

Regulatory Impact Assessment: the Commissioners for Revenue and Customs Bill

November 2004



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the Commissioners for
Revenue and Customs Bill

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REGULATORY IMPACT ASSESSMENT

Issue

1. This report assesses the regulatory impact of the **Commissioners for Revenue and Customs (CRC) Bill**, which will implement the recommendation of the *Review of the Revenue Departments*¹ to create a single new department by integrating Inland Revenue and HM Customs & Excise. The Bill also creates the independent Revenue and Customs Prosecutions Office (RCPO) to prosecute all HMRC's offence cases in England and Wales. The Bill therefore primarily addresses machinery of government matters.

PART I – Background and options for legislation

2. The review considered several options for change, including options such as transferring responsibility for administering particular taxes between the departments. However, it focussed its analysis on three leading options:

- *status quo* plus, under which organisational change would be limited to that necessary to implement the recommendations the Review made on policy and accountability;
- creating a single new department, which integrates Customs and the Revenue; *and*
- strategic alignment, under which a strategic board would be formed to promote the long-term alignment of the existing departments.

3. It concluded that creating a single department offered the most benefits. Primary legislation is therefore necessary to make this machinery of Government change. More details about the remit of the Review of the Revenue Departments and its recommendations are contained at **Annex A**.

Main purpose and intended effect of the Bill

4. The Bill will set in place the legislative framework for the new integrated department along with necessary consequential changes. As well as the legal establishment of HMRC, the Bill also includes the legislative authority for the existing independent prosecuting office for Customs and Excise (CEPO)², brings Inland Revenue prosecutions within its functions, and gives the office a new name: the Revenue and Customs Prosecutions Office (RCPO). Part III of this RIA describes the prosecutions office in more detail.

What this Regulatory Impact Assessment covers

5. This Regulatory Impact Assessment (RIA) appraises various options for both timing and content of the Bill to set up the new department – thereby helping to

¹ The Review of the Revenue Departments ('the review'), Gus O'Donnell, HM Treasury, March 2004

² See also the review of criminal investigations and prosecutions conducted by HM Customs and Excise by the Hon Mr Justice Butterfield at:
http://www.hm-treasury.gov.uk/newsroom_and_speeches/speeches/statement/butterfield03_report_index.cfm

deliver the benefits of the changes recommended by the review. At Part III it also appraises the proposal to create RCPO.

6. This RIA does not look back at the various policy options considered in depth by the review (see Annex A). However, it does provide more detail about the likely costs and benefits of the option adopted.

Details of the establishment of HMRC in the Bill

7. The Commissioners for Revenue and Customs (CRC) Bill establishes a non-Ministerial government department to administer taxes, duties, national insurance contributions, tax credits, child benefit, collection of student loans, frontier and social protection functions, and other matters currently the responsibility of the Commissioners of Inland Revenue and the Commissioners of Customs and Excise.

8. This will include:

- the appointment of Commissioners for the new department, and their officers;
- the transfer of the functions, property, rights and liabilities of the Commissioners of Inland Revenue and the Commissioners of Customs and Excise to the Commissioners of the new department; and
- the Ministerial oversight, governance and financing of the new department.

9. It enables the new department to operate effectively and efficiently from the date of establishment by ensuring:

- that information can be pooled within the new department;
- that existing gateways to exchange information between the new department and others are continued;
- that the confidentiality of information held by the new department is safeguarded to no lesser extent than currently for the predecessor departments; and
- that some provisions are replaced where they currently apply in a different way to the Inland Revenue and HM Customs & Excise (for example in relation to offences against officers).

10. It transfers the information and enforcement powers of the two departments to HMRC; but it ring fences them so that they may only be used in respect of the functions of the specific predecessor department e.g. an officer of Revenue and Customs will be able to exercise the previous Customs and Excise power to enter premises to check records, but only in respect of functions, such as VAT, which were previously vested in HM Customs and Excise.

11. The Bill also sets out arrangements for external scrutiny of aspects of HMRC's functions (primarily related to their criminal investigations), as recommended by the Hon. Mr Justice Butterfield's report (for more details of this report, see Part III).

12. The Bill extends to the United Kingdom, except where otherwise stated.

Top-line options for the Commissioners for Revenue and Customs Bill

13. As described in paragraph 2 above, the O'Donnell Review considered both a *status quo* plus option, and a non-legislative option for integrating the two departments (strategic alignment). Chapter 3 of the Review sets out in detail the benefits and risks of these options and why they were rejected. In short, the benefits to customer service, and increased effectiveness and efficiency identified by the Review depended upon dealing with shared customers in an integrated way.

14. The *status quo* plus option, while having the benefit of minimising the risks associated with change, could not deliver integrated working. The extent to which integration could be delivered through strategic alignment was uncertain and it was felt that the roles of Ministers, the strategic board and the management of the revenue departments would be difficult to set out clearly. Thus the clearer lines of accountability identified by the Review as a key criterion for success would not be achieved.

15. The options considered in this RIA therefore all relate to the legislative approach to implementing the integration of the Revenue and Customs. They included:

- i. a short early Bill, which contains those provisions that are essential to create HMRC and permit it to function effectively. This could mean that further legislation might be required at a later date to make any more substantive changes that might be needed to reap the full benefits;
- ii. a more comprehensive early Bill, which contains all the essential content of **option (i)** above, but also makes more substantive changes in areas such as the powers vested in officers to carry out their functions, or to the mechanics of some business processes (where underpinned by legislation) to facilitate more areas of joint working across indirect and direct taxation; or
- iii. a fully comprehensive Bill in a later legislative session following detailed analysis of the most appropriate strategy for the new department and assessment of the legislative changes needed to underpin that strategy.

Benefits and risks of options for legislation

Option (i)

16. The key benefit of this option is that it enables the new department to be established quickly, allowing work to begin early on what are likely to be major organisational and administrative changes, in order to deliver the benefits of integration. It would allow the new department to come into existence around a year or so after the announcement of the intention to integrate. In addition, by focussing the legislative changes on those essential for the new departments effectiveness, it reduces the risk to business as usual which could arise under **option (ii)**.

17. The main risk is that a short Bill might not provide sufficient legislative scope to enable the full benefits of integration to be realised and that further legislation would be required.

Option (ii)

18. A more comprehensive Bill, in the same parliamentary session as at **option (i)**, would have the benefit of enabling more significant change from the outset. However it would take longer to prepare and be likely to require a greater amount of parliamentary time, so early implementation of the new department would not be possible. Most significantly it would not allow sufficient time for the new department and its management to consider what operational and other changes should be made, over what timescale, and in what order of priority.

19. Business as usual might also be adversely affected due to pressure to deliver significant changes to a very tight timescale. The Treasury Select Committee warned that Ministers and senior management must consider potential risks to business as usual in establishing the integrated department, noting that:

“We consider that tax collection and customer service must remain the departments’ first priority during the merger process.”³

Option (iii)

20. Legislating for the new department in a later session would have the advantages of allowing time to develop a significant package of changes, with consultation where appropriate. But the costs of such a delay would be significant. Only very limited expenditure on planning for legislative change is possible under parliamentary rules. It is estimated that implementation of the new department would be delayed by at least a year compared to **option (i)** and that this would reduce the planned efficiency savings and additional revenue generated by more effective working by around half for each year’s delay.

Preferred option for legislation

21. The Commissioners for Revenue and Customs (CRC) Bill is based on **option (i)**. Neither **option (ii)** nor **option (iii)** were considered to strike the right balance between making an early start on delivering the benefits of integration and the need for a sensible timetable for the development of (and discussion of) detailed plans for change.

Overview of the impact of the Bill on enactment

22. The following sections consider the overall impacts of integrating the Inland Revenue and Customs and Excise in more detail.

³ House of Commons Treasury Committee: *The Merger of Customs & Excise and the Inland Revenue*, 9th Report of Session 2003-04 (Paragraph 31)

PART II – Costs and benefits of integration

RISKS:

23. The review recognised that integration carried risks in terms of maintaining “business as usual” during the transition to the new department. However it assessed that strong management should mitigate any potential risks, with a focus on priority areas (much of the business would not be directly affected by the creation of a new department), and with clear focus on delivery as the core business of the department, to ensure existing priorities are met and areas for change are identified.

24. The need to ensure that business as usual is maintained has also been stressed by the Treasury Select Committee⁴. David Varney, the Chairman of the revenue departments (and Chairman designate HMRC), told the Committee that ensuring tax gathering and service to the public was maintained was:

“very much the focus of our attention and that will be in our [Public Service Agreement] PSA targets and it is in the objectives we are trying to drive through.”⁵

25. **Option (i)** reduces the risk to business as usual compared to rushing forward wholesale changes.

BENEFITS:

Economic

26. The integration of the two departments will contribute significantly towards achieving **efficiency savings**, thereby reducing the cost to Government of administering taxation regimes. As part of the departmental response to the Efficiency Review, plans are in place to achieve gross savings of 12,800 full time equivalent (FTE) posts by March 2008, against a baseline of around 98,000. In addition to these, approximately 3,200 (FTE) savings are to be achieved as a result of the integration of HM Customs & Excise and Inland Revenue⁶.

27. It will also help reduce **compliance costs for customers**, and improve **customer services**. In particular, *in the longer term*, developments such as improved use of information within the new department will offer opportunities to reduce the costs for businesses, charities and voluntary organisations of providing such information. As businesses are often currently customers of both departments, they potentially have most to gain in terms of reduced compliance costs from a more joined-up approach.

28. It will also help improve **compliance**. While this is an area where it is often very difficult to quantify benefits, there is good evidence⁷ from other countries that have undergone integration exercises that revenue increases as compliance costs fall (e.g. Canada and Denmark have integrated their direct and indirect tax

⁴ House of Commons Treasury Committee: *The Merger of Customs & Excise and the Inland Revenue*, 9th Report of Session 2003-04 (Paragraph 31)

⁵ Ibid. paragraph 25.

⁶ Efficiency Technical Note http://www.inlandrevenue.gov.uk/psa/hmrc_etn.pdf

⁷ the Revenue departments. Cited in *the Review of the Revenue Departments*, paragraph 1.23, p 8, March 2004.

administrations in recent years and officials in the integrated tax administrations assess that revenue has increased as a result of merger, including in the short term).

29. This is further supported by some useful pilot studies. For example, Large Business Joint Team trials⁸ have been one of the priority areas being piloted under the existing closer working arrangements between the revenue departments. These trials aim to reduce compliance costs, improve compliance, and contribute to the development of tax policy and legislation relating to large businesses. They began on 1st April 2001, and cover fourteen large business groups in the finance, telecommunications, pharmaceuticals and food retailing sectors participating voluntarily. The trials led to improvements for customers and the departments, and helped inform future work on possible areas where an integrated department should consider compliance costs.

30. Overall, over £11m additional revenue was raised in the first two years of these trials, and the staff concerned believe that significant additional revenue would be collected in the longer term as a result of issues identified during the trials. For example, the systematic comparison of information from a variety of sources will assist the department progressively to improve the quality and focus of its checking, providing a rational basis for the targeting of scarce public resources according to the risks of non-compliance.

Environmental

31. There are no major environmental benefits from the CRC Bill.

Social

32. The effect of establishing a new integrated department will be to enable over time the joining up of services to shared customers – particularly businesses (and charities and the voluntary sector in so far as they currently deal with Inland Revenue and Customs and Excise). This will make it easier for customers of the new department to comply with their obligations. Some customers are not “shared” between the two departments (e.g. Tax Credit claimants). The improved customer focus of the integrated department will benefit them too, as will the commitment to maintain business as usual during the transition period.

Issues of equity and fairness

33. A single integrated department will facilitate greater alignment of strategies, a coherent approach to information, and more flexible resource allocation. It will therefore contribute to helping ensure that the right tax is paid by the right people at the right time, which is fairer to compliant taxpayers and helps further protect revenue collection. The following examples illustrate the benefits that have been derived from this approach in specific circumstances. The Bill will enable such activities on a more widespread basis. They include:

- improved tackling of businesses operating in the shadow economy though better sharing of information and working together;

⁸ the Revenue Departments. Cited in *the Review of the Revenue Departments*, Box 3.3, p 45, March 2004.

- a success rate of over 75 per cent in a 2003 pilot exercise using Revenue systems for tracing ‘missing’ Customs debtors. As the Revenue administers more taxes, it often contacts customers more frequently than Customs and holds more up-to-date details. The 75 per cent rate compares to 25-30 per cent on Customs’ own systems in one region, and around 30 per cent from using a commercial tracing agency⁹; and
- the Revenue becoming aware of undesirable avoidance schemes in Corporation Tax, alerted by information from Customs which had been previously obtained for VAT purposes, at least two years earlier than under normal procedures¹⁰. As VAT returns are rendered quarterly (for the most part), potential non-compliance can be identified by Customs often sooner than by the Revenue, who for example receive Corporation Tax returns some time after the end of the accounting period. A project has now been established on avoidance to allow more systematic measurement of benefits and incorporation into business as usual¹¹.

34. In addition to this, in reporting to the Treasury Committee¹², the Chairman of the Revenue Departments, David Varney, explained when asked when customers would start to see the benefits of merger that:

“One of the things we have done is put together the large business organisation and the large business group, respectively the Inland Revenue and Customs & Excise, into a large business system to create one interface with the larger businesses.”

COSTS:

Economic

35. For the majority of business who seek to comply and see their dealings with the two Revenue Departments in a more holistic way, having a single integrated department to deal with in the future will reduce regulatory burdens. On the other hand, improved enforcement of compliance with tax law could well be expected to increase burdens on non-compliant businesses.

36. In the short term any changes in business processes, powers etc., while potentially benefiting customers in the longer term, may lead to costs for professional advisers and employers to develop new systems and understand the changes. Discussions with stakeholders would be necessary in order to assess the merits of changes, offset against set-up costs. The current Bill does not include any provisions to make material changes to statute governing the administration of tax regimes, in advance of such discussions.

Costs of integrating Inland Revenue and HM Customs and Excise

37. The known costs that arise directly from the creation of HM Revenue and Customs are anticipated to be of the order of £75million over 2004/05 and 2005/06,

⁹ the Revenue Departments. Cited in *the Review of the Revenue Departments*, paragraph 4.12, p 73, March 2004

¹⁰ Finance Act 2004 contains a requirement on businesses to disclose avoidance schemes to Inland Revenue – which will consequently make this only partly a direct result of integration.

¹¹ the Revenue Departments. Cited in *the Review of the Revenue Departments*, paragraph 4.12, p 73, March 2004

¹² House of Commons Treasury Committee: *The Merger of Customs & Excise and the Inland Revenue*, 9th Report of Session 2003-04 (Q205)

including the preparatory costs of alignment of basic services, such as work to put the future IT desktop requirements of the departments on a common platform. Further costs from integration may arise in due course, for example, from changes to join up some of the services the two departments currently provide to business customers independently. These cannot be quantified until the associated policies have been agreed.

Environmental

38. There are no major environmental costs arising from the CRC Bill.

39. Short-term environmental costs are expected to be minimal, given that replacement of office stationery and forms will be carried out over time, according to natural lifecycle and update plans. This approach will also allow the new department to minimise financial costs.

Social

40. Short-term social costs could include human resource issues for Civil Servants involved in the process of the re-organisation which will follow from the integration of the two departments

Consultation

41. The Review of the Revenue Departments consulted a number of interested bodies and individuals in the course of its work, and invited three external experts to review its findings informally prior to publication. After publication, comments were also invited generally. Since then, the Treasury has undertaken an extensive programme of informal consultation to obtain views from business, representative bodies, and trade associations upon the findings of the Review and the legislative approach to implementing its recommendations. **Annex B** contains more information about this programme, plus the findings of the informal consultation exercise.

42. In summary, those consulted were supportive of the proposal to create HMRC and saw the potential benefits, particularly in terms of improved customer service. They were in favour of carefully managed change to ensure business as usual was maintained, and this has been taken into account in the recommendation to introduce an early short bill which did not make more fundamental changes at this stage.

ASSESSMENTS:

Small Firms' Impact Test:

41. The Small Business Service has agreed that evidence drawn from consultations on the Bill, and from a business forum convened specifically to discuss the implications of the proposal, reveal that the Bill will not result in any significant impacts on small businesses. As a result of the analysis and findings from these initial soundings, conducted for the purposes of the Stage 1 Impact Test, there appear to be no small business concerns in relation to the Bill and, as a consequence, the Small Business Service has agreed that a Stage 2 Impact Test is not required.

42. The key messages that emerged from the consultation discussions and business forum were:

- integration is generally welcomed by small firms, who see the formation of HMRC as an opportunity to improve the services provided to small businesses;
- small businesses generally welcomed the approach within the Bill of maintaining the *status quo* pending longer term work to consider more substantive changes to tax regimes. They were keen that work on integration should not disrupt the service provided to them in the meantime, and welcomed the Government's focus on avoiding this; and
- consultees were of the view that, while future more substantive change would deliver welcome benefits, the approach adopted in the CRC Bill means that it will not have a significant immediate impact upon them.

43. Consultees had a variety of views regarding the optimal approach to future integration. Small businesses would welcome the joining up of services, and expressed particular enthusiasm for single points of contact for all queries concerning their business, and integrated debt management activities. While recognising that benefits such as these could take time to emerge, representatives considered that changes of this nature could deliver real improvements to the service they receive.

44. Research shows that the majority of small businesses most value stability in the tax system, certainty that they have complied with the rules, minimum possible contact with the revenue departments and as little disturbance as possible in discharging their obligations. The structures of those organisations dealing with direct and indirect taxes impact on small businesses only in so much as they affect their experiences in these aspects.

45. There will be future policy change proposals under the new department. These will be subject to the usual round of consultation and regulatory impact assessment as appropriate.

Competition Assessment

46. There are no competition implications arising from the Bill. The Bill applies to every sector and to all firms equally.

ENFORCEMENT AND SANCTIONS:

How will the proposal be enforced?

- 47.** The changes introduced by the HMRC Bill are broadly machinery of government changes, and do not therefore require enforcement.
- 48.** The new department will, however, continue to employ the tools and sanctions employed by its predecessor departments in order to enforce compliance with the legal requirements set out in respect of each of the functions for which it is responsible. It includes some alignment to provisions on offences (see below), but does not materially alter the enforcement provisions of the predecessor departments.
- 49.** The impact of the departmental integration on the proposed Revenue and Customs Prosecution Office (RCPO) is included as Part III.

Who will enforce this legislation?

- 50.** Not applicable to the machinery of government change.

Will the legislation impose criminal sanctions for non-compliance?

- 51.** As indicated, most of the Bill is concerned with machinery of government changes within government itself, and non-compliance is not in question. As part of the establishment of the new department, certain provisions such as offences of assaulting, obstructing or impersonating officers are being made uniform, and the criminal penalties already applying for these offences are being aligned on those applying in relation to the police in England and Wales. Provision is also being made to ensure that the existing criminal penalties for unlawful disclosure of taxpayer and other customer information (under section 182 Finance Act 1989) are applied uniformly to all aspects of the new department's work, and cover all those working as Commissioners, officers and contractors of the new department.
- 52.** The Bill also leaves unchanged the civil and criminal sanctions which applied to each of the tax and other functions of the existing departments, now that they are to be administered by the new department.

MONITORING AND REVIEW:

- 53.** Like its predecessor departments the new department established by the legislation will be a non-Ministerial government department run by Commissioners appointed by letters patent with the same basic accountabilities to Ministers, to Parliament and to the public.
- 54.** In common with other government departments, the department will agree with the Treasury as part of the Spending Review process a delivery plan setting out how it proposes to achieve its objectives and targets. The plan will identify the main management and other risks to the effective operation of the department or

successful delivery of its objectives, and the main systems and controls designed to deal with those risks.

55. The department will provide the Treasury with regular reports on the ongoing business of the department, including information on the financial position, progress against targets and efficiency measures. The reports should be derived from the department's internal management systems, and the precise coverage and frequency of reports will be agreed from time to time.

56. The department will publish its performance targets and achievements in keeping with general Treasury and parliamentary requirements (currently in the Spring Report and the Annual Report in the autumn).

57. The efficiency and effectiveness of the department will be subject to monitoring by the National Audit Office, just as the predecessor departments are.

PART III –Revenue and Customs Prosecution Office (RCPO).

58. The CRC Bill also provides for the establishment of an independent prosecution office to undertake prosecutions on behalf of the new department.

Background

59. The Customs and Excise Prosecutions Office (CEPO) was created in April 2003. Following specific recommendations made in the Hon Mr Justice Butterfield's Review¹³, Ministers announced that they accepted the recommendations and that CEPO would be put on a statutory footing.

60. The Butterfield review's proposals were discussed widely throughout the Criminal Justice System and with other interested representative bodies before coming to its conclusion.

61. An independent prosecutions function has been operating under a Memorandum of Understanding between the Attorney General, Customs and Excise and HM Treasury since January 2003 and has in that time begun 2695 prosecutions, including a number of cases with multiple defendants.

62. The decision to integrate Inland Revenue with Customs raised the further question of whether the new prosecutions office should also conduct prosecutions currently the responsibility of Inland Revenue.

63. This Regulatory Impact Assessment examines the options that were considered to put the prosecutions office on a statutory footing.

Options

64. It was not considered an option to leave CEPO indefinitely without a statutory basis. Ministers therefore considered three options:

- that HMRC would be responsible for prosecutions which previously would have been taken by the Board of Inland Revenue, but those which would have been taken by Customs and Excise would continue to be prosecuted by an independent CEPO. It was decided that this would have been wholly inconsistent with the principles of integrating the two Revenue Departments. And there would have been real practical difficulties in putting forward to two different prosecution bodies a case involving, say, a mixed Corporation Tax and VAT fraud;
- all prosecutions would be carried out by HMRC. But this would represent a reversal of the Government's acceptance of the Butterfield Report that a wholly independent prosecuting body was required; or
- all prosecutions would be carried out by the independent successor to CEPO, including those which were currently taken by the Board of Inland Revenue. This option had the advantages of being congruent with the merger of the Revenue Departments and with the Butterfield Review.

¹³ *The Review of Criminal Prosecutions Conducted by HM Customs and Excise* (15 July 2003)

However it meant that the Inland Revenue's prosecution function would be lost.

65. Ministers considered that, with the integration of Revenue and Customs into one department, it would be logical to take the third approach, and that the office should be called the *Revenue and Customs Prosecutions Office (RCPO)*.

Impact of the establishment of Revenue and Customs Prosecutions Office (RCPO)

65. The transition costs to Inland Revenue of integrating the Crime Group (IR prosecutions group) within RCPO are estimated to be around £240,000.

66. Transition costs aside, it is assessed that the impact of this aspect of the Bill will be broadly neutral. The service provided to investigating officers and administrators, as well as to others within the criminal justice service, will not, in practical terms, change at all. However, the enhanced protection for taxpayers provided by the new prosecutions office is arguably a social benefit, in that it should have a positive impact on the prosecution of tax and duty evasion.

Inland Revenue prosecution work

67. The inclusion of Inland Revenue's prosecution work within the remit of the Customs and Excise Prosecution Office successor again has a neutral impact. The prosecution work has existed previously and the fact that it will henceforth be carried out by an amalgamated statutory independent body is simply a reflection of the wider process of integration of the two departments.

68. Our reasons for considering the impact to be neutral (or a modest improvement for stakeholders in the prosecution process) are:

- the transfer of responsibility from the Board of Inland Revenue to the successor to the Customs and Excise Prosecution Office for the prosecution of offences previously under the care and management of the Board is essentially a machinery of government issue, resulting from the integration of the Revenue Departments;
- the Customs and Excise Prosecution Office was created to prosecute offences against Customs and Excise in order to demonstrate the clear independence of the prosecutors from the investigators in those cases, so this is about raising standards;
- to the extent that the Customs and Excise Prosecution Office is taking on Customs cases, this is to deliver the benefits identified in the Butterfield Report. To the extent that it is to deliver Inland Revenue cases, this is a process change caused as a result of the integration of the Revenue Departments. The Butterfield recommendations did not apply to Inland Revenue cases, but if there is any impact on the stakeholders in these prosecution cases caused by these changes, then it is even greater clarity that the prosecuting process is indeed independent and objective. This is considered desirable by all parties who have expressed a view.

Summary and recommendation

69. The findings of the Regulatory Impact Assessment are that:

the new department should be established as soon as possible, through an early, short Bill containing the key provisions essential to create it and enable it to be effective. This takes account of the results of the consultation exercise, the Small Firms' Impact Test, the Competitions Filter, and the cost / benefit analysis, which indicated that an integrated revenue department will lead to an overall reduction in compliance costs for customers and will improve compliance generally, so increasing flow of revenues. A short early Bill will enable work on realising these benefits to begin sooner; *and*

the Bill should include clauses which establish the legislative authority for the existing independent prosecuting office for Customs and Excise (CEPO), bringing Inland Revenue prosecutions within its functions, and giving the office a new name, *the Revenue and Customs Prosecutions Office*.

DECLARATION

I have read the Regulatory Impact Assessment and am satisfied that the benefits justify the costs

Signed 

Date 23 November 2004

Dawn Primarolo MP, Paymaster General, HM Treasury

Annex A – The O’Donnell review

1. In July 2003 the Chancellor of the Exchequer announced a major review of the organisations dealing with tax policy and administration: HM Customs and Excise, the Inland Revenue and HM Treasury. The review was led by Gus O’Donnell, Permanent Secretary to the Treasury and reported alongside the Budget statement of 17 March 2004.

Remit of the review

2. The review’s remit was to examine the best organisational arrangements for achieving the Government’s tax objectives. In meeting its remit, the Review of the Revenue Departments considered issues including:

- ways to improve the arrangements for tax administration¹⁴. Customs and the Revenue provide important services for the Government, the public, and businesses, and the money they collect funds public services. The review examined whether closer working between the departments or organisational change could reduce costs to compliant taxpayers and businesses, encourage enterprise, and improve compliance;
- more coherent use of information, to enhance effectiveness and improve customer service;
- the most appropriate structure for providing policy advice to Ministers, currently spread across three departments and mainly based around individual taxes. The remit highlighted that more co-ordinated tax policy advice was desirable; and
- developing a new framework for accountability for those working on tax, to set out more clearly the roles and responsibilities of all those involved. The review’s remit noted that greater clarity would provide better certainty both for officials and Ministers.

3. Four themes from the review are particularly relevant to the CRC Bill:

- creation of a new department, integrating HM Customs and Excise and the Inland Revenue, so as to be best placed to deliver the perceived benefits;
- clearer roles and responsibilities for tax administration within a new accountability framework and annual remit laid down by Ministers;
- transfer of tax policy development to the Treasury, to improve the ability of the Government to respond to modern tax challenges and create a greater delivery focus in the new department; *and*
- the important role of information – better use of information was seen as key to improving customer service, effectiveness and support for policy, taking account of the need to preserve confidentiality and proportionality.

¹⁴ Inland Revenue and HM Customs and Excise between them administer taxes, duties, national insurance contributions, tax credits, child benefit, collection of student loans, frontier and social protection functions, and other matters.

Summary and recommendations of the Review of the Revenue Departments

The review has considered several options for change, as the means of achieving the review's objectives, rather than ends in their own right (and the objectives will in turn contribute to achieving better outcomes, such as funding better health and education for citizens). The analysis is focussed on three leading options:

- *status quo* plus, under which organisational change would be limited to that necessary to implement the recommendations on policy and accountability;
- creating a single new department, which integrates Customs and the Revenue; and
- strategic alignment, under which a strategic board would be formed to promote the long-term alignment of the existing departments.

The review assesses that creating a new department offers benefits greater than the other options, with improvements to:

- customer service and compliance costs, through more coherent tax policies and the provision of a unified tax service for all customers;
- effectiveness, through alignment of strategies, a coherent approach to information, new approaches to audit, and flexible resource allocation. By better ensuring that the right tax is paid by the right taxpayers (or credit received), fairness would also be enhanced; and
- efficiency, through economies of scale, particularly in transactional processes (although benefits to customers and effectiveness are likely to outweigh efficiency gains).

These gains are dependent upon dealing with shared customers – mainly businesses - in an integrated way, and would not be achieved with the *status quo* plus option. Their achievement through strategic alignment would be uncertain; the roles of Ministers, the strategic board and the management of the revenue departments could be difficult to set out clearly, creating accountability difficulties.

All changes involve costs. Given the scale and nature of the departments, there would be significant short-term costs with the creation of a new department. It is also necessary to consider opportunity costs, particularly for the *status quo* plus option, where the value of lost opportunities could be considerable.

Risks are a more significant consideration than direct financial costs. These include risks to 'business as usual' (including revenue collection) and the disruption of projects already planned. However, other countries that have undertaken the integration of direct and indirect tax administrations have found that revenue has increased rather than fallen as a result of integration, including in the short term. The review assesses that the potential risks can be mitigated by strong management and good planning, and are outweighed by the potential long-term benefits of integration.

(continued below)

Summary and recommendations (continued)

The review therefore recommends that:

- a new single revenue department should be established, integrating Customs and the Revenue.

The details of the implementation of this recommendation will be a matter for the management of the new department, but subject to this, the management should:

- create a new culture and identity for the department, building on the cultures of Customs and the Revenue;
- expand career opportunities for staff, developing strong career paths to provide experience across the new department, with frequent interchange between the new department and the Treasury;
- structure the new department as far as possible around customers and functions rather than taxes, so that customer needs can be better met and compliance improved, for example by establishing an integrated large business office, and more specialised service to small businesses;
- develop a better focussed PSA target on customer service and compliance costs for the 2004 Spending Review, supported by work to develop understanding of compliance costs;
- develop a better focussed PSA target on compliance across the tax system for the 2004 Spending Review, supported by work to develop understanding of the tax gap and other compliance measures;
- generate significant cost savings through improved efficiency, in line with the proposals of this review and that of Sir Peter Gershon; and
- look to identify economies of scale and scope by developing new national services, and reviewing the local office network, including with other departments.

Annex B

Commissioners for Revenue and Customs Bill

Outcomes of informal consultation

The purpose of this Annex is to summarise the outcomes of the informal consultation exercise conducted in respect of the Commissioners for Revenue and Customs Bill.

The Bill implements the principal recommendation of the “*Review of the Revenue Departments*”¹⁵, which was to integrate the Inland Revenue and HM Customs and Excise to form a single new department, to be named HM Revenue and Customs (HMRC). For further information about the Bill, please see the Bill and its accompanying Explanatory Notes.

Consultation process

The “*Review of the Revenue Departments*” obtained the views of a number of senior figures within business prior to reporting its findings. Views were also invited from any interested parties upon the findings of the review when it reported. So there have been ample opportunities for stakeholders to comment upon the principle of forming the new department – we have therefore focussed this latest round of consultation primarily upon the *implementation* of this recommendation, although there has still been some discussion around the principles of integration. We have adopted an informal approach to consultation as the most appropriate method of obtaining stakeholders’ views on what will be a largely machinery of government Bill that – beyond introducing changes to departmental structures – has sought to maintain the status quo in terms of administration of regimes wherever possible. The approach adopted here has been effective in gaining engagement with a comprehensive range of key stakeholders. Any future further proposals for more substantive change will be subject to consultation with stakeholders where appropriate.

HM Treasury, working closely with the Inland Revenue and HM Customs & Excise, conducted an extensive programme of informal consultation between early July and mid-October. This programme was designed to engage with a broad range of HMRC stakeholders, in order to ensure that responses reflected the needs of all HMRC customers. Consultation was principally conducted with the standing consultative groups operated by the Inland Revenue and HM Customs & Excise, which cover most aspects of HMRC’s work and which involve a wide range of both customers and external representative bodies. In addition to consulting these standing groups, a meeting was convened with representatives of small businesses to ensure that this important sector, upon whom research has shown that the burden of compliance can fall disproportionately, was given a genuine opportunity to comment upon the proposals for the Bill. Finally, a number of meetings have taken place with individual representative bodies to explore in detail the issues that they have raised. A full list of the standing groups consulted is at List 1, while the

¹⁵ See “*Review of the Revenue Departments*” published March 2003, available at <http://www.hm-treasury.gov.uk>

names of organisations represented in these groups and other elements of the consultation process are at List 2.

During this exercise, officials have attended 16 meetings of Revenue and Customs standing consultative groups, and convened 6 special meetings or bilaterals. Over 100 representative bodies, trade associations, and individual businesses have attended these meetings, while many more have been given the opportunity to comment through invitations to meetings or correspondence. We have received 2 written representations concerning the Bill, while a further 2 Budget representations have incorporated material relating to the formation of HMRC and have therefore been considered during this consultation process.

In addition to the consultation undertaken by HM Treasury, the Attorney General will speak with legal specialists in relation to the formation of the new Revenue and Customs Prosecutions Office (RCPO), which will be under the jurisdiction of the Attorney. This process involves informal consultation with key figures and organisations in the legal sphere, to ensure that all of the practical considerations attaching to the establishment of RCPO are identified and discussed.

The outcomes of consultation have been used to inform the policy development process, and the development of the Bill's Regulatory Impact Assessment.

Overview

Consultees have been very supportive of the proposal to create HM Revenue and Customs, and in welcoming the change have commented upon the potential for delivering improvements to customer service that this could represent. Some reservations were expressed by consultees involved in international trade, who were concerned that Customs' work on trade facilitation did not fit comfortably within HMRC and might be overshadowed by larger areas of tax collection work within the department, however this sector also saw the potential benefits that could arise for them from the scope for HMRC to deliver enhanced risk assessment processes.

All but one consultee have voiced support for a carefully managed, incremental approach to integration, even if this meant that some customer service improvements could only be achieved through future legislation. A short Bill that creates the new department but avoids making more substantive changes has therefore been welcomed as a sensible first step in this process. The only dissenting voice pressed for avoiding any change until the IT had been developed to allow fully integrated working across a broad range of issues from the outset. Many consultees commented upon the importance of maintaining business as usual throughout the transition process to avoid impacting upon current service levels, and have welcomed the commitment of Ministers and the future management of HMRC to this goal.

Detailed discussion at consultation meetings has largely fallen into two categories – those issues that are directly concerned with the HMRC Bill, and those that relate to broader transition matters, as explained below.

Bill issues

Issue	Points made by consultees	Discussion
HMRC powers – general approach	<p>There was widespread recognition among consultees of the good sense of ring-fencing existing powers within the HMRC Bill to maintain their current scope and effect, and achieve early legislation. A longer term programme of work could then focus on identifying any more substantive changes that would be required, working with business and its representatives. Consultees were supportive of future changes to powers in order to enable effective integrated working across HMRC functions where that would improve the service that they received, and welcomed the prospect of inputting their thinking to inform this work.</p>	<p>We note the support for the approach taken in this Bill of maintaining existing powers to enable HMRC to operate effectively while avoiding substantive change at this stage.</p> <p>However, we also agree with consultees that future changes to powers may be desirable to facilitate integrated working and to drive out the resultant benefits for customers. We are considering options for reform in all areas as part of a longer term programme of work.</p>
HMRC powers – ensuring appropriate use of powers	<p>Consultees expressed concerns around the appropriate use of powers within HMRC pending any future changes. Consultees recognised that different powers attach to different HMRC functions, and observed that a power should only be used in respect of the function for which it is bestowed. Consultees were keen to ensure that the ability to pool information within HMRC should not result in information being sought using, for example, VAT powers, that was in reality desired for corporation tax purposes. Consultees noted the importance of ensuring that both HMRC officers and the public were well informed about what powers could and could not be used for within the new department.</p>	<p>We recognise concerns in this area, but consider that sufficient legal protections exist, both within the HMRC Bill and elsewhere, to prevent inappropriate use of powers in this way. Powers must always be exercised appropriately, proportionately and for the purpose for which they are given. The Government is committed to ensuring that powers are exercised in an appropriate and proportionate manner.</p>

Customer confidentiality	<p>Many consultees – particularly large corporates – emphasised the importance of protecting customer confidentiality. Particular interest was expressed in ensuring that the new allocation of policy responsibilities to HM Treasury should not result in confidential information about individual customers being passed to Treasury officials or Ministers.</p>	<p>The Government recognises and remains committed to maintaining confidentiality for taxpayers’ and other HMRC customers’ affairs. To that end, the Bill contains a statutory duty for all HMRC officers to keep all information that they acquire in the course of their duties confidential unless there is a lawful authority permitting the disclosure of information. And the Bill also makes provision for a criminal offence of unlawful disclosure of confidential information about a customer’s affairs by a HMRC officer.</p> <p>The Government restates its commitment to ensuring that confidential information about taxpayers will not be passed to the Treasury. The Treasury can and does fulfil its policy functions without recourse to such information. The Government also restates its commitment to maintaining the existing convention that Ministers do not intervene in individual cases – the administration of cases is a matter for HMRC and not for the Treasury.</p>
Information pooling within HMRC	<p>Consultees commented that pooling of information within HMRC is a logical position to deliver integrated working (and is not particularly different from the information sharing arrangements currently available between Customs and the Revenue). Consultees recognised the potential for delivering improvements to compliance risk assessment processes through better use of information. One small business representative expressed concerns that a dispute with one part of HMRC should not result in heavy handed treatment for the customer at the hands of</p>	<p>We have noted consultees’ comments in favour of continued internal information pooling.</p>

	another part of HMRC.	
Prosecutions	<p>Consultees universally welcomed the creation of an independent prosecutions office with a remit extending across the full range of HMRC functions. Consultees welcomed the additional level of scrutiny that would be brought to bear on criminal prosecution cases by the office.</p> <p>Some consultees commented that alignment of criminal investigation processes across HMRC would be desirable. Several consultees commented that the ‘Hansard’ procedures currently operated by the Inland Revenue operate effectively, and so sought their continuation within HMRC.</p>	<p>We are pleased that consultees supported the establishment of an independent prosecutions office with a remit extending across all HMRC functions.</p> <p>We recognise the potential, as in many other areas of HMRC’s work, for alignment of prosecution policy and process across HMRC. The management of HMRC will be considering potential areas and priorities for reform as part of the longer term programme of integration-related work following the creation of HMRC. Consultation will be undertaken as appropriate as this work develops.</p>

Non-Bill transition issues

In addition to discussion of Bill matters, consultees have discussed a number of broader issues around integration and the challenges and benefits that are likely to emerge from it. These issues include:

- **Efficiency savings** – consultees expressed concerns over the potential for efficiency savings to have a detrimental impact upon service levels. They commented that the burden of administering tax regimes should not be moved away from HMRC and towards business, and that reductions in staff numbers should not result in the loss of HMRC’s most experienced and knowledgeable members of staff. Small business representatives suggested that some small firms lack the technology or expertise required to conduct business with HMRC electronically, and suggested that these firms would therefore not welcome any introduction of mandatory e-filing.
- **Delivering real integration** – consultees commented that integration needed to deliver joined up services rather than stopping at a merged department (some consultees commented that the National Insurance Contributions Office is still perceived in business as removed from the Revenue’s core business despite the fact that the merger of the Contributions Agency happened some years ago). Consultees commented that there are barriers to integration – such as the wide variety of IT in the two departments – and raised fears that these might impede the delivery of integrated services. Consultees were keen that development of joined up services and culture should build upon the best of the two existing departments, and also look for entirely new approaches to issues.
- **Priorities for reform** – consultees offered views on the priorities for delivering integration. Suggestions included integrating debt management

activities to take a whole customer view, rationalising appeal processes, and developing integrated visits and services tailored to the needs of different customer groups.

We recognise the importance of the above points made by consultees. These points have been taken into account throughout the development of the Bill, and will be used to inform developing work on delivery of integration.

Finally, although not directly linked to the formation of HMRC, consultees discussed the new policy arrangements recommended by the “*Review of the Revenue Departments*” and implemented over the course of the summer. Comments included:

- The importance of consultation as an integral part of the policy development process;
- The importance of delivering an effective working partnership between HMRC and the Treasury, in order to present a joined up approach to policy issues and to ensure that policy development reflected operational realities; and
- The importance of ensuring that representative bodies understand the practicalities of the new arrangements and are steered to the appropriate part of each organisation when they have queries.

We recognise that the factors identified by consultees are critical to successful delivery of the new policy arrangements, and – along with the future management of HMRC and the Treasury management – the Government is committed to making a success of those arrangements.

Summary

The Government would like to thank all those individuals and organisations who were represented in the consultation process for their views.

The Commissioners for Revenue and Customs Bill is the first stage in the process of integration. Future proposals for further development will, where appropriate, be accompanied by consultation in the usual manner.

List 1

Standing groups engaged in the consultation process

Inland Revenue consultative groups

Better Regulation Consultative Committee
Business Tax Forum
Business Tax Forum lawyers and accountants sub-group
Corporation Tax Operational Consultative Committee
Employers Umbrella Group
Energy Group Consultation Group
Large Corporates Forum
Occupational Pension Scheme Joint Working Group
Operational Consultative Committee
Receivables Intermediaries Group
Tax Credits Consultation Group
Voluntary and Community Sector Steering Group
Working Together Steering Group

HM Customs & Excise consultative groups

Joint Alcohol, Tobacco and Customs Group
Joint Customs Consultative Committee
Joint VAT Consultative Committee

List 2

Organisations represented during consultation

The organisations listed below are those who have been involved in the consultation exercise. Many of these organisations were represented at several of the consultative meetings and / or participated in bilateral meetings with the Treasury to explore issues they raised in more detail. In these cases, discussion has taken place with a number of people representing the organisation to ensure that all aspects of their interest (such as corporation tax, VAT and personal taxes) have been considered and discussed with the appropriate specialists.

100 Group

Airline Operators Committee Cargo UK (AOCC UK)

Allen & Overy

Ashursts

The Association of Accounting Technicians (AAT)

The Association of British Insurers (ABI)

The Association of British Travel Agents Ltd (ABTA)

The Association of Chartered Certified Accountants (ACCA)

The Association of Consulting Actuaries (ACA)

The Association of Convenience Stores

The Association of International Courier Express Services (AICES)

The Association of Pension Lawyers (APL)

The Association of Remote Gambling Operators

The Association of Taxation Technicians (ATT)

The Automated Customs and International Trade Association (ACITA)

Berwin Leighton Paisner

Betfair

The Betting Exchange Trade Association

Birmingham City Council

Bonded Warehousekeepers Association

Brindex

British American Tobacco

British Amusements Catering Trade Association

British Bankers' Association

British Beer and Pub Association

British Chambers of Commerce

British Chemical Distribution & Traders Association

British Computer Society

British Essence Manufacturers Association

British International Freight Association

British Ports Association

British Retail Consortium

British Telecom

Chamber of Shipping

Charities Tax Reform Group

Chartered Institute of Management Accountants (CIMA)

Chartered Institute of Taxation (CIOT)

Child Poverty Action Group

Citizens Advice Bureaux (CAB)

Clifford Chance

Confederation of British Industry (CBI)

The Council for Ethnic Minority Voluntary Sector Organisations

Customs Air Transport Consultative Group (CATICG)
Customs Practitioners Group (CPG)
EMI Group Plc
Ernst & Young
The Environmental Services Association
Eversheds
Federation of Independent Advice Centres
Federation of Small Businesses (FSB)
Finance and Leasing Association (FLA)
Food and Drink Federation (FDF)
The Forum of Private Business
Freshfields
The Gin and Vodka Association of Great Britain
HHG Plc
HSBC
ICI Plc
Institute of Chartered Accountants in England and Wales (ICAEW)
Institute of Chartered Accountants of Scotland (ICAS)
Institute of Chartered Shipbrokers (ICSB)
Institute of Directors
Institute of Financial Accountants (IFA)
Institute of Indirect Taxation
Institute of Payroll and Pensions Management
KPMG
Law Society of England and Wales
Law Society of Scotland
Linklaters
Local Government Association
Low Income Tax Reform Group
Macfarlanes
The Money Advice Association
The National Association of Cider Makers
The National Association of Pension Funds (NAPF)
The National Association of Welfare Rights Advisers (NAWRA)
National Council for One Parent Families
The National Market Traders Federation
National Pharmaceutical Association
Oil Taxation Action Committee
Payroll Alliance
Pinsents
PriceWaterhouseCoopers
The Princes Trust
Railway Industry
Retail Enterprise Network
Rolls Royce
Royal Bank of Scotland
The Scotch Whisky Association
Scottish Power
Slaughter & May
Small Business Service
The Society of Pension Consultants (SPC)
TaxAid
The Tobacco Manufacturers Association
UBS
UK Oil Industry Taxation Committee

UK Travel Retail Forum
United Kingdom Commercial Aviation Industry Customs Group
United Kingdom Offshore Operators Association
United Kingdom Vineyards Association
United Kingdom Warehousing Association
Unilever Plc
VAT in Industry Group
VAT Practitioners Group
Vodafone
The Wine and Spirit Association of Great Britain and Northern Ireland

