

Big fish, little fish...

HMRC's compliance strategy is under the spotlight, says TaxWatch's Mike Lewis

The UK is in a fiscal tight spot. The Chancellor has promised to raise an additional £7.5 billion over the next four years by boosting HMRC compliance efforts. The Autumn Budget is likely to see more measures intended to make this number go up: perhaps extra compliance funding, new powers, additional anti-avoidance legislation.

None of this is new. Successive governments have looked to the tax gap, rightly, as a way to balance the books without raising taxes. What matters is how it's done. As a recent address to the Chartered Institute of Taxation by ex-FIS head Simon Yorke reminded us, the 'strategic intent' of HMRC's compliance efforts has varied over time: from the 'volume crime' approach to criminal enforcement targets in the 2010s; through to prioritizing defences against non-compliance such as tightening VAT registration to counter carousel fraud; and resourcing the long, complex, cross-border investigations needed to boost compliance yield from small numbers of highly lucrative 'whales' like Bernie Ecclestone.

It remains to be seen how HMRC's promised £1.7bn of additional compliance funding and 5,500 new compliance officers are going to be deployed. This year's tax gap publication, however, put the spotlight squarely on one area: small business non-compliance, now responsible for 60% of the tax gap, according to HMRC.

It would be absurd to ignore this ballooning category of non-compliance. The fact that 37% of small businesses' corporation tax returns apparently have significant errors – larger than £1000 of extra tax liability – shows the potential revenue gains from getting their tax returns right, and from tackling deliberate non-compliance in this sector.

However, before we close the books on wealthy offshore evaders and focus on 'men in white vans' (as tax lawyer Dan Neidle has characterized the problem), let's consider resources and efficiency. The tax gap figures suggest that a large slice of the small business gap is due to errors and failure to take due care. These are categories that customer service and upstream compliance functions are supposed to tackle: individual, incremental work, including by directorates other than customer compliance which do not appear to be getting additional staff or significant extra funding.

HMRC's compliance statistics also consistently show that larger and wealthier customer groups are easier to get revenue from per pound of compliance spend. Though ROI (return on investment – compliance yield divided by compliance spend) is a crude way of measuring the efficiency of compliance efforts, it nonetheless provides a rule-of-thumb indication of where revenue gains can be made most efficiently. Each pound that HMRC spent on non-

wealthy individual compliance in 2024/5 yielded £6.48 in additional revenue. That rose to £12.76 for wealthy individuals. Similarly, a pound spent on small business compliance yielded £10.40 in extra revenue; rising to £21.14 for mid-size businesses; and a massive £57.94 for large businesses.

In May, the National Audit Office disclosed that just one case pursued by HMRC's wealthy compliance team netted £2.5bn of compliance yield between 2022 and 2024: a larger sum than HMRC's total estimate of wealthy individuals' tax gap (£2.1 billion), just from one compliance case.

Of course, compliance strategy shouldn't be guided by financial efficiency alone: tax morale and the integrity of the system relies on everyone paying their due taxes, whoever they are. Differing ROIs, moreover, might be due to factors that can be changed – like differing capabilities or resourcing between compliance teams – rather than an immutable function of tackling non-compliance in a given taxpayer group.

Nonetheless, for tackling deliberate non-compliance amongst some taxpayer categories, penalizing or prosecuting 'enablers' of multiple cases of failed avoidance and evasion may be a more effective use of resources: scheme promoters, or those knowingly establishing and managing opaque legal vehicles for tax evaders. HMRC's belated focus on enablers in recent years is welcome. But, here again, new powers and compliance cases have focused on a small category of marketed scheme promoters whose numbers and revenue risk may be waning. HMRC estimates that there are now no more than "about 20ish active promoters", some linked to each other. This year's tax gap figures estimate that the tax authority loses around £200 million annually to marketed avoidance schemes – down from £1.5 billion in 2005-6. This is now a fairly small slice of the £47 billion tax gap.

HMRC is currently consulting on new powers against this small group, including new strict liability offences for failing to comply with DOTAS disclosure obligations, and the quasi-sanctions regime of the Promoter Action Notice, intended to starve promoters of access to service providers like banks and online advertising. TaxWatch has broadly welcomed these new proposed powers: but unless powers are actually used, both existing and new, they're toothless.

Meanwhile, bespoke enablers of much larger categories of avoidance and evasion, beyond marketed schemes, are barely being touched by penalties and prosecutions. TaxWatch has found, for example, that civil investigations that might lead to penalties for dishonest conduct by tax advisers, on the statute books since 2012, weren't even initiated through issuing a 'Conduct Order' more than five times in any year between 2020 and 2024, and possibly never in some years. As far as we can tell, powers to publish the names of tax advisers penalised for dishonesty – a measure that would help protect unwitting taxpayers – have never been used. Likewise, HMRC has confirmed that no penalty has ever been issued

to an enabler of offshore tax evasion since the measure was introduced in 2017 in the aftermath of the Panama Papers leak. Early August saw the start of HMRC's very first attempted prosecution of a company for alleged failure to prevent its staff from facilitating tax evasion: a corporate offence that also hasn't previously been used. This is welcome, although the trial itself won't begin until September 2027, a decade after the offence was first introduced.

Finally, beyond efficiency and powers, we need to think about fairness. This year's tax gap figures show that the estimated tax gap for 'wealthy taxpayers' – about with incomes over £200,000 or assets of over £2 million in any of the past three years – is roughly the same as the tax gap for all other individual taxpayers combined (around 35.4 million people). The difference between the missing tax of the two groups is narrowing – even before we consider that the wealthy tax gap is itself, according to the National Audit Office, likely a significant underestimate.

A different but comparable story can be told for business taxpayers. Although the small business tax gap now stands at a massive £28 billion of missing tax annually, and rising, that covers a population of 5.1 million small businesses. That equates to an average tax gap per taxpayer of under £6,000. Meanwhile, the aggregate tax gap of the 2,000 taxpayers falling within the Large Business Directorate is falling, but still represents an average tax gap per taxpayer of £2.9 million.

Efficiency matters. Taxpayers' equal treatment before the law matters. But perhaps it's time we also started thinking about the incidence of compliance efforts in similar terms to how we think about tax incidence itself. Everyone should pay their due: but are compliance efforts targeted at different taxpayers and enablers in proportion either to their responsibility for missing tax, or the reasons for their non-compliance? Equally, the processes and compliance routes accorded to different taxpayer groups may differ in ways that are not well understood. How does the experience of the digital disclosure facility for errors, carelessness and evasion by ordinary taxpayers, for instance, compare to the Worldwide Disclosure Facility for upper-end taxpayers with undeclared offshore income and gains?

TaxWatch plans next year to get under the bonnet of these questions, with research which will construct a 'Fair Tax Enforcement Index', tracking the incidence and outcomes of different compliance and enforcement efforts. We welcome suggestions about how this index should be designed, and what it should look at.

- Mike Lewis, TaxWatch