of its enforcement and compliance activities through compliance yield: its estimate of the additional revenues it has generated, and the revenue losses it has prevented. HMRC estimated that the Welsh share of net losses from compliance risks for 2020-21, the most recent data available, was £390 million. HMRC calculates these figures as a proportion of the equivalent UK figure, rather than using Welsh-specific data to quantify the risks. HMRC does not consider or report on geographical variations in the level of compliance risk, or the relative success of compliance activity in Wales compared with the rest of the UK (paragraph 2.31).

**15 HMRC has limited performance data about its compliance activities in Wales.** Unlike its income tax system, which flags residents as Welsh, HMRC’s compliance system cannot readily identify people living in Wales. HMRC therefore cannot easily track and monitor compliance activity in Wales and this affects its ability to collect performance data about the extent of Welsh non-compliance (paragraph 2.29).



**16 HMRC's compliance activities increased in 2022-23 but it failed to meet its target for compliance yield.** Across the UK, the number of compliance cases that HMRC opened in 2022-23 was higher than in 2021-22 but 17% lower than in 2019-20 before the pandemic. It closed 20% fewer cases than in 2019-20. HMRC says this partly reflects its strategy to focus increasingly on upstream efforts to ensure taxpayers comply in the first place, and to prioritise larger and higher-impact cases. HMRC's yield from its tax compliance activities for the whole of the UK was £34.0 billion in 2022-23, up 10% compared with 2021-22 and higher than the average over the past five years (2018-19 to 2022-23) of £33.2 billion. Compliance yield in 2022-23 was, however, below HMRC's target of £36 billion. As a proportion of total revenue, compliance yield remained at 4.2% (paragraphs 2.28 to 2.30).

**17 UK tax debt has increased since 2022 and remains higher than pre-pandemic levels.** HMRC's debt balance is affected by external factors that have an impact on taxpayers' ability to pay their tax liabilities, including current inflationary pressures and increases in the cost of living. At 31 March 2023, total tax debt for the UK was £43.9 billion, 11.9% (£4.7 billion) higher than the level of debt that HMRC reported at 31 March 2022. Tax debt more than trebled in the first six months of 2020-21 due to the wider economic impact of the COVID-19 pandemic and HMRC's decision to suspend most debt collection. It remains higher than the five years leading up to the pandemic when tax debt was typically around £14 billion. HMRC has a new strategy to bring down tax debt in the long term but expects it to remain high throughout 2023-24. HMRC does not produce an estimate of the total income tax debt attributable to Welsh taxpayers (paragraphs 2.33 and 2.34).

## Costs

**18 In 2022-23 HMRC incurred and recharged £0.4 million to the Welsh Government for the cost of administering Welsh income tax.** We examined HMRC's method for estimating the costs of collecting and administering Welsh income tax for the year ended 31 March 2023. Based on our audit work, we have concluded that the amount paid by the Welsh Government was accurate and fair in the context of the agreement between HMRC and the Welsh Government (paragraphs 3.4 and 3.5).