HM Revenue & Customs

Measuring tax gaps 2013 edition

Tax gap estimates for 2011-12

An Official Statistics release 11 October 2013

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This statistical release presents estimates of net tax gaps for 2011-12 and previous years for HMRC administered taxes. It has been produced by Government analysts working within HMRC, in line with the values, principles and protocols set out in the Code of Practice for Official Statistics.

Estimating the scale of, and trends in, net tax gaps is difficult and a relatively untested area of work for governments in the EU and around the world. These are our best estimates based on the information available, but there are many sources of uncertainty and potential error. Most 2011-12 estimates are provisional. Revisions to previous estimates reflect changes to underlying data and our deepening understanding of the tax gap.

The 2011-12 UK tax gap at a glance

What is the tax gap?

The ‘tax gap’ is the difference between the amount of tax that should, in theory, be collected by HMRC, against what is actually collected. See page 6 for a more detailed explanation.

We use it to identify trends in individuals’ and companies’ compliance within the letter and the spirit of the tax law. (The ‘spirit’ of the law refers to our interpretation of what Parliament intended in setting a particular piece of tax legislation).

Why is there a tax gap?

The tax gap reflects tax lost for a variety of reasons, including criminal attacks on the tax system, non-payment, the deliberate (and illegal) concealment of income or assets, the use of schemes designed to avoid payment of tax, error and where taxpayers simply don’t take enough care with their tax returns. Losses can also arise due to different interpretations of the tax effects of complex transactions.

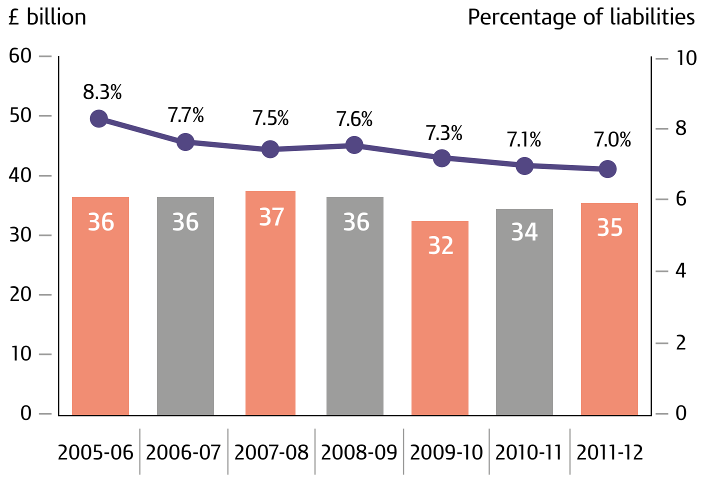
How is it calculated?

The tax gap is an Official Statistic that we compile and update each year. We use a range of internal and external data and different analytical techniques to produce annual estimates, which we revise as more accurate data becomes available.

The tax gap over time

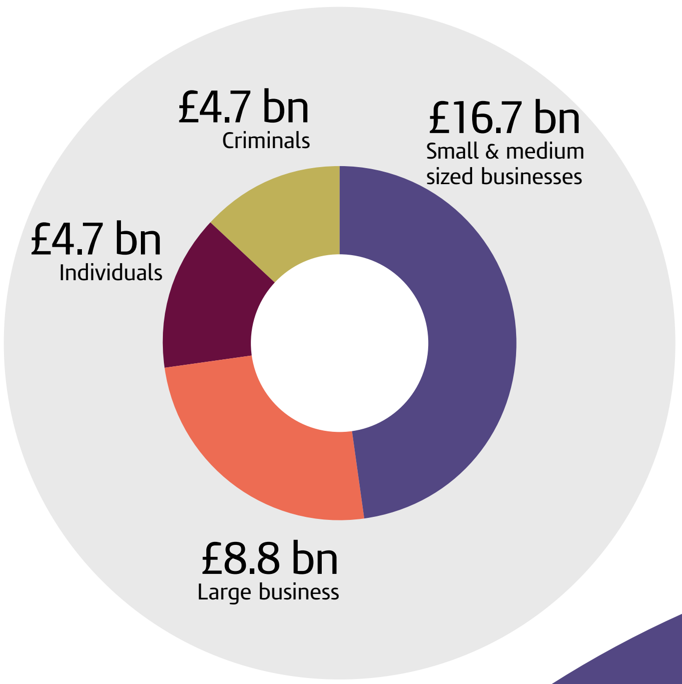
Since 2005-06, the overall trend in the tax gap, as a percentage of total tax liabilities, is down. The latest estimate is £35 billion, or 7.0% of total tax liabilities.

Value of tax gap and percentage of liabilities: 2005-06 to 2011-12

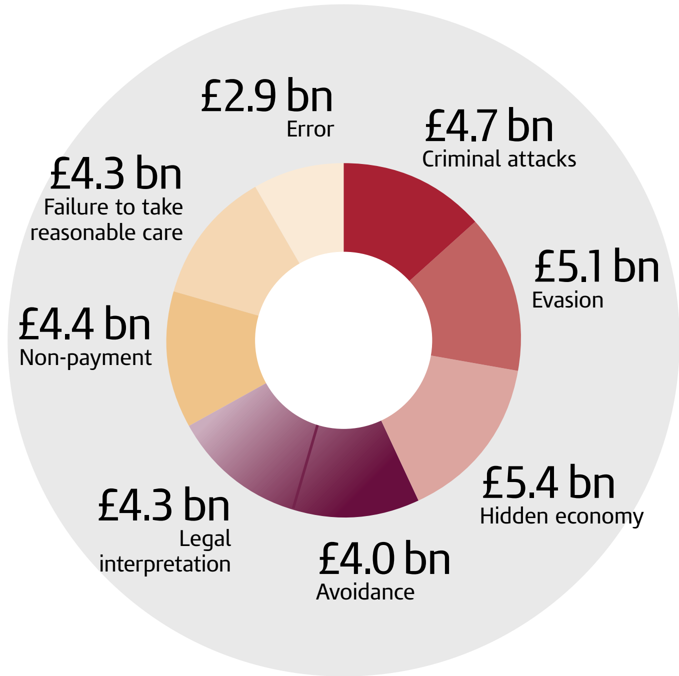


These charts show the £35 billion tax gap by customer group, behaviour and type of tax.

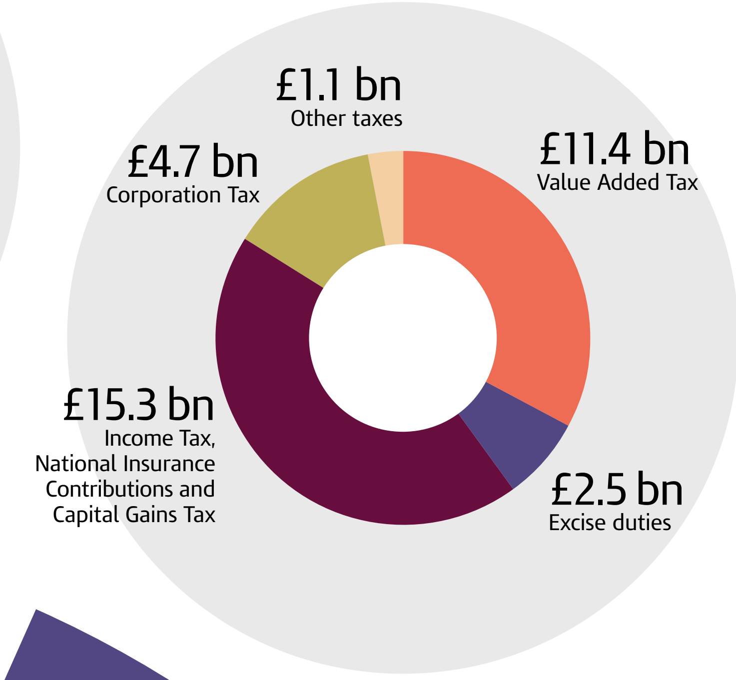
Value of the tax gap by customer group

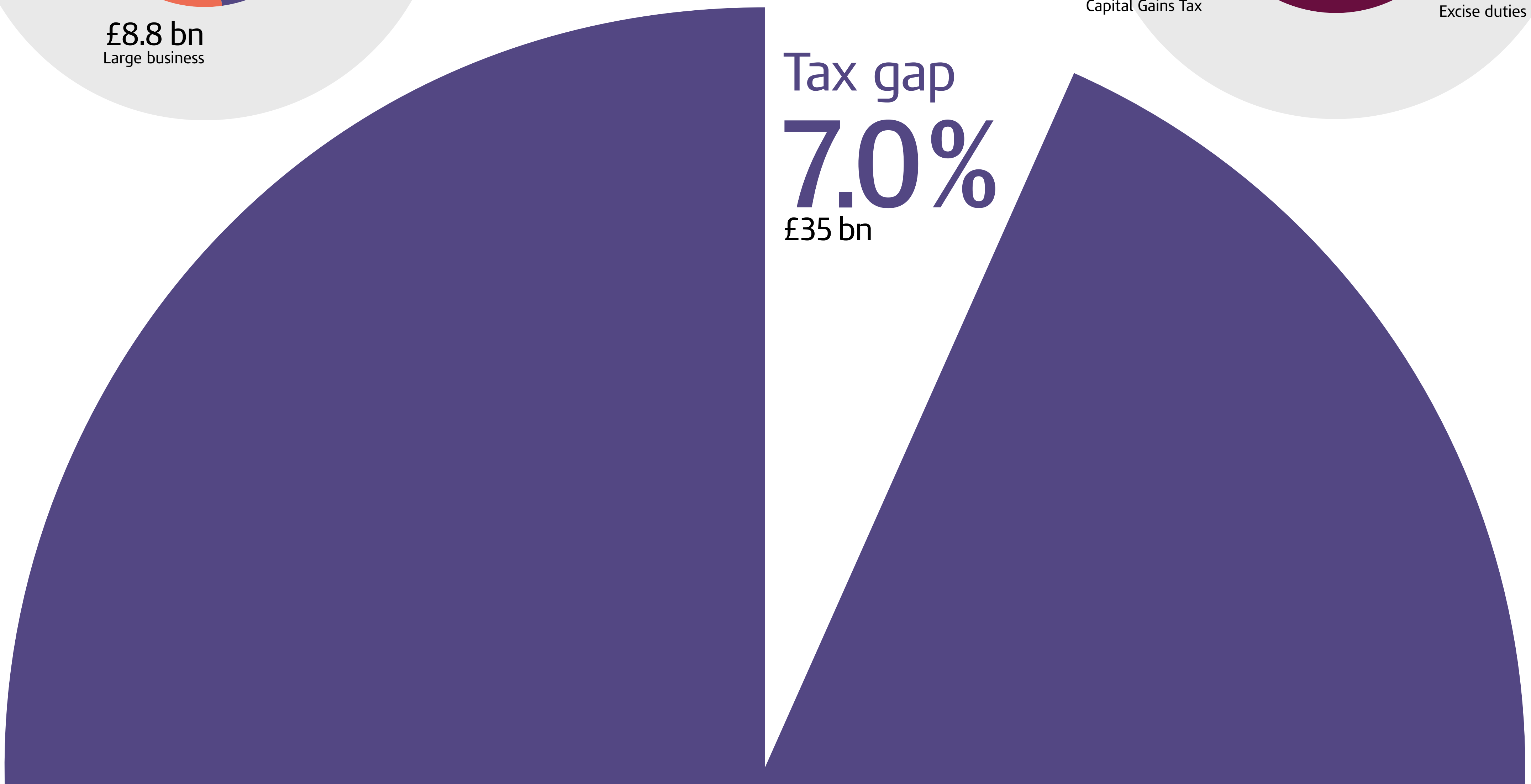


Value of the tax gap by behaviour



Value of the tax gap by type of tax



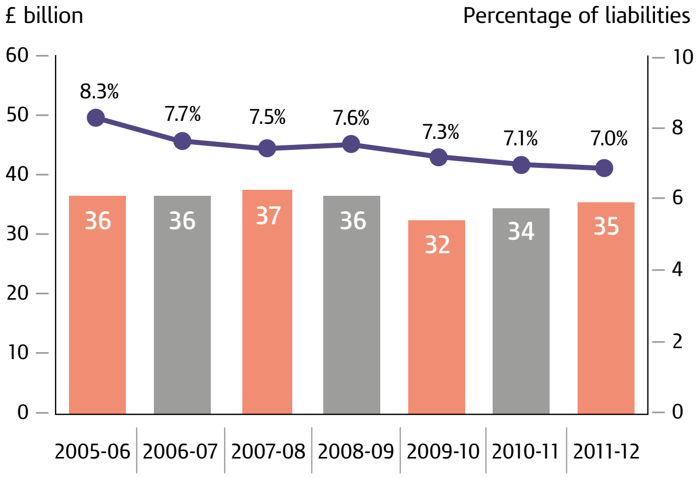


1 – Summary

Key findings

- The tax gap in 2011-12 (the latest year) is estimated to be £35 billion which is 7.0 per cent of tax liabilities.

Figure 1.1 Tax gap and percentage of liabilities: 2005-06 to 2011-12



- The percentage tax gap has reduced steadily from 8.3 per cent in 2005-06 to 7.0 per cent in 2011-12. The current tax gap estimate of £35 billion is £7 billion lower than it would have been if the percentage tax gap had remained at the 2005-06 level of 8.3 per cent.
- The largest reductions over this period have been in the VAT and excise tax gaps.
- When expressed as a percentage of tax liabilities, the tax gap fell slightly from 7.1 per cent to 7.0 per cent between 2010-11 and 2011-12.
- The tax gap has increased between 2010-11 and 2011-12 from £34 billion to £35 billion, which is mainly due to:
  - an increase in the VAT gap of £1.5 billion (see Chapter 2), offset by
  - a reduction in the alcohol tax gap of £0.4 billion (see Chapter 3).
- A large amount of new operational and external data has been received since the tax gap estimates were published in October 2012. As a result, the tax gap in 2010-11 has been revised up from £32 billion to £34 billion, causing the percentage tax gap to increase from 6.7 per cent to 7.1 per cent. The largest changes contributing to the 2010-11 revision are:
  - An increase of £1.6 billion in those components estimated using random enquiry programmes. This is largely a result of having operational data for a later year than was available at the time of the previous publication (Chapter 6 and 7).
  - An increase in the VAT gap of £0.3 billion following changes to the Office for National Statistics (ONS) National Accounts figures on which the calculation is based (Chapter 2).
- The tax gap estimates for years prior to 2010-11 have also been revised, with the largest contributing factor being the revisions to the VAT gap estimates (see Table 1.6)

Definition, scope and measurement

1.1 The tax gap is the difference between tax collected and the tax that should be collected (the theoretical liability). The theoretical liability represents the tax that would be paid if all individuals and companies complied with both the letter of the law and HMRC's interpretation of the intention of Parliament in setting law (referred to as the spirit of the law). The tax gap estimate is net of the Department's compliance activities.

1.2 The total theoretical liability is calculated as the tax gap plus the amount of tax actually received[A].

1.3 An equivalent way of defining the tax gap is the tax that is lost through non-payment, use of avoidance schemes, interpretation of tax effect of complex transactions, error, failure to take reasonable care, evasion, the hidden economy and organised criminal attack.

1.4 Tax gap estimates cover all taxes administered by HMRC, and exclude Council Tax and Business Rates which are administered by local authorities. Estimates exclude the impact of tax credits.

1.5 All of the tax gap estimates shown are subject to error. The main sources of error are random errors due to sampling and systematic errors due to assumptions used to derive the estimates. All methodologies are subject to review which could result in revisions to the published estimates.

1.6 Data up to 2009-10 is more robust than later years, some of which are projected based on historic operational data.

1.7 VAT and excise tax gaps are estimated **top-down**; that is by comparing consumption expenditure data with tax receipts. Most other components are estimated **bottom-up**; that is building up from departmental operational data and management information. A top-down approach has been explored for direct taxes, but concluded that this approach is not feasible[B]. Methodologies and data sources for estimating each tax gap component are set out in the relevant chapters, with additional information in the 'Methodological Annex for Measuring Tax Gaps 2013'.

A HM Revenue and Customs receipts, September 2013 http://www.hmrc.gov.uk/statistics/receipts/receipts-stats.xls

B HMRC, The practicality of a top down approach to the direct tax gap, August 2011 http://www.hmrc.gov.uk/research/taxgap-workingpaper.pdf

All tables in this document are available in Excel.

Tax gap components: 2011-12

1.8 Table 1.1 shows the composition of tax gap estimates for 2011-12. A colour coding system is used in the table to represent the robustness of the estimates.

1.9 The estimates of the excise tax gaps shown in Table 1.1 are for excise duty only. They differ from the excise tax gap estimates in Chapters 3 to 5 which include VAT.

1.10 The percentage tax gap for 2011-12 is 7 per cent of total theoretical liabilities (tax gap plus receipts). This suggests that around 93 per cent of tax due is paid.

Table 1.1: Tax gap estimates 2011-12

Tax	Type	Component	2011-12	
			Percentage tax gap[1]	Point estimate (£ billion)[2,3,4]
Value Added Tax	**Total VAT**		**10.4%**	**11.4**
Excise duties	Tobacco duties	Cigarette duty	7%	0.7
		Hand rolled tobacco duty	35%	0.6
		Total tobacco	**12.0%**	**1.3**
	Alcohol duties	Spirits duty	3%	0.1
		Beer duty	9%	0.4
		Wine duty	6%	0.2
		Total alcohol	**6.6%**	**0.7**
	Hydrocarbon oils duties	Great Britain diesel duty	2%	0.3
		Great Britain petrol duty	N/A	N/A
		Northern Ireland diesel duty	27%	0.1
		Northern Ireland petrol duty	11%	0.03
		Total hydrocarbon oils	**1.5%**	**0.4**
		Other excise duties	5%	0.1
	Total excise duties[5]		**4.9%**	**2.5**
Income Tax, National Insurance Contributions, Capital Gains Tax (IT, NICs, CGT)	Self Assessment	Non-business taxpayers	N/A	0.3
		Business taxpayers	N/A	4.3
		Large partnerships	10%	0.6
		Total Self Assessment	**17.4%**	**5.2**
	PAYE	Small and medium employers	2%	1.7
		Large employers	2%	2.2
		Total PAYE	**1.7%**	**3.8**
	Avoidance	**Total avoidance (IT, NICs, CGT)**	**N/A**	**2.0**
	Hidden economy	PAYE individuals not in self assessment	N/A	1.0
		Ghosts	N/A	1.3
		Moonlighters	N/A	1.9
		Total hidden economy (IT, NICs, CGT)	**N/A**	**4.3**
	Total IT, NICs, CGT		**5.8%**	**15.3**
Corporation Tax		Small and medium businesses	12%	2.3
		Large businesses[6]	8%	2.3
	Total Corporation Tax		**9.6%**	**4.7**
Other direct and indirect taxes	Stamp duties	Stamp Duty Land Tax	3%	0.2
		Stamp Duty Reserve Tax	1%	0.02
		Total stamp duties	**2.5%**	**0.2**
	Other direct taxes	Inheritance tax	12%	0.4
		Petroleum Revenue Tax	2%	0.04
	Other indirect taxes	Environmental taxes, Insurance Premium Tax	4%	0.4
	Total other taxes		**4.2%**	**1.1**
Total tax gap[7]			**7.0%**	**35**

Developing methodology. (Wine duty; Total avoidance (IT, NICs, CGT); Stamp Duty Land Tax)

Experimental methodology, illustrative indicators for gaps with no direct measure. (Other excise duties; Large partnerships; Large employers; Hidden economy rows; Stamp Duty Reserve Tax; Inheritance tax; Petroleum Revenue Tax; Environmental taxes, Insurance Premium Tax)

1 Tax gap as a proportion of theoretical liability which is defined as the tax gap plus the amount of tax actually received. Total percentage tax gap estimates are rounded to the nearest 0.1 per cent with individual estimates rounded to the nearest 1 per cent.
2 The overall tax gap is rounded to the nearest £1 billion. Other estimates are rounded to the nearest £100 million or the nearest £10 million if they are less than £50 million.
3 Estimates cover all sources of revenue loss including non-payment.
4 Refer to chapters for further details on definitions and methodologies.
5 The excise tax gap estimates are for excise duty only and show duty loss as a percentage of revenue due. They therefore differ from estimates in Chapters 3-5 which include VAT and show the illicit market share.
6 The Corporation Tax gap estimate for large businesses is derived from two methodologies. An established methodology exists for businesses managed by the Large Business Service and an illustrative methodology is used for businesses managed by HMRC's Large and Complex unit.
7 HMRC is developing an evidence base of funds held by UK individuals internationally. The methodologies will be reviewed to ensure that they reflect this new data.

Tax gap time series: 2005-06 to 2011-12

1.11 Table 1.2 shows the percentage tax gap since 2005-06 by type of tax. The tax gap as a percentage of tax liabilities gives a better measure of compliance over time because it takes out some of the effects of inflation and changes to tax rates.

1.12 Over this period there has been a steady reduction in the percentage tax gap. The largest reductions over this period have been in the VAT and excise tax gaps.

1.13 Direct tax gap estimates (IT, NICs, CGT and Corporation Tax) are based on operational data for which the latest available year is either 2009-10 or 2010-11. Estimates for years before this point are based on actual data. Estimates of the tax gap for years after this point are projected assuming stable underlying compliance behaviour, with actual data on tax liabilities, non-payment and compliance yield being used.

1.14 A time series of the tax gap components from 2005-06 to 2011-12 is shown in Table 1.3. The tax gap stayed fairly flat between 2005-06 and 2008-09 at around £36 billion, falling back to £32 billion in 2009-10 and rising again in 2010-11 to £34 billion and 2011-12 to £35 billion.

Table 1.2: Tax gap by type of tax: 2005-06 to 2011-12 (percentage tax gap)[1]

Tax	Type	Percentage tax gap						
		2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12
Value Added Tax		**14.4%**	**12.9%**	**11.7%**	**14.2%**	**11.6%**	**10.4%**	**10.4%**
Excise duties	Tobacco duties	N/A	N/A	16.5%	17.1%	16.2%	12.4%	12.0%
	Alcohol duties	N/A	N/A	10.0%	6.4%	6.9%	11.0%	6.6%
	Hydrocarbon oils duties	N/A	N/A	2.8%	3.3%	2.8%	2.0%	1.5%
	Other excise duties	N/A	N/A	7.0%	6.0%	6.0%	6.0%	5.0%
	Total excise duties	**8.0%**	**8.0%**	**7.4%**	**7.2%**	**6.7%**	**6.1%**	**4.9%**
Income Tax, National Insurance Contributions, Capital Gains Tax (IT, NICs, CGT)[2]	Self Assessment	20.3%	19.5%	21.5%	13.7%	18.7%	17.0%	17.4%
	PAYE	1.5%	1.4%	1.5%	1.3%	1.5%	1.7%	1.7%
	Avoidance	N/A	N/A	N/A	N/A	N/A	N/A	N/A
	Hidden economy	N/A	N/A	N/A	N/A	N/A	N/A	N/A
	Total IT, NICs, CGT	**5.4%**	**5.3%**	**5.7%**	**4.7%**	**5.9%**	**5.9%**	**5.8%**
Corporation Tax	Small and medium businesses	13.1%	11.1%	10.9%	11.6%	8.6%	11.9%	11.9%
	Large business	N/A	10.1%	9.0%	9.9%	9.3%	9.0%	8.0%
	Total Corporation Tax	**11.8%**	**10.4%**	**9.6%**	**10.5%**	**9.0%**	**10.1%**	**9.6%**
Other direct and indirect taxes	Stamp duties	N/A	N/A	9.0%	14.9%	2.4%	2.5%	2.5%
	Other taxes[3]	3.2%	3.1%	6.0%	5.3%	6.5%	5.7%	5.2%
	Total other direct and indirect taxes	**7.3%**	**7.5%**	**7.5%**	**9.0%**	**4.9%**	**4.5%**	**4.2%**
Total tax gap		**8.3%**	**7.7%**	**7.5%**	**7.6%**	**7.3%**	**7.1%**	**7.0%**

1 Estimates are rounded to nearest 0.1 per cent.
2 Percentage tax gap estimates for avoidance and the hidden economy are not shown as tax receipts cannot be calculated.
3 'Other taxes' includes Inheritance Tax, Petroleum Revenue Tax, Environmental taxes and Insurance Premium Tax.

Table 1.3: Tax gap by type of tax: 2005-06 to 2011-12

Tax	Type	Point estimates (£ billion)[1]						
		2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12
Value Added Tax	**Total VAT**	**12.3**	**11.5**	**10.8**	**13.2**	**9.4**	**9.9**	**11.4**
Excise duties	Tobacco duties	2.1	2.0	1.6	1.7	1.7	1.3	1.3
	Alcohol duties	0.5	0.6	0.9	0.6	0.6	1.1	0.7
	Hydrocarbon oils duties	0.8	0.8	0.7	0.8	0.8	0.5	0.4
	Other excise duties	0.2	0.2	0.2	0.2	0.2	0.1	0.1
	Total excise duties	**3.5**	**3.6**	**3.4**	**3.3**	**3.3**	**3.1**	**2.5**
Income Tax, National Insurance Contributions, Capital Gains Tax[2]	Self Assessment	5.4	5.9	7.6	4.8	5.6	5.3	5.2
	PAYE	3.1	3.1	3.3	2.8	3.2	3.8	3.8
	Avoidance	N/A	N/A	N/A	N/A	N/A	N/A	2.0
	Hidden economy	N/A	N/A	N/A	N/A	N/A	N/A	4.3
	Total IT, NICs, CGT	**12.5**	**13.1**	**15.3**	**12.3**	**14.8**	**15.3**	**15.3**
Corporation Tax	Small and medium businesses	1.8	1.7	1.7	1.9	1.3	2.0	2.3
	Large businesses	3.7	3.5	3.2	3.2	2.2	2.7	2.3
	Total Corporation Tax	**5.6**	**5.1**	**4.9**	**5.0**	**3.6**	**4.7**	**4.7**
Other direct and indirect taxes	Stamp duties	1.1	1.3	1.4	1.4	0.2	0.2	0.2
	Other taxes[3]	0.8	0.8	0.9	0.8	0.8	0.8	0.8
	Total other direct and indirect taxes	**1.9**	**2.2**	**2.3**	**2.2**	**1.0**	**1.1**	**1.1**
Total tax gap		**36**	**36**	**37**	**36**	**32**	**34**	**35**
Total theoretical tax liabilities		**434**	**459**	**488**	**475**	**441**	**481**	**502**
Total percentage tax gap (%)		**8.3%**	**7.7%**	**7.5%**	**7.6%**	**7.3%**	**7.1%**	**7.0%**

[1] The overall tax gap is rounded to the nearest £1 billion. Other estimates are rounded to the nearest £100 million. Figures may not appear to sum due to rounding.

[2] Tax gap estimates for avoidance and the hidden economy are not shown prior to 2011-12 because the data available does not enable estimates to be updated for earlier years.

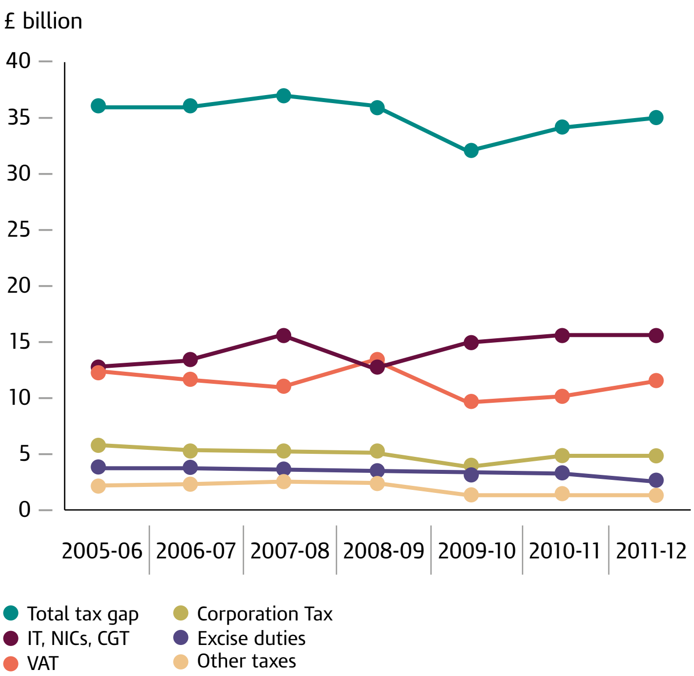
[3] 'Other taxes' includes Inheritance Tax, Petroleum Revenue Tax, Environmental taxes and Insurance Premium Tax.

Estimates for these years are projections and will be revised when operational data becomes available.

Tax gap segmentation

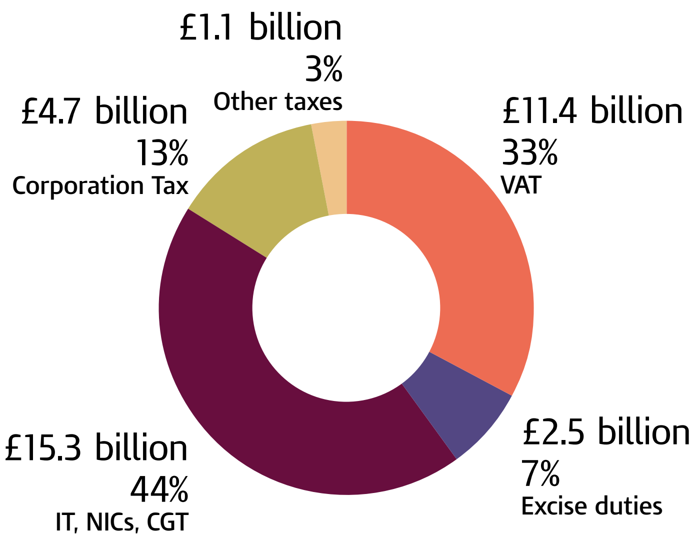
1.15 Figure 1.2 shows the contribution each type of tax has made to the value of the tax gap between 2005-06 and 2011-12. The two largest tax components of the tax gap have consistently been from IT, CGT and NICs and VAT. This reflects the fact that the majority of tax receipts are collected from these types of tax (55 per cent from IT, NICs and CGT, and 19 per cent from VAT). Figure 1.3 shows the value of the tax gap in 2011-12 by type of tax. The largest component is IT, NICs and CGT that comprises 44 per cent of the total tax gap.

Figure 1.2: Value of the tax gap by type of tax, 2005-06 to 2011-12*,†



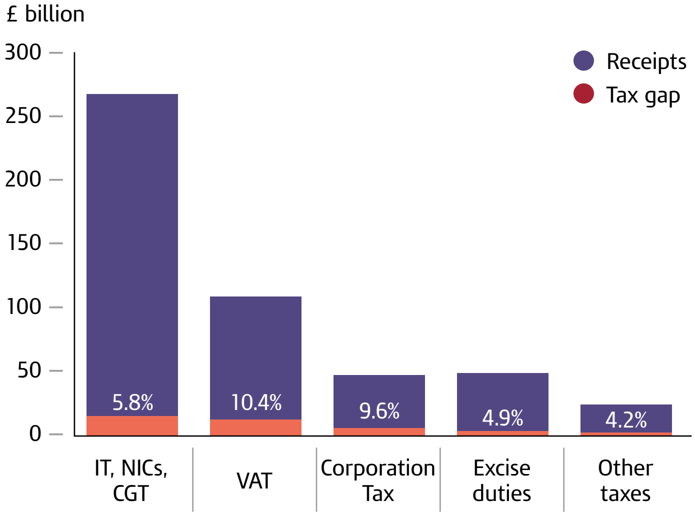
* Estimates are rounded to nearest 0.1 per cent
† 'Other taxes' includes Stamp Duties, Inheritance Tax, Petroleum Revenue Tax, Environmental Taxes and Insurance Premium Tax

Figure 1.3: Value of the tax gap by type of tax, 2011-12



1.16 Figure 1.4 illustrates that the majority of tax receipts are collected from IT, NICs and CGT and VAT. It also shows that the tax gap for IT, NICs and CGT of £15.3 billion equates to just 5.8 per cent of the total theoretical liabilities for IT, NICs and CGT. This can be compared to the VAT tax gap (£11.4 billion) which equates to 10.4 per cent of VAT theoretical tax liabilities.

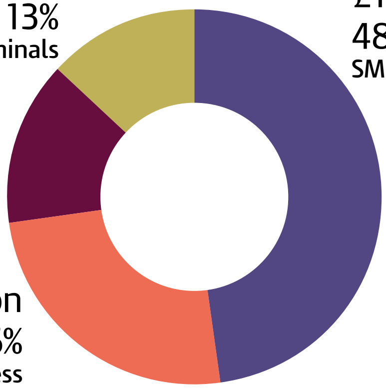
Figure 1.4: Total theoretical liabilities* by type of tax, 2011-12



* Percentage tax gap as a proportion of total theoretical liabilities.

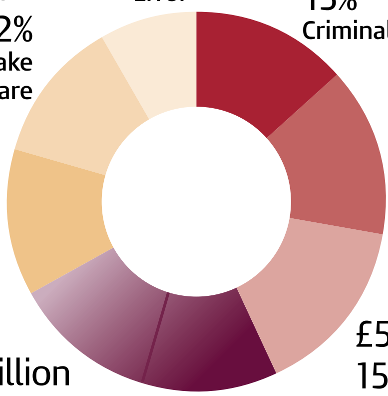
1.17 Figure 1.5, shows the value of the 2011-12 tax gap broken down by customer group. It is estimated that nearly half of the 2011-12 tax gap can be attributed to small and medium-sized businesses and one quarter from large businesses. The remainder is split between criminals and individuals.

Figure 1.5: Value of the tax gap by customer group, 2011-12



1.18 Figure 1.6 shows the estimated composition of taxpayer behaviours within the overall value of the tax gap for 2011-12. These estimates involve management assumptions and judgement and can only be used to give a broad indication of behaviours. Behaviours are defined in Table 1.5. As the estimates are based on judgement, great caution is required when comparing with similar analysis in previous publications.

Figure 1.6: Value of the tax gap by behaviour, 2011-12*



*These numbers do not sum to 100% due to rounding.

1.19 Table 1.4 shows the avoidance tax gap estimate for 2011-12. These estimates involve management assumptions and judgement. Last year the avoidance tax gap for 2010-11 was shown as £5 billion. The avoidance tax gap for 2010-11 is now estimated to be closer to £4 billion due in part to revisions to the Stamp Duty Reserve Tax estimates (see Tables 1.6 and 1.7). Behaviours cannot be compared year on year because the data available does not always enable estimates to be updated for earlier years. The estimate for 2011-12 is £4.0 billion.

Table 1.4: Avoidance tax gap by type of tax, 2011-12 (£ billion)

Type of Tax	2011-12
IT, NICs and CGT	2.0
Corporation Tax	1.5
VAT	0.2
Other direct taxes[1]	0.3
Total	**4.0**

[1] 'Other direct taxes' includes Stamp Duties, Inheritance Tax, Petroleum Revenue Tax.

Table 1.5: Description of behaviours

Criminal attacks	Organised criminal gangs undertake co-ordinated and systematic attacks on the tax system. This includes smuggling (e.g. of alcohol or tobacco), VAT repayment fraud and VAT Missing Trader Intra-Community (MTIC) fraud.
Evasion	Tax evasion is illegal activity, where registered individuals or businesses deliberately omit, conceal or misrepresent information in order to reduce their tax liabilities.
Hidden economy	This definition of the hidden economy reflects sources of undeclared economic activity, and consists of undeclared activities of both 'ghosts' whose entire income is unknown to HMRC, and 'moonlighters' who are known to HMRC in relation to part of their income, but have other source(s) of income unknown to HMRC. The hidden economy is the non-declaration of an entire source of hidden income, whereas evasion is the deliberate understatement of a declared source of income.
Avoidance	Tax avoidance is bending the rules of the tax system to gain a tax advantage that Parliament never intended. It often involves contrived, artificial transactions that serve little or no commercial purpose other than to produce a tax advantage. It involves operating within the letter but not the spirit of the law. Tax avoidance is not the same as legitimate tax planning. Legitimate tax planning involves using tax reliefs for the purpose for which they were intended. For example, claiming tax relief on capital investment, saving in a tax-exempt ISA or saving for retirement by making contributions to a pension scheme are all legitimate forms of tax planning.
Legal interpretation	Legal interpretation relates to the potential tax loss from cases where HMRC and individuals or businesses have different views of how, or whether, the law applies to specific and often complex transactions. Examples include the correct categorisation of an asset for allowances, the allocation of profits within a group of companies, or VAT liability of a particular item. In these situations the customer will have an alternative view of the law and of how it applies to the facts in their case to that held by HMRC.
Non-payment	For direct taxes, non-payment refers to tax debts that are written off by HMRC and therefore result in a permanent loss of tax - mainly as a result of insolvency. It does not, therefore, include debts that are eventually paid. VAT non-payment differs as it is based on the difference between new debts arising and debt payments (see Chapter 2).
Failure to take reasonable care	Failure to take reasonable care results from customers' carelessness and/or negligence in adequately recording their transactions and/or in preparing their tax returns. Judgments of 'reasonable care' should consider and reflect customers' knowledge, abilities and circumstances.
Error	Errors result from mistakes made in preparing tax calculations, completing returns or in supplying other relevant information, despite the customer taking reasonable care.

Revisions to tax gap estimates: 2005-06 to 2010-11

1.20 Estimates for some of the tax gap components have been revised since ‘Measuring Tax Gaps 2012’, due to improvements in the methodologies used, updated data available, and projections based on more recent years. Table 1.6 summarises the amount of revisions for each component and Table 1.7 summarises the reasons. Further information is available within the chapters.

Table 1.6: Revisions to estimates since last publication (‘Measuring Tax Gaps 2012’)[1,2]

Tax	Type	Component	Point estimates (£ billion)					
			2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
Value Added Tax	**Total VAT**		**+1.3**	**+1.3**	**+1.2**	**+1.9**	**+0.8**	**+0.3**
Excise duties	Excise duties	Cigarette duty	-0.1	-0.1	-0.3	-0.2	-0.1	-0.2
		Hand rolled tobacco duty	neg	neg	neg	neg	+0.1	neg
		Total tobacco	**-0.1**	**-0.1**	**-0.3**	**-0.2**	**neg**	**-0.2**
	Alcohol duties	Spirits duty	-	-	-	-	-	neg
		Beer duty	-	-0.1	-	-	-	+0.1
		Wine duty	-	-	+0.3	+0.2	+0.2	+0.5
		Total alcohol	-	**-0.1**	**+0.3**	**+0.2**	**+0.2**	**+0.6**
	Hydrocarbon oils duties	Great Britain diesel duty	+0.2	+0.2	+0.2	+0.2	+0.3	+0.3
		Great Britain petrol duty	-	-	-	-	-	-
		Northern Ireland diesel duty	-	neg	neg	-	-	neg
		Northern Ireland petrol duty	-	-	-	-	-	neg
		Total hydrocarbon oils	**+0.2**	**+0.1**	**+0.1**	**+0.2**	**+0.3**	**+0.3**
		Other excise duties	+0.2	+0.2	+0.2	+0.2	+0.2	+0.1
	Total excise duties		**+0.3**	**+0.1**	**+0.4**	**+0.3**	**+0.6**	**+0.7**
Income Tax, National Insurance Contributions, Capital Gains Tax (IT, NICs, CGT)	Self Assessment	Non-business taxpayers	-0.3	-0.1	+0.3	+0.2	neg	-0.1
		Business taxpayers	-0.2	-0.3	+0.2	-0.1	+0.4	+0.3
		Large partnerships	-0.1	-0.1	+0.1	neg	neg	-0.1
		Total Self Assessment	**-0.6**	**-0.4**	**+0.5**	**+0.1**	**+0.4**	**+0.1**
	PAYE	Small and medium employers	+0.3	+0.1	+0.2	+0.1	+0.3	+0.9
		Large employers	-	-	-	-	-	neg
		Total PAYE	**+0.3**	**+0.1**	**+0.2**	**+0.1**	**+0.3**	**+0.9**
	Avoidance	**Total avoidance (IT, NICs, CGT)**	**N/A**	**N/A**	**N/A**	**N/A**	**N/A**	**N/A**
	Hidden economy	PAYE individuals not in self assessment	N/A	N/A	N/A	N/A	N/A	neg
		Ghosts	N/A	N/A	N/A	N/A	N/A	neg
		Moonlighters	N/A	N/A	N/A	N/A	N/A	neg
		Total hidden economy (IT, NICs, CGT)	N/A	N/A	N/A	N/A	N/A	**-0.1**
	Total IT, NICs, CGT		**-0.3**	**-0.3**	**+0.7**	**+0.5**	**+0.7**	**+1.0**
Corporation Tax		Small and medium businesses	-0.1	-0.3	-0.1	+0.3	-0.1	+0.6
		Large and Complex businesses	+0.4	+0.3	+0.3	+0.2	-0.2	+0.1
		Businesses managed by the Large Business Service	+0.2	neg	+0.4	+0.3	neg	neg
	Total Corporation Tax		**+0.6**	**+0.1**	**+0.7**	**+0.8**	**-0.3**	**+0.6**
Other taxes	Stamp duties	Stamp Duty Land Tax	N/A	N/A	N/A	N/A	N/A	-0.1
		Stamp Duty Reserve Tax	N/A	N/A	N/A	N/A	N/A	-0.3
		Total stamp duties	-	-	-	-	-0.3	-0.3
	Other direct taxes	Inheritance Tax	-	-	-	-	+0.1	+0.1
		Petroleum Revenue Tax	-	neg	neg	-	-	neg
	Other indirect taxes	Environmental taxes, Insurance Premium Tax	-0.2	-0.5	-0.4	-0.4	-0.5	-0.5
	Total other taxes		**-0.2**	**-0.5**	**-0.4**	**-0.4**	**-0.7**	**-0.7**
Total tax gap			**+1.6**	**+0.7**	**+2.6**	**+3.1**	**+1.0**	**+1.9**

1 neg denotes negligible, revisions are less than £50 million.
2 N/A denotes that comparable estimates for earlier years are not available.

1.21 Figure 1.7 shows the revisions made to aggregate tax gap estimates since 'Measuring Tax Gaps 2010'. The tax gap for the 2008-09 tax year proved the hardest to estimate; however, firmer operational data for relevant tax cases relating to that year is not available. Improvements to our projection methods were made in the 2012 edition. The extent of revisions shows that the tax gap measure is a long-term indicator and that overall trends are more reliable than year-on-year changes. The latest figures are within the previously published range.

Figure 1.7: Revisions to the value of the tax gap as a percentage of liabilities since 'Measuring Tax Gaps 2010'

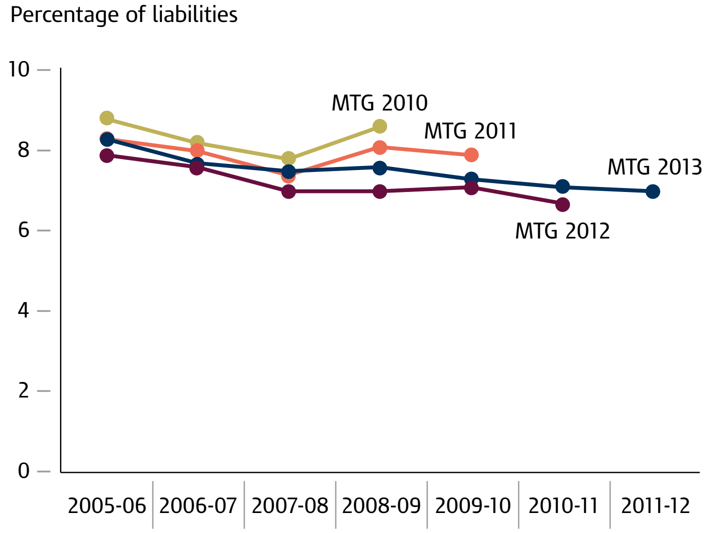


Table 1.7: Description of revisions to estimates since last publication

Tax gap component	Revisions
Value Added Tax	
	• The VAT gap estimates have been updated with expenditure data consistent with the latest national accounts published on 31 July 2013. This has resulted in an increase in the level of the VAT gap for all years; however, the overall trend has remained the same. • The method used to provide MTIC fraud estimates has recently been reviewed with a new methodology in place which better captures changes in the way MTIC fraud is carried out. It is not possible to recalculate past years using the new methodology, as the data is not available before this point. • In April 2011 HMRC introduced a new, more automated administrative data system for recording VAT debt. As a result, the estimate for 2011-12 may not be directly comparable with estimates up to and including 2010-11. • This is the first time an estimate for VAT avoidance has been published. The tax gap arising from the avoidance of VAT is estimated by applying the same methodology that is used to estimate the IT, NICs and CGT tax gap due to avoidance. • A preliminary estimate for 2012-13 will be published at the time of the autumn and spring publications of the Economic and Fiscal Outlook.

Excise duties and other indirect taxes	
Alcohol	• The 2010-11 estimates have been revised for both spirits and beer as the Living Costs and Food survey data were not available at the time of publishing 'Measuring Tax Gaps 2012'. Additionally, ONS population estimates were updated following Census 2011 results. Experimental figures for the wine tax gap have been published for the first time.
Tobacco	• There have been small revisions to estimates of the cigarette tax gap compared with published figures in previous releases of Measuring Tax Gaps. Improvements have been made to the methodology so that the range between the upper and lower estimates has been reduced. • Some minor revisions to previously published estimates of hand rolling tobacco have also been made. This is due to new data being available for use in the models, namely ONS population estimates where improved figures were released following the publication of the Census 2011 results.
Oils	• Various input data have been revised historically, including: distances driven, fuel efficiencies, information on heavy goods vehicles and the amount of fuel delivered in the UK. These updates have revised estimates for previous years. The inclusion of an element of uncertainty to GB diesel consumption has also resulted in revised estimates for previous years.

Income Tax, National Insurance Contributions, Capital Gains Tax	
Self Assessment	• 2005-06 to 2008-09 have been revised due to the settlement of more enquiries relating to those years. • 2009-10 has been revised due to using actual data rather than being projected from the 2008-09 estimate. • 2010-11 has been revised as it is now projected from the 2009-10 estimate rather than the 2008-09 estimate. Projections are made assuming stable compliance behaviour, using the year on year change in relevant tax liabilities. • Methodological improvements to the treatment of large 'outlier' enquiry settlements have led to amendments to some years. The largest impact was an increase in 2007-08. • Improved reallocation of non-payment from Self Assessment to SME employers has led to decreases in all years from 2005-06, with the largest impact being in 2010-11.
Small employers	• 2005-06 to 2009-10 have been revised due to the settlement of more reviews. • 2010-11 has been revised as it now uses actual data rather than is projected from the 2009-10 estimate. Projections are made assuming stable compliance behaviour, using the year on year change in relevant tax liabilities. • Methodological improvements to the treatment of large 'outlier' enquiry settlements have led to changes across all years. The largest impact was an increase in 2010-11. • Improved reallocation of non-payment from Self Assessment to SME employers has led to increases in all years from 2005-06, with the largest impact being in 2010-11.
Avoidance	• Avoidance estimates cannot be fully updated as HMRC's register of information on identified avoidance schemes are not revised for previous years.
Hidden economy	• Hidden economy tax gap estimates for previous years are recalculated, but remain illustrative.

Corporation Tax	
Businesses managed by the Large Business Service	• 2005-06 to 2008-09 have been revised with data from the closure of more risks, better estimates of tax under consideration on LBS' case management system and the incorporation of further quality assurance checks into the methodology. • 2009-10 has been revised as it is now estimated from case management data rather than projected from 2008-09. • 2010-11 has been revised as it is now projected from 2009-10 data instead of 2008-09 data. • Projections are made assuming stable compliance behaviour, using the year on year change in LBS CT tax receipts.
Large and Complex businesses	• 2010-11 has been revised as it is estimated from the updated tax under consideration estimate for 2009-10 for businesses managed by the LBS.
Small and medium-sized businesses	• 2007-08 and 2008-09 estimates are shown for the first time as the addition of extra enquiry information in the past year has resulted in enough data now being available to regard the 2007-08 and 2008-09 financial years as fit for publication. • All the other years to 2010-11 published last year have been revised due to: (a) settlement of more enquiries relating to those years; (b) use of operational data for all the years rather than projections; and (c) analysis of the enquiries on a financial year basis instead of a calendar year basis. • Methodological improvements to the treatment of large 'outlier' enquiries have led to changes across all years.

Other indirect taxes	
	• These figures have been revised to exclude wine, which now has a separate estimate in Chapter 3.

Other direct taxes	
Inheritance Tax	• There has been a methodological change to the percentage of liabilities that is estimated to be tax gap. It has been increased from 17.5 per cent to 20 per cent.
Stamp Duty Land Tax	• SDLT methodology has been reviewed and improved since MTG 2012, and the estimates for 2009-10 and 2010-11 have been revised accordingly. The estimate is now substantially based on information held by HMRC.
Stamp Duty Reserve Tax	• There has been a methodological change to the percentage of liabilities that is estimated to be tax gap. It has been decreased from 10 per cent to 1.5 per cent.
Petroleum Revenue Tax	• No revisions to previously published estimates.

2 – VAT gap

Key findings

- The VAT gap is estimated at £11.4 billion in 2011-12. This equates to around 10.4 per cent of the estimated VAT total theoretical liability (VTTL). This estimate includes:
  - £0.5 billion to £1.0 billion of MTIC (Missing Trader Intra-Community) fraud
  - £1.8 billion of VAT debt
  - £0.2 billion due to VAT avoidance.
- The VAT gap has increased between 2010-11 and 2011-12 from £9.9 billion to £11.4 billion. However, in percentage terms, the VAT gap has remained flat at 10.4 per cent. The increase in the point estimate is largely due to an increase in the standard rate of VAT to 20 per cent in January 2011.
- The 2011-12 estimate of MTIC fraud has remained at the same level as in 2010-11. VAT debt has increased from £0.9 billion in 2010-11 to £1.8 billion in 2011-12 (Figure 2.2). The increase in VAT debt is partly due to the increase in the VAT rate, as well as the introduction of a new administrative data system.
- In 2011-12, approximately 70 per cent of net VTTL is from household consumption with the remaining proportion from consumption by businesses making exempt supplies, government and housing sectors (Figure 2.3).
- Restaurants and hotels, recreation and culture, and transport are the largest contributors to the household sector. This is consistent with estimates in previous years (Figure 2.4).
- The Office for National Statistics (ONS) recently revised its national accounts estimates which led to an increase in the level of GDP. The upward revision was associated with an increase in estimates of expenditure for all years, which has flowed through into an upward revision to the VTTL and hence into the VAT gap. For 2010-11, the VAT gap has been revised up from £9.6 billion to £9.9 billion and the percentage VAT gap has been revised from 10.1 per cent to 10.4 per cent. However, the overall trend in the VAT gap has remained the same (Figure 2.5).

Results and tables

2.1 Table 2.1 shows the estimated net VAT total theoretical liability (VTTL), net VAT receipts and the estimated VAT gap for years 2007-08 to 2011-12.

Table 2.1: Estimated VAT gap (£ billion)[1]

	2007-08	2008-09	2009-10	2010-11	2011-12
Net VTTL	92.8	93.0	80.8	95.3	109.8
Net VAT receipts[2]	82.0	79.8	71.4	85.4	98.4
VAT gap (point estimate)	**10.8**	**13.2**	**9.4**	**9.9**	**11.4**
of which MTIC fraud	1.0-1.5	1.0-1.5	1.0-1.5	0.5-1.0	0.5-1.0
of which debt	0.9	2.4	1.8	0.9	1.8
VAT gap (per cent)[3]	**11.7%**	**14.2%**	**11.6%**	**10.4%**	**10.4%**

1 The amounts are rounded to the nearest £0.1 billion.
2 Net VAT receipts are expressed net of payments and repayments.
3 The VAT gap as a percentage of VTTL has been rounded to the nearest 0.1 per cent.

2.2 While the value of the VAT gap fluctuates over the period 2007-08 to 2011-12 this is mainly due to changes in the standard rate of VAT over this period. The VAT gap expressed as a percentage of VTTL provides a like-for-like comparison excluding the impact of any rate change.

2.3 Figure 2.1 shows a time series of the VAT gap over the period 2005-06 to 2011-12. The VAT gap excluding debt has remained broadly stable from 2009-10 onwards at around 9 per cent of VTTL.

Figure 2.1: Time series of the VAT gap, including and excluding debt

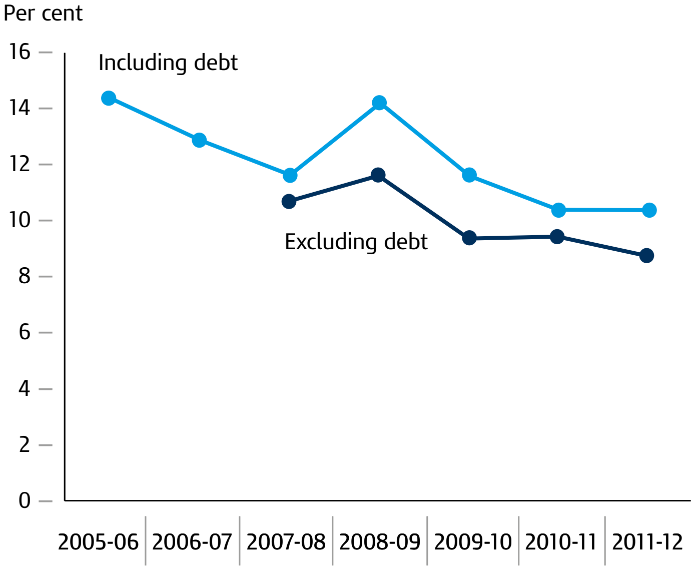
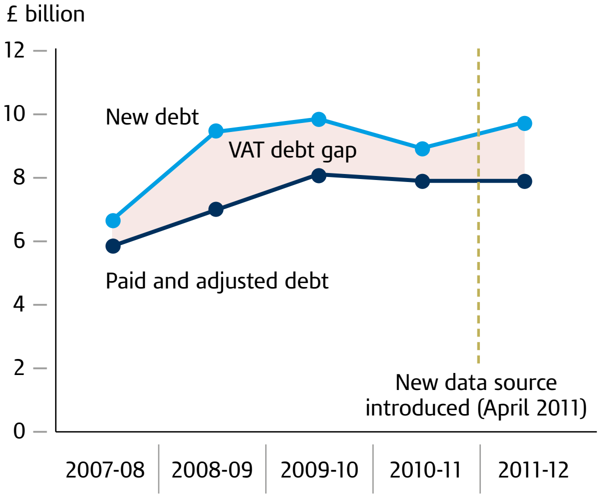


Figure 2.2: Time series of VAT debt



MTIC (Missing Trader Intra-Community) fraud

2.4 The level of MTIC fraud has declined since a peak of between £3.0 billion and £4.0 billion in 2005-06. It has stayed broadly stable between £0.5 billion and £1.5 billion from 2007-08 onwards with the estimate for 2011-12 being between £0.5 billion and £1.0 billion. (See 'Methodology and data issues' section for definition of MTIC fraud.)

VAT Debt

2.5 The contribution of debt to the VAT gap is defined as the amount of VAT declared by businesses but not yet paid to HMRC. The VAT gap peaked in 2008-09 at 14.2 per cent. This was the result of an increase in VAT debt from £0.9 billion in 2007-08 to £2.4 billion in 2008-09 brought on by the economic downturn. The level of debt returned to the pre-recession level of £0.9 billion in 2010-11, before increasing to £1.8 billion in 2011-12.

2.6 The rise in VAT debt in 2011-12 from the low level in 2010-11 is partly due to the increase in the VAT rate in January 2011. There could also be an impact on the level of VAT debt from the introduction of a new administrative data system used by HMRC to record debt.

2.7 Figure 2.2 shows that the lower 2010-11 VAT debt estimate is driven by a fall in new debt, with the level of paid and adjusted debt remaining stable between 2009-10 and 2011-12. (See 'Methodology and data issues' section for definition of VAT debt.)

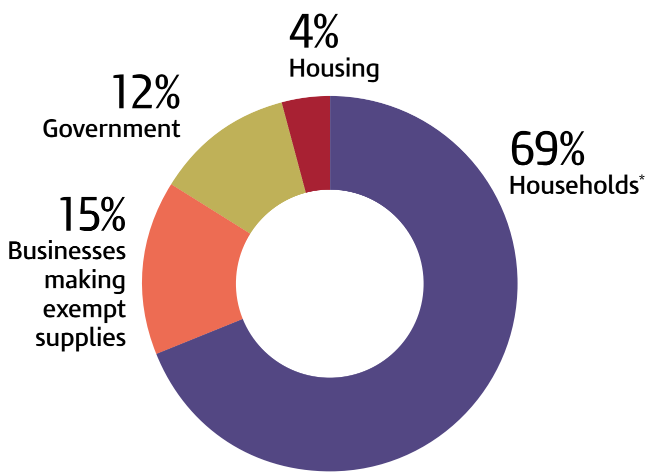
Avoidance

2.8 Another component of the VAT gap is VAT avoidance – bending the rules of the tax system to gain a tax advantage that Parliament never intended (see Table 1.5: Description of behaviours). VAT avoidance is estimated to be £0.2 billion in 2011-12.

Sectoral analysis

2.9 Figure 2.3 shows each sector's contribution to the VTTL in percentage terms, with household consumption contributing approximately 70 per cent in 2011-12. This is consistent with the estimates of the VAT gap in previous years.

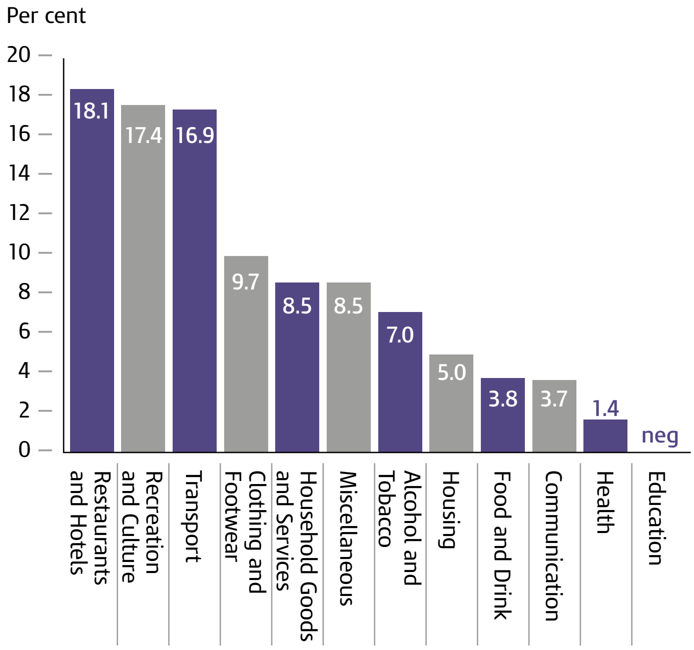
Figure 2.3: Components of the VTTL in 2011-12



* Households component also includes estimates of expenditure by non-profit institutions serving households.

2.10 Estimates of the contribution to the household sector in percentage terms of each relevant expenditure component for 2011-12 are given in Figure 2.4. Restaurants and hotels, recreation and culture and transport are the largest contributors to the household sector. Again, this is consistent with the estimates of the VAT gap in previous years.

Figure 2.4: VAT-able expenditure for the household sector in 2011-12*



* neg denotes negligible, an estimate of less than 0.05 per cent.

Methodology and data issues

2.11 The total level of VAT losses is measured by comparing the net VAT total theoretical liability (VTTL) with actual VAT receipts. The difference between these amounts is known as the VAT gap.

2.12 The VAT gap methodology uses a 'top-down' approach which involves:

- gathering data primarily from the Office for National Statistics (ONS) detailing the total amount of expenditure in the economy that is subject to VAT
- estimating the rate of tax on that expenditure based on commodity breakdowns of the expenditure data to derive the gross VTTL
- the gross VTTL in the economy is built up from the five expenditure components: household consumption, capital expenditure on housing, government expenditure, charities expenditure and expenditure of businesses making exempt supplies
- subtracting any legitimate refunds (deductions) occurring through schemes and reliefs to arrive at the net VTTL
- subtracting actual VAT receipts from the net VTTL
- the net VTTL for the calendar year is compared to the VAT receipts for the corresponding financial year, assuming a three-month lag between the economic activity and the payment to HMRC of the associated VAT
- the residual element, the gap, is assumed to be the total VAT gap including fraud, debt and other losses.

2.13 This release includes data available up to 26 September 2013. Data are consistent with United Kingdom National Accounts – The Blue Book, 2013 edition, published on 31 July 2013.

2.14 The next release of the Blue Book has a provisional publication date of 31 October 2014 and the Consumer Trends data, which also feed into the VAT gap model, are released on a quarterly basis in September, December, March and June. For the exact date of release please refer to the UK National Statistics Publication Hub.

2.15 VAT gap estimates are incorporated annually into the total tax gap as part of the 'Measuring Tax Gaps' publication. These estimates will be subject to further revision as more data becomes available and methodological improvements are implemented.

2.16 A preliminary estimate for 2012-13 relies on the publication of revised forecasts for the UK economy by the Office for Budget Responsibility. Therefore, preliminary estimates of the VAT gap for 2012-13 will be published at the time of the autumn and spring publications of the Economic and Fiscal Outlook. For the exact date of release please refer to the HMRC website.

MTIC (Missing Trader Intra-Community) VAT fraud

2.17 MTIC VAT fraud is an organised criminal attack on the EU VAT system in which fraudulent traders acquire goods or services VAT free from EU Member States. They charge VAT on their onward sale and go 'missing' to avoid paying the VAT charged to the relevant tax authorities. One form of the fraud – known as carousel fraud – involves a series of contrived transactions within and beyond the EU, with the aim of creating large unpaid VAT liabilities and in some cases invalid VAT repayment claims.

2.18 The method used to provide MTIC fraud estimates has recently been reviewed with a new methodology in place which better captures changes in the way MTIC fraud is carried out. It is not possible to recalculate past years using the new methodology, as the data is not available before this point. There is therefore a break in the time series between 2010-11 and 2011-12, with estimates up to and including 2010-11 calculated using the previous methodology. However, the estimate for 2011-12 which is produced using the new methodology has given the same estimate of £0.5 billion to £1.0 billion as published last year for 2010-11 using the old methodology. It is not the intention to revise estimates for years before 2011-12 in this or future publications.

2.19 It is not appropriate to reveal details of the methodology used to provide MTIC fraud estimates, as to do so may have a detrimental effect on compliance activity.

VAT Debt

2.20 For VAT, debt is defined as the difference between new debts arising in the financial year and debt payments plus debt adjustments made in the financial year, unlike for direct taxes, where non-payment is equated to debt written off. Debt adjustments refer to the difference between the amount initially declared by the trader and the finalised amount due.

2.21 The contribution of debt to the VAT gap is estimated using statistics from HMRC administrative data with adjustments made to exclude MTIC debt and to reflect the deferral of payments under the Time To Pay arrangements. As a consequence of data quality issues, the debt contribution can only be measured from 2007-08.

2.22 The methodology detailed above to produce estimates for the contribution of debt to the VAT gap does not relate to debt stocks or debt written-off. Therefore, estimates shown will differ from the VAT debt balance as reported in the HMRC annual report.

2.23 In April 2011 HMRC introduced a new, more automated administrative data system for recording VAT debt. As the estimate for 2011-12 was produced using a different data source to previous years, differences in the way the new system classifies debt may impact on the figures. As a result the estimate for 2011-12 may not be directly comparable with estimates up to and including 2010-11.

Avoidance

2.24 The tax gap arising from the avoidance of VAT can be estimated by applying the same methodology that is used to estimate the IT, NICs and CGT tax gap due to avoidance (as described in Chapter 6). The illustrative estimate is £0.2 billion for 2011-12. This estimate includes an uplift on the assumption that not all the tax at risk from avoidance has been identified and recorded on HMRC's avoidance risk register.

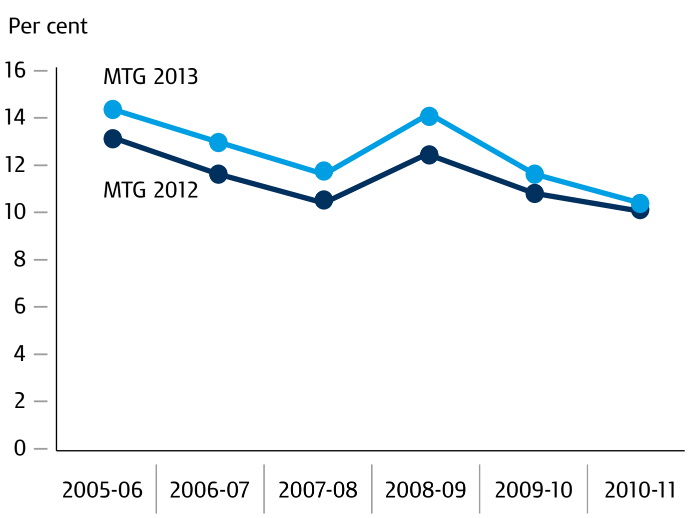
Revisions

2.25 The ONS National Accounts data are a key component of the VAT gap estimate. Every year, ONS updates the UK national accounts through a process known as annual supply and use balancing. This brings together detailed data on the three approaches to measuring gross domestic product (GDP) and balances them by product and industry. At the same time, any major methodological or classification changes may be implemented within the accounts. They are currently part way through a work programme designed to meet their international obligations to introduce a new European System of Accounts (ESA10) by 2014.

2.26 The VAT gap calculation is based on the data used in the expenditure approach to measure GDP. In the latest update, ONS revised its estimates of GDP upwards, leading to an increase in the level of GDP throughout the period since 1997, by an average of just over 1 per cent. The upward revision to GDP was associated with an increase in estimates of expenditure for all years, which has flowed through into an upward revision to the VTTL and hence into the VAT gap. More detailed articles on all the methodological changes can be found on the ONS National Accounts articles web page.

2.27 The impact of revisions made to the VAT gap estimates since last year's publication 'Measuring Tax Gaps 2012' (MTG 2012) are given in Figure 2.5. This has resulted in an increase in the level of the VAT gap. However, the overall trend has remained the same. For the period 2005-06 to 2010-11, the VAT gap has been revised upwards by 0.3 to 1.8 percentage points, or £0.3 billion to £1.9 billion. The VAT gap for 2010-11 has been revised up from £9.6 billion to £9.9 billion and the percentage VAT gap has been revised from 10.1 per cent to 10.4 per cent.

Figure 2.5: Revisions to the VAT gap estimates since Measuring Tax Gaps 2012



3 – Alcohol tax gaps

Key findings for spirits

- The spirits illicit market share is 3 per cent in 2011-12, with associated revenue losses of £120 million.
- The spirits illicit market share fluctuates between 2 and 6 per cent between 2008-09 and 2011-12, suggesting a consistently lower share than the 8 per cent estimated in 2007-08. This temporary increase in 2010-11 is consistent for spirits, wine and beer. This is a decrease of 5 percentage points over the period.

3.1 Further tables on spirits, showing a breakdown of UK market share, UK revenue and volumes can be found online in the 'Measuring Tax Gaps 2013' tables in Excel.

Results and tables for spirits

Figure 3.1: Spirits: Illicit market shares – mid-point estimate and confidence intervals

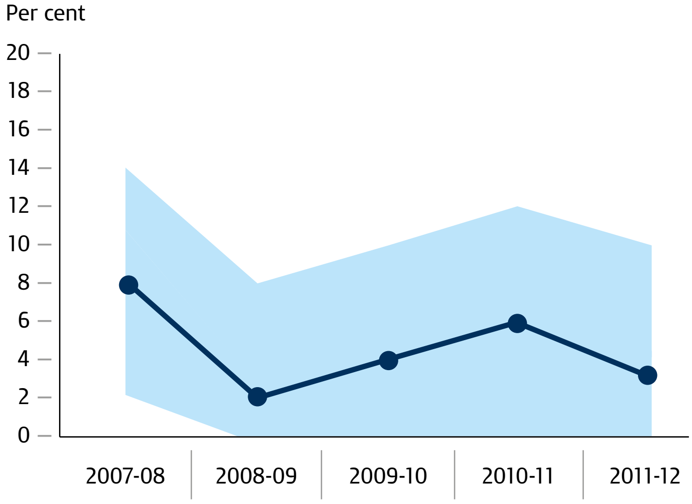


Table 3.1: Spirits: Illicit market share and associated revenue losses

	2007-08	2008-09	2009-10	2010-11[1]	2011-12[2]
Illicit market shares (per cent)[3]					
Upper estimate	14%	8%	10%	12%	10%
Mid-point estimate	8%	2%	4%	6%	3%
Lower estimate[4]	2%	0%	0%	0%	0%
Associated revenue losses (£ million)[5,6]					
Upper estimate	550	310	410	560	490
Mid-point estimate	310	80	140	250	120
Lower estimate[4]	70	0	0	0	0

1 Figures for 2010-11 have been revised.
2 Figures for 2011-12 are provisional.
3 Figures independently rounded to the nearest 1 per cent.
4 Negative numbers have been truncated at zero.
5 Includes both duty and VAT.
6 Figures independently rounded to the nearest £10 million.

Methodology and data issues for spirits

3.2 The spirits tax gap estimate is produced using a top-down methodology; total consumption is estimated, from which legitimate consumption is subtracted with the residual being the illicit market.

3.3 Total consumption is estimated using the Living Costs and Food Survey (LCF). Legitimate consumption is based upon the returns to HMRC from the volumes of alcohol on which duty have been paid. The details of the methodology are presented in the separate Methodological Annex.

3.4 For spirits, the central estimate is best interpreted as an indicator of long-term trend in the illicit market share, rather than a precise estimate of the level or year-to-year changes. The upper and lower estimates are 95% confidence intervals indicating the potential size of fluctuations in the mid-point estimates due to sampling error. They do not take account of any systematic tendency to over or under estimate the size of the tax gap that might arise from the modelling assumptions.

Revisions

3.5 The LCF survey only becomes available around 18 months after the survey period. For this reason, estimates for 2012-13 are not yet available and some elements of the 2011-12 estimates have been produced using forecasts. Therefore, estimates for 2011-12 should be considered provisional. In addition, the estimates for 2010-11 have been revised with new data.

Key findings for beer

- The beer illicit market share is 9 per cent in 2011-12, with associated revenue losses of £550 million.
- The illicit market share in beer shows a generally level trend of 9 per cent from 2007-08 to 2009-10, followed by an increasing trend to 11 per cent in 2010-11, before dropping to back to 9 per cent in 2011-12. This temporary increase in 2010-11 is consistent for spirits, wine and beer.

3.6 Further tables on beer, showing a breakdown of UK market share, UK revenues and volumes can be found online in the 'Measuring Tax Gaps 2013' tables in Excel.

Results and tables for beer

Figure 3.2: Beer: Illicit market shares – upper, lower and implied mid-point estimate

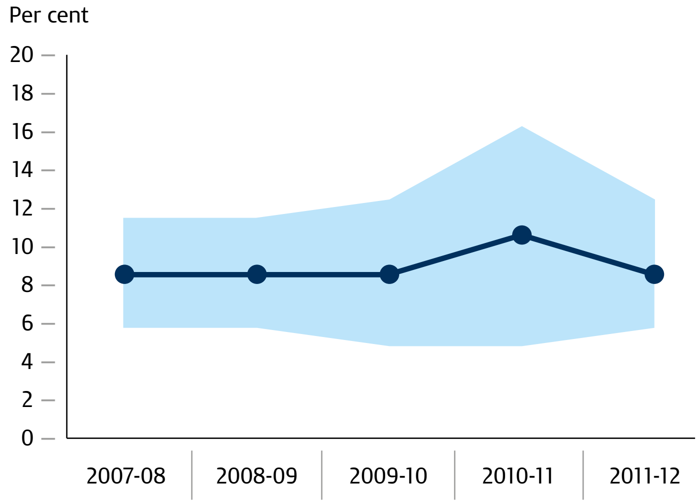


Table 3.2: Beer: Illicit market share and associated revenue losses

	2007-08	2008-09	2009-10	2010-11[1]	2011-12[2]
Illicit market shares (per cent)[3]					
Upper estimate	12 %	12 %	13 %	17 %	13 %
Implied mid-point	9 %	9 %	9 %	11 %	9 %
Lower estimate	6 %	6 %	5 %	5 %	6 %
Associated revenue losses (£ million)[4,5]					
Upper estimate	650	650	700	1,050	750
Implied mid-point	500	450	500	650	550
Lower estimate	300	300	250	300	350

1 Figures for 2010-11 have been revised.
2 Figures for 2011-12 are provisional.
3 Figures independently rounded to the nearest 1 per cent.
4 Includes both duty and VAT.
5 Figures independently rounded to the nearest £50 million.

Methodology and data issues for beer

Upper estimate

3.7 The beer tax gap upper estimate is produced using a top-down methodology; total consumption is estimated, from which legitimate consumption is subtracted, the residual being the illicit market.

3.8 Total consumption is estimated using the Living Costs and Food Survey (LCF). Legitimate consumption is based upon the returns to HMRC from the volumes of alcohol on which duty have been paid. The details of the methodology are presented in the separate Methodological Annex.

Lower estimate

3.9 The beer tax gap lower estimate is produced using a bottom-up methodology. This means estimates of illicit beer are made directly, using departmental data. The bottom-up methodology is less comprehensive than the top-down methodology, as is does not cover all types of fraud. The lower estimate includes only estimates of the diversion of UK produced beer and drawback fraud.

3.10 A number of beer frauds are not included in this methodology as it is difficult to estimate them. This is one of the reasons it is a lower bound estimate. These include smuggled beer, diversion of foreign produced beer and counterfeit beer.

Implied mid-point

3.11 The implied mid-point estimate is calculated as the average of the upper and lower estimates. It is only intended as an indicator of long-term trend – the true tax gap could lie anywhere within the bounds.

3.12 The upper and lower estimates should be interpreted as indicators of long-term trend, rather than precise estimates of the level or of year-to-year changes. They do not take account of any systematic tendency to over or under-estimate the size of the tax gap that might arise from the modelling assumptions.

Revisions

3.13 The LCF survey only becomes available around 18 months after the survey period. For this reason, estimates for 2012-13 are not yet available and some elements of the 2011-12 estimates have been produced using forecasts. Therefore, estimates for 2011-12 should be considered provisional. In addition, the estimates for 2010-11 have been revised with new data.

Key findings for wine

- The wine illicit market share is 6 per cent in 2011-12, with associated revenue losses of £350 million.
- The illicit market share for wine shows a decreasing trend from 11 per cent in 2007-08 to 6 per cent in 2008-09 to 2009-10, followed by an increasing trend to 12 per cent in 2010-11, before dropping to 6 per cent in 2011-12. This temporary increase in 2010-11 is consistent for spirits, wine and beer. This is a decrease of 5 percentage points over the period.

3.14 Further tables on wine, showing a breakdown of UK market share, UK revenue and volumes can be found online in the 'Measuring Tax Gaps 2013' tables in Excel.

Results and tables for wine

Figure 3.3: Wine: Illicit market shares – mid-point estimate and confidence intervals

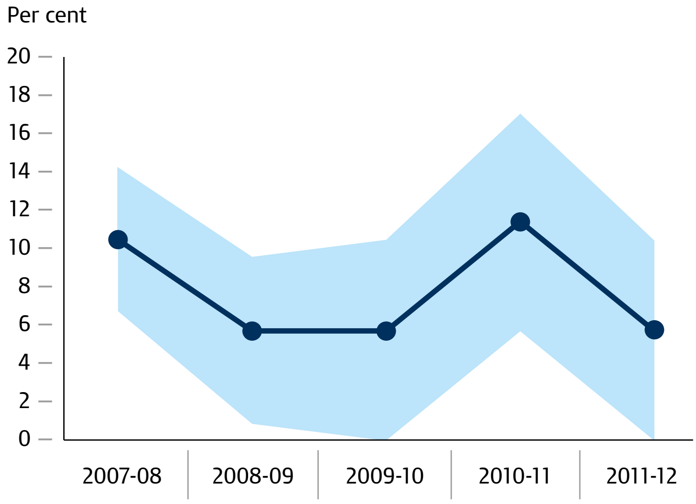


Table 3.3: Wine: Illicit market share and associated revenue losses

	2007-08	2008-09	2009-10	2010-11[1]	2011-12[2]
Illicit market shares (per cent)[3]					
Upper estimate[4]	15%	10%	11%	18%	11%
Mid-point estimate	11%	6%	6%	12%	6%
Lower estimate[4,5]	7%	1%	0%	6%	0%
Associated revenue losses (£ million)[6,7]					
Upper estimate[4]	820	470	570	1,140	700
Mid-point estimate	570	250	280	730	350
Lower estimate[4,5]	320	40	0	320	0

1 Figures for 2010-11 have been revised.
2 Figures for 2011-12 are provisional.
3 Figures independently rounded to the nearest 1 per cent.
4 Confidence intervals are experimental and should be taken as indicative.
5 Negative numbers have been truncated at zero.
6 Includes both duty and VAT.
7 Figures independently rounded to the nearest £10 million.

Methodology and data issues for wine

3.15 The wine tax gap is a new estimate, produced using an experimental top-down methodology; total consumption is estimated, from which legitimate consumption is subtracted, with the residual being the illicit market.

3.16 Total consumption is estimated using the Living Costs and Food Survey (LCF) and commercial research. Legitimate consumption is based upon the returns to HMRC from the volumes of alcohol on which duty have been paid. The details of the methodology are presented in the separate Methodological Annex.

3.17 For wine, the central estimate is best interpreted as an indicator of long term trend in the illicit market share rather than a precise estimate of the level or year-to-year changes. The 95% confidence intervals are experimental and therefore only indicative of the potential size of fluctuations in the estimates due to sampling error. They do not take account of any systematic tendency to over or under estimate the size of the tax gap that might arise from the modelling assumptions.

3.18 The LCF survey only becomes available around 18 months after the survey period. For this reason, estimates for 2012-13 are not yet available and some elements of the 2011-12 estimates have been produced using forecasts. Therefore, estimates for 2011-12 should be considered provisional.

4 - Tobacco tax gaps

Key findings for cigarettes

- The illicit market share for cigarettes is estimated to be 7 per cent in 2011-12, with associated revenue losses of £900 million.
- There has been a decreasing trend in the cigarette illicit market share. The level in 2011-12 is 5 percentage points lower compared with 2007-08.

Results and tables for cigarettes

The mid-point estimate should be interpreted as an indicator of long-term trends rather than a precise estimate of year-to-year changes.

Figure 4.1: Illicit market share for cigarettes — upper, lower and mid-point estimate

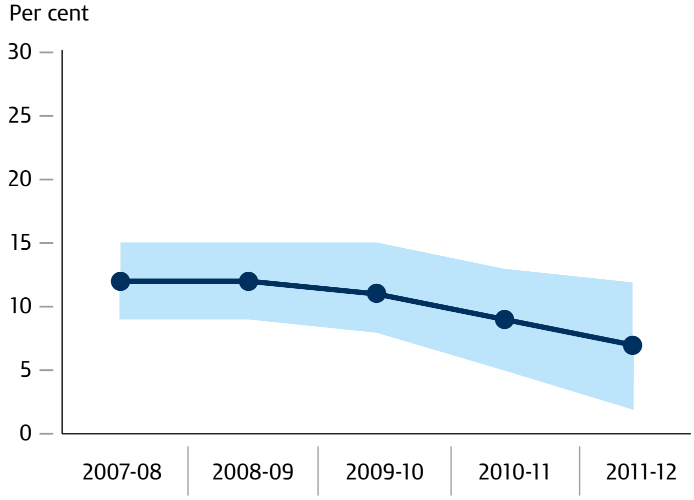


Table 4.1: Illicit market share and revenue losses for cigarettes[1]

	2007-08	2008-09	2009-10	2010-11	2011-12
Illicit market shares (per cent)					
Upper estimate	15%	15%	15%	13%	12%
Mid-point estimate	12%	12%	11%	9%	7%
Lower estimate	9%	9%	8%	5%	2%
Associated revenue losses (£ million)[2,3]					
Upper estimate	1,800	1,800	1,800	1,500	1,500
Mid-point estimate	1,400	1,400	1,300	1,000	900
of which:					
VAT	300	200	200	200	200
Duty	1,100	1,100	1,100	800	700
Lower estimate	1,000	1,000	900	500	200

1 Figures are independently rounded to the nearest 1 per cent or £100 million.
2 Includes both duty and VAT.
3 Based on the Weighted Average Price (WAP) of all UK duty paid cigarettes.

Key findings for hand rolling tobacco

- The illicit market share for hand rolling tobacco is estimated to be 35 per cent in 2011-12, with associated revenue losses of £700 million.
- These latest mid-point estimates show a downward trend in the last five years, with the illicit market share reducing from 49 per cent in 2007-08.

Results and tables for hand rolling tobacco

The mid-point estimate should be interpreted as an indicator of long-term trends rather than a precise estimate of year-to-year changes.

Figure 4.2: Illicit market share for hand rolling tobacco – upper, lower and mid-point estimate

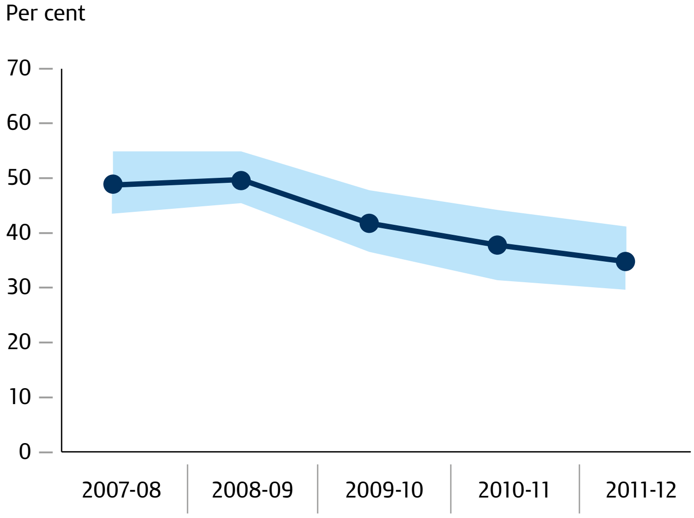


Table 4.2: Illicit market share and revenue losses for hand rolling tobacco[1]

	2007-08	2008-09	2009-10	2010-11	2011-12
Illicit market shares (per cent)					
Upper estimate	55%	55%	48%	44%	41%
Mid-point estimate	49%	50%	42%	38%	35%
Lower estimate	44%	46%	37%	32%	30%
Associated revenue losses (£ million)[2,3]					
Upper estimate	800	900	800	800	900
Mid-point estimate	700	800	700	700	700
of which:					
VAT	200	200	100	200	200
Duty	500	600	600	500	600
Lower estimate	500	700	600	500	600

1 Figures are independently rounded to the nearest 1 per cent or £100 million.
2 Includes both duty and VAT.
3 Weighted Average Price (WAP) data for all UK duty paid hand rolling tobacco is not available prior to 2012-13, so the losses are based on the price of a 'typical brand'.

Methodology and data issues for cigarettes and hand rolling tobacco

4.1 Further tables on cigarettes and hand rolling tobacco, showing a breakdown of UK market share and volumes can be found online in the 'Measuring Tax Gaps 2013' tables in Excel.

4.2 The estimates are produced using a top-down methodology; that is total consumption is estimated, from which legitimate consumption is subtracted, the residual being the illicit market.

4.3 The estimates are presented as lying within a range defined by the upper and lower estimates. The range provides an indication of the size of potential systematic errors due to under-reporting, and of the sampling error associated with the consumption estimates which are based on survey data. The midpoint of this range is also shown, and this figure represents the most likely estimate of the scale of the illicit market.

4.4 The Methodological Annex contains details on the methodology used.

Revisions

4.5 There have been small revisions to estimates of the cigarette tax gap compared with published figures in previous releases of 'Measuring Tax Gaps'. Improvements have been made to the methodology so that the range between the upper and lower estimates has been reduced.

4.6 Some minor revisions to previously published estimates of hand rolling tobacco have also been made. This is due to new data being available for use in the models, most namely ONS population estimates where improved figures were released following the publication of the Census 2011 results.

5 - Oils tax gaps

Key findings for GB diesel and petrol

- The GB diesel illicit market share lies within the range of 0 to 6 per cent in 2011-12, with associated revenue losses between £0 and £1,250 million.
- The illicit market share in GB diesel shows a generally level trend from 2007-08 to 2009-10, between 4 per cent and 5 per cent. This is followed by a reduction to 2 per cent in 2011-12.

Results and tables for GB diesel

The reduction to 2 per cent in 2011-12 may not be a true reflection of the illicit market share due to the sensitivity of the modelling assumptions when the tax gap is small.

5.1 Further tables on GB diesel, showing a breakdown of UK market share and volumes can be found online in the 'Measuring Tax Gaps 2013' tables in Excel.

Table 5.1: GB diesel: Illicit market share and associated revenue losses[1]

	2007-08	2008-09	2009-10	2010-11	2011-12[2]
Illicit market shares (per cent)[3]					
Upper estimate	7%	9%	9%	7%	6%
Mid-point estimate	4%	5%	5%	3%	2%
Lower estimate[4]	1%	1%	1%	0%	0%
Associated revenue losses (£ million)[5,6]					
Upper estimate	1,250	1,700	1,600	1,350	1,250
Mid-point estimate	700	950	850	500	400
Lower estimate[4]	100	200	100	0	0

1 Figures for previous years have been revised.
2 Figures for 2011-12 are provisional.
3 Figures independently rounded to the nearest 1 per cent.
4 Negative numbers have been truncated at zero.
5 Includes both duty and VAT.
6 Figures independently rounded to the nearest £50 million.

Methodology and data issues for GB diesel and petrol

5.2 The GB diesel tax gap estimates are produced using a top-down methodology; total consumption is estimated, from which legitimate consumption is subtracted, the residual being the illicit market.

5.3 Estimates of GB diesel and petrol consumption are derived from a number of data sources including sample surveys, vehicle testing and administrative data.

5.4 Petrol is considered to be less vulnerable to illicit activity than diesel, because of the low demand from commercial sectors and the flammable nature of the product. Therefore, the illicit market share in GB petrol is assumed to be negligible and this assumption lies behind the calculation for GB diesel.

5.5 The mid-point estimate is best interpreted as an indicator of long-term trends in the illicit market share rather than a precise estimate of the level or year-to-year changes. The confidence intervals indicate the potential size of chance fluctuations in the estimates due to sampling error. They do not take account of any systematic tendency to over or under-estimate the size of the tax gap that might arise from the modelling assumptions.

Revisions

5.6 Some elements of the 2011-12 estimates have been produced using forecasts. Therefore, estimates for 2011-12 should be considered provisional.

5.7 Various input data have been revised historically, including: distances driven, fuel efficiencies, information on heavy goods vehicles and the amount of fuel delivered in the UK. These updates have revised estimates for previous years.

5.8 This year there was an improvement in the methodology used to estimate the GB tax gap as additional data was obtained. As a result an element of uncertainty could be included to GB diesel consumption and this led to a revision in estimates for previous years. Uncertainty reflects wasted or unused diesel and consumption of diesel for domestic purposes and in non agricultural machinery. Further details can be found in the 'Methodological Annex'.

Key findings for Northern Ireland (NI) diesel

- For 2011-12 HMRC estimates that the market share for fraudulent diesel in NI is 12-13 per cent.
- The NI diesel non-UK duty paid market share is 27 per cent in 2011-12, with associated uncollected revenue of £160 million.
- The non-UK duty paid market share in NI diesel shows a decreasing trend from 30 per cent in 2007-08 to 27 per cent in 2011-12, with an unusually low estimate of 12 per cent in 2009-10.

Results and tables for NI diesel

5.9 The non-UK duty paid market includes both the illicit market and legitimate cross-border shopping consumed in Northern Ireland. HMRC has undertaken early modelling of the magnitude of cross-border shopping between the Republic of Ireland and Northern Ireland. This work is not yet fully robust, but clearly indicates that in most years about half of the non-UK duty paid figure is from completely legitimate cross-border shopping. For 2011-12 HMRC estimates that that the market share for fraudulent diesel is 12-13 per cent.

5.10 Analysis suggests that the low level of the non-UK duty paid market share in 2009-10 may be mainly due to a reduction in the amount of cross-border shopping by Northern Ireland residents in the Republic of Ireland. This is thought to be an anomaly peculiar to that year and is likely caused by a smaller price differential between the two countries in 2009-10, making it less cost effective for NI residents to cross the border to shop for their fuel.

5.11 Further tables on NI diesel, showing a breakdown of UK market share and volumes can be found online in the 'Measuring Tax Gaps 2013' tables in Excel.

Table 5.2: NI diesel: Non-UK duty paid market share and associated uncollected revenue[1]

	2007-08	2008-09	2009-10[2]	2010-11	2011-12[3]
Cross-border shopping + Illicit Market Shares (per cent)[4]					
Upper estimate	36%	30%	19%	31%	33%
Mid-point estimate	30%	24%	12%	25%	27%
Lower estimate	24%	18%	5%	19%	21%
Associated uncollected revenue (£ million)[5,6]					
Upper estimate	200	170	110	200	210
Mid-point estimate	160	130	60	150	160
Lower estimate	120	90	20	100	110

1 Figures for previous years have been revised.
2 The low level of the non-UK duty paid market in 2009-10 is believed to be due to a reduced level of cross border shopping.
3 Figures for 2011-12 are provisional.
4 Figures independently rounded to the nearest 1 per cent.
5 Includes both duty and VAT.
6 Figures independently rounded to the nearest £10 million.

Methodology and data issues for NI diesel

5.12 Estimates of Northern Ireland diesel and petrol consumption are based on the average consumption per vehicle in Great Britain. Details of the methodology are given in the separate 'Methodological Annex'.

5.13 The estimates for Northern Ireland relate to the non-UK duty paid market, rather than the illicit market. The non-UK duty paid market includes both the illicit market and legitimate cross-border shopping consumed in Northern Ireland. Up to now it has been difficult to separate these two markets as HMRC did not have a robust estimate of cross-border shopping between Northern Ireland and the Republic of Ireland. However, exploratory modelling has been carried out which has given an indication of the cross-border shopping element.

5.14 The central estimate is best interpreted as an indicator of long-term trends in the non-UK duty paid market share rather than a precise estimate of the level or year-to-year changes. The confidence intervals indicate the potential size of chance fluctuations in the estimates are due to sampling error. They do not take account of any systematic tendency to over- or under-estimate the size of the non-UK duty paid market that might arise from the modelling assumptions.

Revisions

5.15 Some elements of the 2011-12 estimates have been produced using forecasts. Therefore, estimates for 2011-12 should be considered provisional.

5.16 The changes to the input data and methodology for the Great Britain models affect the average consumption in Great Britain, which is an input for the Northern Ireland models. Consequently the time series for Northern Ireland has been revised.

5.17 As in the case of GB diesel, an element of uncertainty has been introduced to NI diesel consumption to reflect diesel that is wasted or unused and diesel that is used for domestic purposes and in non agricultural machinery. Further details can be found in the 'Methodological Annex'.

Key findings for NI petrol

- For 2011-12 HMRC estimates the market share for fraudulent petrol in NI to be negligible
- The NI petrol non-UK duty paid market share is 11 per cent in 2011-12, with associated uncollected revenue of £40 million.
- The non-UK duty paid market share in NI petrol shows a generally decreasing trend from 18 per cent in 2007-08 to 11 per cent in 2011-12. There is no estimate for 2009-10 due to issues with cross-border shopping.

Results and tables for NI petrol

5.18 The non-UK duty paid market includes both the illicit market and legitimate cross-border shopping consumed in Northern Ireland.

5.19 The non-UK duty paid market share could not be estimated in 2009-10 because there was a significant change in cross-border shopping behaviour between Northern Ireland and the Republic of Ireland. The reason for this change in behaviour is thought to be the low price differential between the two countries throughout 2009-10.

5.20 Further tables on NI petrol, showing a breakdown of UK market share and volumes can be found online in the 'Measuring Tax Gaps 2013' tables in Excel.

Table 5.3: NI petrol: Non-UK duty paid market share and associated uncollected revenue[1]

	2007-08	2008-09	2009-10[2]	2010-11	2011-12[3]
Cross-border shopping + Illicit Market Shares (per cent)[4]					
Upper estimate	22%	19%	No data	16%	15%
Mid-point estimate	18%	15%	No data	12%	11%
Lower estimate	14%	10%	No data	7%	6%
Associated uncollected revenue (£ million)[5,6]					
Upper estimate	80	70	No data	60	60
Mid-point estimate	60	50	No data	50	40
Lower estimate	50	30	No data	30	20

1 Figures for previous years have been revised.
2 The non-UK duty paid market share could not be estimated in 2009-10 due to a significant change in cross-border shopping behaviour.
3 Figures for 2011-12 are provisional.
4 Figures independently rounded to the nearest 1 per cent.
5 Includes both duty and VAT.
6 Figures independently rounded to the nearest £10 million.

Methodology and data issues for NI petrol

5.21 Estimates of Northern Ireland diesel and petrol consumption are based on the average consumption per vehicle in Great Britain. Details of the methodology are given in the separate 'Methodological Annex'.

5.22 The estimates for Northern Ireland relate to the non-UK duty paid market, rather than the illicit market.

5.23 The central estimate is best interpreted as an indicator of long-term trends in the non-UK duty paid market share rather than a precise estimate of the level or year-to-year changes.

5.24 To produce a NI non-UK duty paid estimate, the cross-border shopping of Republic of Ireland residents must be removed from the clearances to be consistent with the estimate of total consumption of petrol for NI residents.

5.25 The reason for the change in behaviour in 2009-10 is thought to be that the price differential between the two countries was at a low level throughout that time. This meant that there was very little incentive for Northern Ireland residents to buy their fuel in the Republic of Ireland, leading to lower than normal levels of cross-border shopping. For some months, petrol was less expensive in Northern Ireland than in the Republic of Ireland, which gave the residents of the Republic of Ireland an incentive to buy their petrol in Northern Ireland, leading to negative cross-border shopping.

Revisions

5.26 Some elements of the 2011-12 estimates have been produced using forecasts. Therefore, estimates for 2011-12 should be considered provisional.

5.27 The changes to the input data and methodology for the Great Britain models affect the average consumption in Great Britain, which is an input for the Northern Ireland models. Consequently the time series for Northern Ireland has been revised.

Methodology and data issues for Petroleum Revenue Tax

5.28 An illustrative indicator of the tax gap from Petroleum Revenue Tax (PRT) has been produced using the expert opinion of PRT specialists. Given the narrowly defined extent of the tax (limited to oil-producing fields developed before April 1993), the small number of businesses involved and HMRC's compliance approach of six-monthly reviews, a range of between 1 per cent and 3 per cent of receipts has been used to calculate an illustrative tax gap. This produces an estimate of between £20 million and £60 million in 2011-12.

Key findings for Petroleum Revenue Tax

The illustrative tax gap for 2011-12 is £40 million.

Table 5.4: Petroleum Revenue Tax – illustrative tax losses (£ million)

	2007-08	2008-09	2009-10	2010-11	2011-12
Revenue losses					
Illustrative upper estimate	45	80	30	45	60
Illustrative mid-point	30	50	20	30	40
Illustrative lower estimate	15	30	10	15	20

6 – Income Tax gaps, including NICs and Capital Gains Tax

Key findings

- In 2011-12 the total estimated tax gap for Income Tax, National Insurance Contributions and Capital Gains Tax (IT, NICs and CGT) is £15.3 billion, which is broadly consistent with the revised figure for 2010-11. The new 2011-12 estimate consists of:
  - £5.2 billion from individuals and large partnerships in Self Assessment (SA)
  - £3.8 billion from employers (PAYE)
  - £2.0 billion from avoidance
  - £4.3 billion from the hidden economy.
- The tax gap for IT, NICs and CGT accounts for 44 per cent of the overall tax gap in 2011-12.

Individuals and partnerships in Self Assessment (excluding large partnerships)

- In 2011-12 the total tax gap from individuals in Self Assessment of £4.6 billion is 17 per cent of SA tax liabilities (Table 6.1).
- The tax gap from business taxpayers contributes the majority of the total SA tax gap, with non-business taxpayers accounting for just £0.3 billion out of the £4.6 billion total tax gap (Table 6.2).
- The proportion of SA taxpayers who under-declared their tax liabilities has fallen slightly from 29 per cent in 2005-06 to 27 per cent in 2009-10 (Table 6.3).
- Business taxpayers are more than twice as likely to under-declare their tax liabilities than non-business taxpayers (37 per cent compared to 14 per cent – Tables 6.4 and 6.5).

Large partnerships in Self Assessment

- In 2011-12 the total tax gap from large partnerships of £0.6 billion is 10 per cent of liabilities (Table 6.6).

Small and medium-sized employers (SMEs)

- In 2011-12 the total tax gap from SMEs of £1.7 billion is 1.9 per cent of SME PAYE tax liabilities (Table 6.7).
- The proportion of small and medium-sized employers failing to correctly operate their PAYE scheme has decreased from 41 per cent in 2005-06 to 26 per cent in 2010-11 (Table 6.8).

Large employers

- In 2011-12 the total tax gap from large employers is 1.5 per cent of large employer PAYE liabilities or £2.2 billion (Table 6.9).

Hidden economy

- The direct tax hidden economy estimate is £4.3 billion in 2011-12. This consists of ghosts (£1.3 billion), moonlighters (£1.9 billion) and PAYE individuals not in Self Assessment (£1.0 billion).

Avoidance

- The avoidance tax gap for IT, NICs and CGT for 2011-12 is £2.0 billion.
- The overall estimate for the avoidance tax gap, which also includes VAT and Corporation Tax avoidance, is £4.0 billion (Figure 1.6).

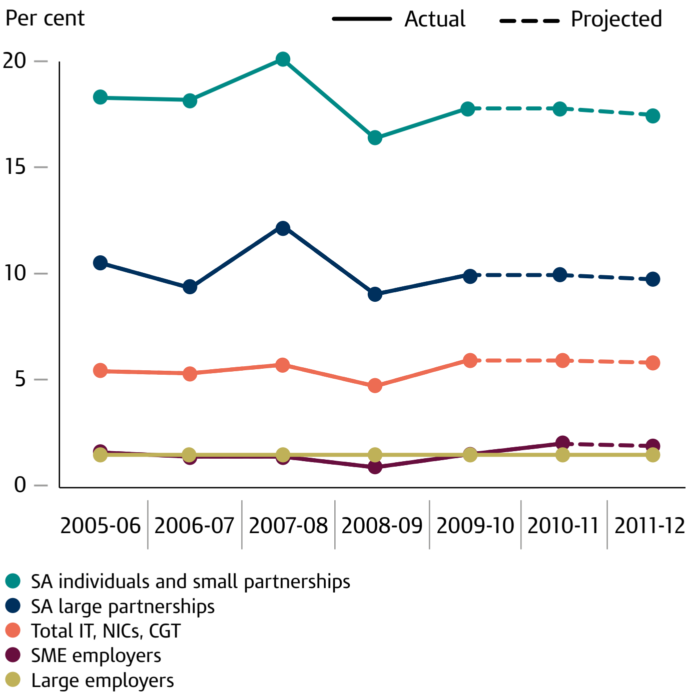
Introduction

6.1 The overall tax gap for Income Tax, NICs and CGT is estimated in a number of different ways. The estimates for small and medium-sized businesses, individuals and small partnerships, and SME employers are all derived from the results of random enquiry programmes. The tax gaps for large partnerships and large employers are illustrative tax gaps produced by assuming the tax at risk will represent a similar proportion of liabilities to all other SA or employer taxpayers, as shown by the results of the random programme.

6.2 Figure 6.1 shows that the tax gap estimate as a proportion of total liabilities has stayed broadly stable at between 5 per cent and 6 per cent from 2005-06 to 2011-12, with the exception of a slight dip below 5 per cent in 2008-09. The tax gap as a proportion of liabilities is larger for those in SA than for employers, and also shows more variation from year to year. The trends for both SME and large employers are more stable, with the percentage around 1 per cent to 2 per cent across all the years shown.

6.3 As the total liabilities for SA represents less than 15 per cent of the total liabilities for IT, NICs and CGT, the trends in SME and large employers have greater influence on the total IT, NICs and CGT trend.

Figure 6.1: SA individuals, SA large partnerships, SME employers and large employers gap as a proportion of liabilities, 2005-06 to 2011-12



Results and tables for individuals in Self Assessment (SA)

6.4 Estimates of tax gaps from incorrect returns in this section come from the Income Tax Self Assessment random enquiry programme and data on compliance yield and non-payment. The latest programme data available is for the 2009-10 tax year, with subsequent years projected forward based on the year on year change in liabilities.

6.5 Table 6.1 shows estimated tax gaps for SA taxpayers (excluding large partnerships) due to incorrect returns for the tax years 2005-06 to 2011-12. The SA tax gap as a proportion of liabilities has remained broadly stable over this period, with a high of 20 per cent in 2007-08 followed by a low of 16 per cent in 2008-09. Non-payment has remained broadly stable, staying between £0.2 billion and £0.3 billion.

Table 6.1: Self Assessment tax gap (excluding large partnerships) (£ billion)[1]

	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12
Under-declared liabilities due to incorrect returns							
Point estimate	5.2	5.6	7.1	4.9	5.5	5.2	5.2
Lower estimate	2.6	2.6	3.2	2.3	2.6	2.4	2.4
Upper estimate	9.6	10.4	14.0	9.2	10.2	9.6	9.6
Compliance yield[2]	0.6	0.6	0.9	0.9	0.9	0.8	0.8
Non-payment	0.2	0.2	0.3	0.2	0.3	0.3	0.2
Net total tax gap							
Point estimate	4.8	5.2	6.5	4.2	4.9	4.6	4.6
Lower estimate	2.1	2.2	2.6	1.6	2.0	1.9	1.8
Upper estimate	9.1	10.1	13.4	8.6	9.6	9.1	9.0
Total theoretical tax liabilities	26.3	28.8	32.5	25.9	27.7	26.2	26.2
Proportion of liabilities	**18%**	**18%**	**20%**	**16%**	**18%**	**18%**	**17%**

1 Figures rounded to the nearest £0.1 billion. As a result components may not appear to sum.
2 By period of settlement of enquiry.

6.6 Table 6.2 shows estimated tax gaps for SA taxpayers (excluding large partnerships) split by business and non-business taxpayers for the tax years 2005-06 to 2011-12. Business taxpayers accounted for around 90 per cent of the net total tax gap between 2005-06 and 2011-12, except for 2007-08 when the level decreased to 78 per cent due to a significant rise in the tax gap from non-business taxpayers.

Table 6.2: Self Assessment tax gap by type of taxpayer (£ billion)[1]

	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12
Under-declared liabilities due to incorrect returns							
Net total tax gap	4.8	5.2	6.5	4.2	4.9	4.6	4.6
Business Taxpayers	4.2	4.8	5.1	3.8	4.5	4.3	4.3
Non-Business Taxpayers	0.6	0.4	1.4	0.4	0.4	0.3	0.3

1 Figures rounded to the nearest £0.1 billion. As a result components may not appear to sum.

6.7 Table 6.3 shows the estimated proportion of incorrect SA returns leading to under-declaration of liabilities has slightly decreased from 29 per cent to 27 per cent between the tax years 2005-06 to 2009-10. This decrease is driven by a fall in the proportion of returns where the annualised under-declared liability was less than £500 from 14 per cent to 11 per cent.

Table 6.3: Self Assessment returns with under-declared tax liability (per cent)[1]

	2005-06	2006-07	2007-08	2008-09	2009-10
Proportion	29%	29%	29%	27%	27%
of which, under-declared liability per annum					
£1 to £500	14%	14%	13%	13%	11%
£501 to £1,000	6%	5%	6%	5%	5%
over £1,000	9%	9%	10%	9%	11%

1 Figures rounded to the nearest 1 per cent. As a result components may not appear to sum.

6.8 The proportion of under-declarations shown in Table 6.3 can be further split by business and non-business taxpayers. Table 6.4 shows the estimated proportion of incorrect SA returns leading to under-declaration of liabilities for the tax years 2005-06 to 2009-10 for business taxpayers only. The proportion of incorrect SA returns from business taxpayers has fallen from 49 per cent to 37 per cent between the tax years 2005-06 to 2009-10. This reduction is driven by falls across all levels of under-declarations.

Table 6.4: Business taxpayers: Self Assessment returns with under-declared tax liability (per cent)[1]

	2005-06	2006-07	2007-08	2008-09	2009-10
Proportion	49%	44%	44%	39%	37%
of which, under-declared liability per annum					
£1 to £500	21%	19%	16%	16%	14%
£501 to £1,000	10%	8%	10%	9%	7%
over £1,000	18%	16%	18%	14%	16%

1 Figures rounded to the nearest 1 per cent. As a result components may not appear to sum.

6.9 Table 6.5 shows the estimated proportion of incorrect SA returns leading to under-declaration of liabilities for non-business taxpayers has stayed broadly stable between the tax years 2005-06 to 2009-10. The level of incorrect SA returns with under-declared tax liabilities is lower for non-business taxpayers than business taxpayers because the majority of Income Tax paid by these non-business taxpayers is deducted at source under PAYE, leading to lower levels of incorrect SA returns.

Table 6.5: Non-business taxpayers: Self Assessment returns with under-declared tax liability (per cent)[1]

	2005-06	2006-07	2007-08	2008-09	2009-10
Proportion	14%	15%	16%	15%	14%
of which, under-declared liability per annum					
£1 to £500	10%	10%	10%	9%	8%
£501 to £1,000	2%	3%	2%	2%	2%
over £1,000	2%	3%	4%	4%	4%

[1] Figures rounded to the nearest 1 per cent. As a result components may not appear to sum.

Results and tables for large partnerships in Self Assessment

6.10 Large partnerships are not covered by the random enquiry programme and therefore an illustrative tax gap is produced by assuming the tax at risk will represent a similar proportion of liabilities to all other SA taxpayers, as shown by the results of the random programme.

6.11 Table 6.6 shows the tax gap for large partnerships in Self Assessment is broadly in line with previous years' estimates at £0.6 billion in 2011-12. This follows the spike in 2007-08 to £1.1 billion, which was in line with the spike seen in total SA tax liabilities for that year.

Table 6.6: Tax gap for large partnerships in Self Assessments (£ billion)[1]

	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12
Under-declared liabilities due to incorrect returns							
Point estimate	0.7	0.8	1.3	0.8	0.8	0.8	0.8
Lower estimate	0.6	0.7	1.0	0.6	0.7	0.7	0.7
Upper estimate	0.8	0.9	1.6	0.9	1.0	0.9	0.9
Compliance yield[2]	0.1	0.2	0.3	0.3	0.2	0.2	0.2
Non-payment	0.0	0.1	0.1	0.1	0.1	0.1	0.1
Net total tax gap							
Point estimate	0.6	0.6	1.1	0.6	0.7	0.6	0.6
Lower estimate	0.5	0.5	0.8	0.5	0.5	0.5	0.5
Upper estimate	0.7	0.8	1.4	0.8	0.8	0.8	0.8
Total theoretical tax liabilities	5.7	6.8	9.0	6.7	6.8	6.5	6.4
Proportion of liabilities	**10%**	**9%**	**12%**	**9%**	**10%**	**10%**	**10%**

[1] Figures rounded to the nearest £0.1 billion. As a result components may not appear to sum.
[2] By period of settlement of enquiry.

Results and tables for small and medium-sized employers

6.12 Estimates of tax gaps from incorrect returns in this section come from the Employer Compliance random enquiry programme and data on compliance yield and non-payment. The latest programme data available is for the 2010-11 tax year, with 2011-12 projected forward based on the trend in liabilities.

6.13 Table 6.7 shows estimated tax gaps for small and medium-sized employers for the tax years 2005-06 to 2011-12 has remained at around 1 per cent to 2 per cent of liabilities, with a low of 0.9 per cent in 2008-09. Non-payment has increased from a low of £0.5 billion in 2008-09 to £1.0 billion in 2011-12 which has increased the net total tax gap.

Table 6.7: Tax gap for small and medium-sized employers (£ billion)[1]

	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12
Under-declared liabilities due to incorrect returns							
Point estimate	0.9	0.9	1.0	0.5	0.6	1.0	1.0
Lower estimate	0.7	0.8	0.9	0.5	0.5	0.7	0.7
Upper estimate	1.0	1.0	1.2	0.6	0.7	1.3	1.3
Compliance yield[2]	0.3	0.4	0.3	0.3	0.2	0.3	0.4
Non-payment	0.7	0.7	0.6	0.5	0.9	1.0	1.0
Net total tax gap							
Point estimate	1.3	1.1	1.3	0.8	1.2	1.7	1.7
Lower estimate	1.1	1.0	1.1	0.7	1.1	1.4	1.4
Upper estimate	1.4	1.2	1.4	0.8	1.3	2.0	1.9
Total theoretical tax liabilities	76.9	82.3	91.1	86.9	81.4	85.0	86.3
Proportion of liabilities	**1.6%**	**1.4%**	**1.4%**	**0.9%**	**1.5%**	**2.0%**	**1.9%**

1 Figures rounded to the nearest £0.1 billion. As a result components may not appear to sum.
2 By period of settlement of enquiry.

6.14 Table 6.8 shows the estimated proportion of employers failing to meet their obligations in respect of operating a PAYE scheme for the tax years 2005-06 to 2010-11. The proportion of employers where the annualised under-declared liability was more than £0 but less than £1,000 fell from 25 per cent to 14 per cent over the period; the proportion where annualised under-declared liabilities exceeded £1,000 fell from 17 per cent to 12 per cent.

Table 6.8: Small and medium-sized employers: employers found to be failing to meet PAYE scheme obligations (per cent)[1]

	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
Proportion	41%	40%	39%	34%	27%	26%
of which, under-declared liability per annum						
£1 to £1,000	25%	23%	23%	18%	14%	14%
over £1,000	17%	18%	17%	16%	13%	12%

1 Figures rounded to the nearest 1 per cent. As a result components may not appear to sum.

Results and tables for large employers

6.15 Large employers are not covered by the random enquiry programme and therefore an illustrative tax gap is produced by assuming the tax at risk will represent a similar proportion of liabilities to SME employers, as shown by the results of its random enquiry programme.

6.16 Table 6.9 shows estimated tax gaps for large employers has gradually increased in line with total liabilities between the tax years 2005-06 to 2011-12.

Table 6.9: Estimated tax gap for large employers (£ billion)[1]

	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12
Under-declared liabilities due to incorrect returns							
Point estimate	1.8	1.9	1.7	1.7	1.5	1.6	1.6
Lower estimate	1.2	1.2	1.0	1.1	0.9	0.8	0.9
Upper estimate	2.4	2.5	2.4	2.4	2.2	2.3	2.3
Compliance yield[2]	0.1	0.1	0.1	0.1	0.2	0.3	0.3
Non-payment	0.1	0.2	0.4	0.4	0.7	0.8	0.8
Net total identified tax gap							
Point estimate	1.8	1.9	2.0	2.0	2.0	2.1	2.2
Lower estimate	1.2	1.3	1.4	1.4	1.4	1.4	1.5
Upper estimate	2.4	2.6	2.7	2.7	2.7	2.8	2.9
Total theoretical tax liabilities	124.4	132.9	137.4	136.7	137.8	144.6	146.7
Proportion of liabilities	**1.5%**	**1.5%**	**1.5%**	**1.5%**	**1.5%**	**1.5%**	**1.5%**

1 Figures rounded to the nearest £0.1 billion. As a result components may not appear to sum.
2 By period of settlement of enquiry.

Results and tables for avoidance and hidden economy

Avoidance

6.17 The avoidance tax gap for IT, NICs and CGT for 2011-12 is £2.0 billion.

6.18 The IT, NICs and CGT avoidance tax gap is estimated using HMRC's register of information on identified avoidance schemes for individuals, trusts, partnerships and employers.

Hidden economy

6.19 The direct tax hidden economy estimate of £4.3 billion in 2011-12 is composed of three elements: ghosts, moonlighters and PAYE individuals not in Self Assessment.

Ghosts and moonlighters

6.20 The 2011-12 illustrative estimates for ghosts is £1.3 billion and for moonlighters is £1.9 billion.

PAYE individuals not in Self Assessment

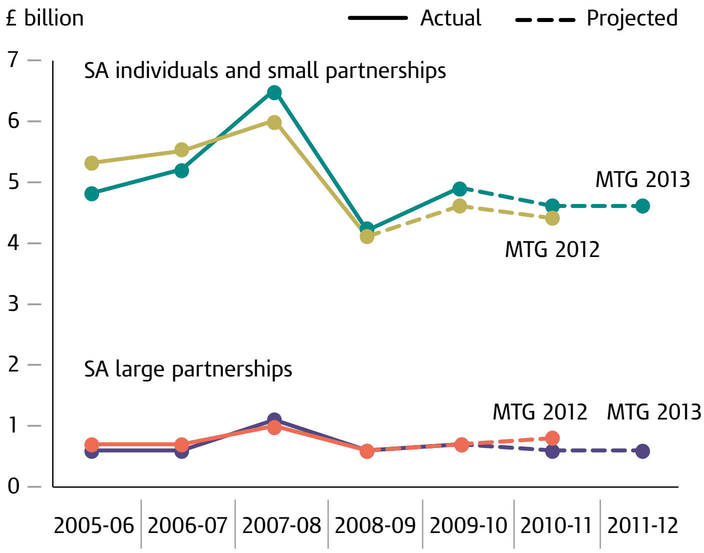
6.21 The 2011-12 illustrative estimate relating to income and capital gains of individuals taxed through PAYE but who do not receive SA returns is £1.0 billion. Estimates for 2010-11 and 2011-12 are projected from 2009-10 data in line with growth in GDP.

Revisions

6.22 Figures 6.2 and 6.3 show the published figures for this year and the equivalent published figures from MTG 2012 for IT, NICs and CGT. Revisions are as a result both of updated data and methodological changes as well as the inclusion of an additional year of data from the random enquiry programmes.

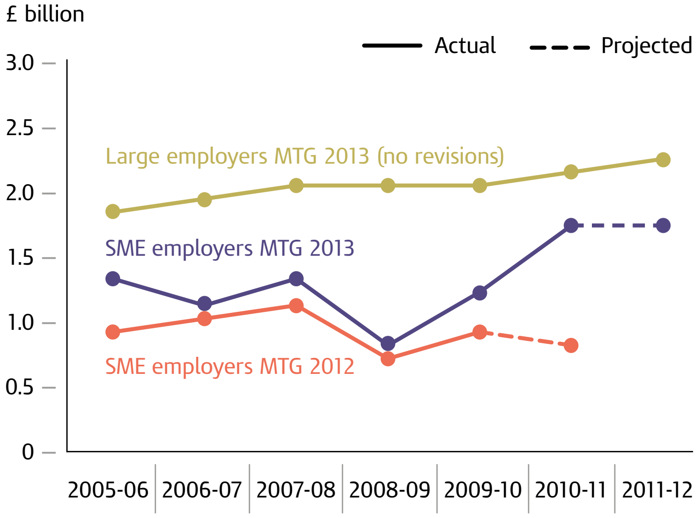
6.23 Figure 6.2 shows changes to both the SA SME and individuals and SA large partnerships. Last year's estimate for 2009-10 and 2010-11, published in MTG 2012 were projected forward from the 2008-09 estimates using the trend in estimated total SME SA tax liabilities. Now that actual data for 2009-10 is available, the estimates for 2010-11 (and 2011-12) have been projected using the latest year.

Figure 6.2: Revisions to SA individuals and small partnerships and SA large partnerships net tax gap between MTG 2012 and MTG 2013, 2005-06 to 2011-12



6.24 Figure 6.3 shows the changes to estimates for SME employers and large employers since they were last published in MTG 2012. Last year's estimate for 2010-11 was projected forward from the 2009-10 estimates using the trend in estimated total SME PAYE tax liabilities. Now that actual data for 2010-11 is available, this estimate has been revised. The large employers net tax gap estimate has not changed since last published.

Figure 6.3: Revisions to SME employers and large employers net tax gap between MTG 2012 and MTG 2013, 2005-06 to 2011-12



6.25 There are a number of revisions to earlier years, particularly in those figures for SMEs derived from the random enquiry programmes. These are driven by a number of factors including; long-running cases settling since last publication, and methodological improvements to the estimates (see methodology and data issues).

6.26 A more accurate allocation of non-payment between employers and SA has caused some significant revisions, especially in the later years. The improved allocation has led to an increase in the SME employers tax gap and reductions in the gaps for SA across all years. The largest impact on the SA individuals and small partnerships estimate was a £0.6 billion decrease in 2010-11, however this reduction was more than offset by other increases caused by updated data. The largest impact on SME employers was a £0.4 billion increase in 2010-11.

6.27 The SME employers estimate for 2010-11 has been revised to £1.7 billion from £0.8 billion published in MTG 2012. In addition to the increase caused by the reallocation of non-payment detailed above, the inclusion of actual data for 2010-11 has also caused the estimate to increase significantly.

Methodology and data issues

Overview

6.28 The IT, NICs and CGT components of the tax gap are estimated using departmental sources, such as surveys, administrative and operational data. Estimation methods are based on compliance activity which can, in some cases, take years to complete. Therefore the resulting tax gap estimates typically apply to periods before 2011-12. This has two consequences:

- In order to produce a tax gap for years which have not yet been estimated, the latest available estimate is projected forward. The projections are made using the change in the tax liabilities for the relevant tax. Using tax liabilities ensures that our projections reflect changes to tax rates and taxable income, and projects a stable level of underlying compliance. Hidden economy components are projected forward using growth in GDP or wages and salaries rather than tax liabilities, as there is no directly relevant data series to base predictions on.
- Estimates for earlier years have been revised since previously published as a result of the inclusion of additional data from compliance checks that have since been completed.

6.29 Methods used differ between taxes, according to the type of non-compliance and the type of taxpayer involved. The main methods used to estimate tax gaps for direct taxes are random enquiries, data matching and risk registers. In addition, where robust methodologies have not yet been developed, an illustrative estimate of the tax gap is given based on expert opinion or derived by selecting the nearest equivalent measured gap.

Table 6.10 Summary of methods by tax gap estimate

Tax gap	Population section	Methods used
Employers (IT and NICs on employment income and tax on occupational pensions)	Employers with up to 250 employees (except where the employer is part of a complex group).	Random enquiries
	Employers that are dealt with by the Large Business Service or are within the Local Compliance Large and Complex population.	Illustrative estimate
SA (IT, NICs and CGT)	'Business taxpayers' consisting of self-employed taxpayers and partnerships with up to four partners who receive notices to file an SA return.	Random enquiries
	'Non-business taxpayers' consisting of individuals without business income and trusts who receive notices to file an SA return.	Random enquiries
	Partnerships with five or more partners who receive notices to file an SA return.	Illustrative estimate
Avoidance (IT, NICs and CGT)	Individuals, trusts, partnerships and employers.	Risk register
Hidden economy	Employees and pensioners who are taxed through PAYE but are outside SA.	Data matching
	Ghosts	Illustrative estimate
	Moonlighters	Illustrative estimate

Random enquiries

6.30 Random enquiry programmes involve samples of taxpayers being selected at random and their returns being subjected to full enquiries by HMRC officers. The results of the random enquiry programmes show the proportion of taxpayers under-reporting their tax liabilities and the corresponding amount of additional tax due. These results can be used to produce an estimate for the amount of under-declared tax liability for the whole population, as the enquiries are randomly selected and form a representative sample. A proportion of the under-declared liabilities will be recovered as a result of HMRC compliance activity. This is called compliance yield and is subtracted from the estimate of under-declared liabilities.

6.31 The random enquiry programmes will not identify all incorrect returns or the full scale of tax gaps, especially where independent information from third parties is not available to verify the data supplied by the taxpayer. This means that tax gap estimates produced through random enquiries will underestimate the full extent of the tax gap.

6.32 The Internal Revenue Service (IRS) in the United States (US) has tackled this problem by using a range of 'multipliers' to make adjustments for non detection[C]. These multipliers are generated through supplementary studies on particular tax return entries, together with econometric analysis of non-detection rates across IRS examiners.

6.33 Across all of the random enquiry programmes the way that cases with very large under-reported tax liabilities are treated has changed. Previously these large 'outliers' were excluded from the analysis because when included in full they are too influential and distort the analysis. However, for this publication these large cases are now included in the analysis, but the level of their under-reported liabilities has been capped to reduce their impact on the overall results. Including these capped cases in the analysis will increase the estimates in the years where they were previously excluded. However, the impact is somewhat offset by capping cases which were previously uncapped and included in the analysis. This is because they are below the threshold for outliers, but are higher than the level set for capping. This will have reduced the overall results. (See 'Methodological Annex' for more details).

[C] James Andreoni, Brian Erard and Jonathan Feinstein (1998) 'Tax Compliance', Journal of Economic Literature, Vol. 36, No. 2. (Jun., 1998), pp. 818-860

Non-payment

6.34 If appropriate the tax gap estimates include a measure of associated losses from non-payment of tax by the relevant type of taxpayer. The estimates of non-payment for direct taxes come from HMRC's financial statements and represent amounts written off or remitted, that is, debts that are not collectable. Direct tax debts that are later paid do not form part of the direct tax gap, although payment will be deferred. Due to timing effects the amounts written off during a tax year will not all relate to liabilities arising during that year.

6.35 There has been an improvement in the methodology used to allocate the split of non-payments between SA and employers. This improvement has caused a lower allocation to SA and a corresponding higher allocation to employers. These more accurate splits feed into the net tax gap figures, with the greatest effect being seen in 2010-11.

Large employers

6.36 Larger employers, those with 250 or more employees, including those dealt with by the Large Business Service and employers which are part of a complex group, are not covered by the Employer Compliance random enquiry programme and therefore an alternative methodology is required to produce an indicator of the associated tax gap. An illustrative estimate can be produced by assuming that the tax at risk will represent a similar proportion of liabilities to SME employers, as shown by the results of the random programme.

Large partnerships

6.37 Partnerships with five or more partners are not covered by the SA random enquiry programme and therefore an alternative methodology is required to estimate the associated tax gap. An illustrative estimate can be produced by assuming that the tax at risk will represent a similar proportion of liabilities to all other SA taxpayers, as shown by the results of the random programme.

Avoidance

6.38 The IT, NICs and CGT avoidance tax gap is estimated using HMRC's register of information on identified avoidance schemes for individuals, trusts, partnerships and employers. This gives an estimate for the total amount of tax that is considered to be at risk whilst avoidance schemes are in operation. The estimates reflect the legal framework in place at the time and will not include any subsequent changes to the tax law to prevent further use of avoidance schemes.

6.39 Annual estimates are derived by dividing the total tax under consideration with the average number of years that schemes are assumed to operate. The main source of error in these estimates is that HMRC may not identify all risks – which will lead to an underestimation of the tax gap. It is difficult to quantify the extent to which this source of error impacts upon the estimates.

6.40 The 2010-11 estimate of the IT, NICs and CGT tax gap in 'Measuring Tax Gaps 2012' included an uplift for unidentified risks based on management judgment. However, following a recent HMRC review of the register of avoidance schemes no uplift was deemed appropriate for the 2011-12 estimate.

Hidden economy

6.41 The direct tax hidden economy estimate is composed of three elements:

- PAYE individuals not in Self Assessment
- Ghosts
- Moonlighters.

PAYE individuals not in Self Assessment

6.42 A tax gap estimate is produced for employees and pensioners taxed under PAYE who do not receive Self Assessment returns and have not returned details of additional taxable income.

6.43 In last year's publication an estimate for 2010-11 was projected from a new methodology that produced an estimate for 2009-10. In the absence of updated data, the estimate for 2011-12 is also projected from the 2009-10 estimate.

6.44 By matching data supplied by third parties to a sample of HMRC PAYE records, it has been possible to produce an estimate of the tax gap relating to income and capital gains of individuals taxed through PAYE but who do not receive SA returns. Several sources of income were investigated, such as income from lettings, bank and building society interest and capital gains. Where a difference was found between income in the third party data and the tax records, the tax that should have been paid on this income, if any, was then calculated and identified as the tax gap. The results from the sample were then grossed to produce an estimate of the overall tax gap for all employees and pensioners taxed through PAYE who are outside SA.

6.45 The limitations associated with the results of this exercise relate to the coverage of the third party data used to establish evidence of additional undeclared income. Not all potential sources of income could be investigated due to availability of data and the investigation of some sources was limited by the completeness of the information. The resulting estimate should therefore be interpreted broadly as a lower limit for the true scale of the tax gap relating to this group of taxpayers.

Ghosts and moonlighters

6.46 'Ghosts' are individuals who receive income from employment or self-employment but are not known to HMRC because they and/or their employers fail to declare their earnings. Ghosts are not accurately recorded by any government agency or survey and therefore any estimate as to their number or the consequential loss of duty is approximate.

6.47 'Moonlighters' are individuals who pay tax on their main job through PAYE, but who fail to declare earnings from a second job or additional income from self-employment.

6.48 Using a series of assumptions, it has been possible to produce illustrative estimates of the tax gap from moonlighters and ghosts. Due to the extent of the assumptions used to produce this estimate and the inherent uncertainties in the methodologies, this estimate has a large margin of error and should be treated with due caution.

7 – Corporation Tax gaps

Key findings for Corporation Tax

- The estimated total net tax gap for Corporation Tax is £4.7 billion in 2011-12 (also £4.7 billion in 2010-11), equivalent to 13 per cent of the overall tax gap.
- The tax gap from Corporation Tax is estimated to be 10 per cent of the estimated Corporation Tax liabilities in both 2010-11 and 2011-12.

Key findings for large businesses

- In 2011-12 the Corporation Tax gap for large businesses, which is comprised of businesses managed by the Large Business Service (LBS) and businesses managed by Local Compliance Large and Complex (L&C), is estimated to be 8 per cent of large business Corporation Tax liabilities.
- The LBS element of the large business Corporation Tax gap is projected to be 6 per cent of LBS Corporation Tax liabilities and the L&C element is estimated to be 12 per cent of L&C Corporation Tax liabilities in 2011-12.
- The projected LBS Corporation Tax gap is £1.4 billion for both 2010-11 and 2011-12. The projections are based on the change in the LBS Corporation Tax receipts, which is applied to the new estimate for 2009-10.
- The 2009-10 estimate of the LBS Corporation Tax gap is £1.1 billion which is in line with the projected estimate for 2009-10 published in 'Measuring Tax Gaps 2012' (MTG 2012).
- The number of LBS Corporation Tax avoidance risks and technical risks subject to litigation decreased by 31 per cent between 2008-09 and 2009-10.
- The average tax under consideration (TuC) per LBS avoidance risk and technical risks subject to litigation decreased from £9.5 million in 2008-09 to £7.5 million in 2009-10.
- The illustrative tax gap estimate from business managed by L&C has decreased from £1.3 billion in 2010-11 to £0.9 billion in 2011-12.

Key findings for small and medium-sized businesses

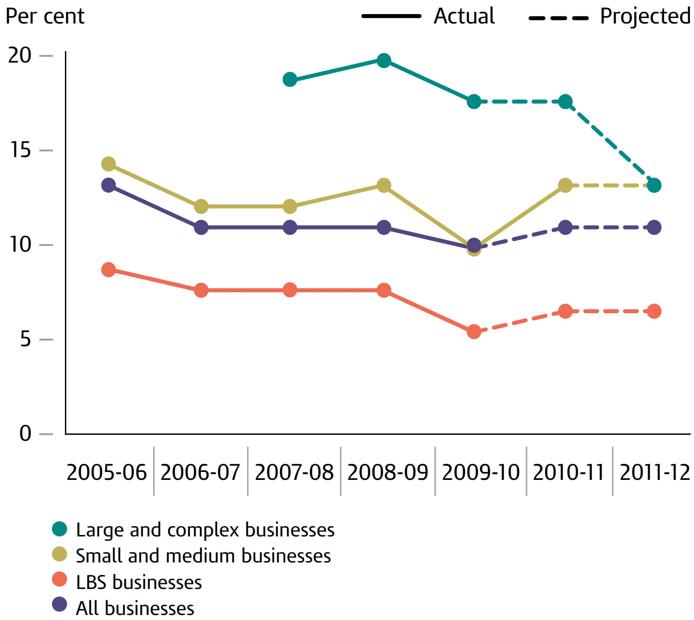
- The Corporation Tax gap for small and medium-sized businesses (SMEs) is estimated to be 12 per cent of SME Corporation Tax liabilities in 2011-12.
- Between 2005-06 and 2011-12 the tax gap as a percentage of liabilities has stayed broadly stable at between 11 per cent and 13 per cent, with the exception of a dip to 9 per cent in 2009-10.
- The projected Corporation Tax gap for SMEs is £2.3 billion in 2011-12. This is £0.3 billion higher than 2010-11. The projection is based on the change in estimated total SME Corporation Tax liabilities.
- The 2010-11 estimate of £2.0 billion has been revised up by £0.6 billion from the projected estimate for 2010-11 published last year.
- The proportion of SMEs submitting an incorrect return leading to a loss of tax declined from 42 per cent in 2005-06 to 26 per cent by 2009-10, before rising to a provisional estimate of 36 per cent in 2010-11.

Introduction

7.1 The tax gap for Corporation Tax is estimated separately for SMEs and large businesses. The large business estimates are subdivided into two categories; 'Large Business Service' (LBS) and 'Large and Complex' (L&C). These are the two divisions of HMRC that manage the relationship with these businesses. The LBS handles the largest businesses, approximately 800 groups, and L&C oversees a much larger number of comparatively smaller businesses, approximately 9,500. In Chapter 1, estimates for LBS and L&C are combined under the heading 'Large business'.

7.2 Figure 7.1 shows that the tax gap estimate as a proportion of total Corporation Tax liabilities has stayed broadly stable, declining slightly from 12 per cent in 2005-06 to 10 per cent in 2011-12 with the exception of 9 per cent in 2009-10. The overall trend masks some differences in the estimate between businesses of different sizes. Businesses managed by LBS exhibit a lower percentage tax gap compared with smaller businesses, perhaps due to the scrutiny of Customer Relationship Managers who closely mark the largest businesses. The Corporation Tax estimate for SME businesses follows a similar trend to both LBS and overall, with the exception of 2009-10 where the dip in the tax gap estimate was more pronounced. Given that the L&C tax gap estimate is derived from an illustrative methodology based on the LBS methodology, care should be taken in interpreting the L&C estimate.

Figure 7.1: Corporation Tax gap as a proportion of liabilities, 2005-06 to 2011-12



Results and tables for the Large Business Service

7.3 The 2011-12 large business Corporation Tax gap estimates are derived from HMRC operational data relating to accounting periods ending in 2009-10 as this is the latest year of available information (see Table 7.1). The 2009-10 estimate of the LBS Corporation Tax gap is £1.1 billion, in line with the projected estimate published last year and £0.6 billion lower than the revised 2008-09 estimate. The fall between 2008-09 and 2009-10 is likely to have been driven by the impact of the UK recession starting in 2008[D] which led to a 14 per cent fall in corporate profits. Reduced profits[E] or the availability of losses would have reduced both the appetite for avoidance and the amount of risk. This is reflected in the figures presented here:

- The number of avoidance risks and technical risks subject to litigation identified fell from 323 in 2008-09 to 223 in 2009-10 (31 per cent).
- The average tax under consideration (TuC) from avoidance risks and technical risks subject to litigation decreased from £9.5 million to £7.5 million between 2008-09 and 2009-10 (see Table 7.2).
- The total TuC from avoidance risks and technical risks subject to litigation decreased 43 per cent (from £3.7 billion in 2008-09 to £2.1 billion in 2009-10) (see Figure 7.2). Over the same period the compliance yield from these types of risks fell (from £2.0 billion to £1.0 billion or 48 per cent).

7.4 The overall fall in the number of risks from 1,069 to 812 between 2008-09 and 2009-10 and the increase in their average value from £5.1 million to £5.5 million is consistent with the LBS strategy to focus resources on higher yielding risks[F]. The estimates also suggest a longer-term shift in the types of risks being dealt with by LBS; from avoidance risks and technical risks subject to litigation to technical risks not subject to litigation. TuC from risks not subject to litigation rose from 35 per cent of all risks in 2005-06 (£2.3 billion of £6.8 billion TuC) to 57 per cent in 2009-10 (£2.8 billion of £4.9 billion TuC). This, along with the increase from £1.7 million to £4.8 million in the average value for these risks over the five-year period, appears to indicate a move away from artificial avoidance and that issues have been resolved satisfactorily under HMRC's strategy (Table 7.2). The above figures are also consistent with large businesses becoming more compliant. However, it is difficult to separate and quantify this effect from the impact of the recession.

[D] The UK was in recession for the five quarters from April 2008 to June 2009. ONS (2013) 'Quarterly National Accounts – Q1 2013', June 2013. http://www.ons.gov.uk/ons/rel/naa2/quarterly-national-accounts/q1-2013/index.html

[E] See HMRC Corporation Tax statistics, Table 11.2, http://www.hmrc.gov.uk/statistics/ct-receipts.htm. Gross taxable trading profits plus other taxable income and net capital gains fell from £460 billion to £398 billion between 2008-09 and 2009-10. This figure excludes life assurance, overseas and North Sea oil companies.

[F] See 2006 Review of Links with Large Business; http://www.hmrc.gov.uk/large-business/review-outcomes.htm

Table 7.1: Estimated Corporation Tax gap for LBS groups: accounting periods ending in 2005-06 to 2011-12 (£ billion)

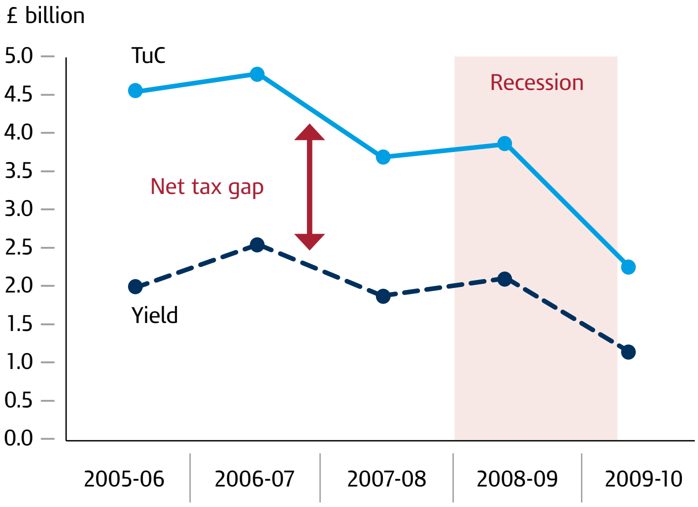
	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11[1]	2011-12[1]
Total number of risks[2,3]	**1,942**	**1,473**	**1,247**	**1,069**	**812**		
Number of technical risks not subject to litigation	1,390	1,012	876	746	589		
Number of avoidance risks and technical risks subject to litigation	552	461	371	323	223		
Total Tax under Consideration (TuC)[4,5]	**6.8**	**7.5**	**7.1**	**6.1**	**4.9**	N/A	N/A
TuC from technical risks not subject to litigation	2.3	2.9	3.5	2.4	2.8		
TuC from avoidance risks and technical risks subject to litigation	4.4	4.7	3.6	3.7	2.1		
Compliance yield[6]	1.9	2.4	1.8	2.0	1.0		
Tax gap[7]	**2.6**	**2.2**	**1.8**	**1.7**	**1.1**	**1.4**	**1.4**
Total theoretical liabilities[8]	**31.5**	**29.9**	**27.6**	**25.6**	**20.2**	N/A	N/A
Tax gap as a proportion of theoretical liabilities	**8%**	**7%**	**7%**	**7%**	**5%**	**6%**	**6%**

1 Tax gap estimates for 2010-11 and 2011-12 are projected using factors of 1.26 and 1.25 respectively, based on the trend in Corporation Tax receipts for LBS groups. The tax gap as a proportion of liabilities for 2010-11 and 2011-12 is derived from a combination of the projected tax gap and estimated liabilities.
2 Risks may span more than one accounting period.
3 Estimates will include both risks that are being worked (open) and risks that have been settled (closed) – see Table 7.4.
4 Tax under Consideration is defined in the glossary.
5 Figures may not appear to sum due to rounding.
6 Compliance yield = the total yield from closed avoidance or litigated technical risks plus the estimated compliance yield from open avoidance risks and technical risks in litigation. Compliance yield in this table relates to a specific accounting period and therefore cannot be compared to reported compliance yield.
7 Tax gap = TuC on avoidance risks and technical risks subject to litigation minus compliance yield. This includes tax gap from risks identified or recorded in subsequent APs of £0.2 billion in 2005-06, £0.3 billion in 2006-07, £0.3 billion in 2007-08, £0.4 billion in 2008-09 and £0.3 billion in 2009-10.
8 Total theoretical liabilities = the estimated Corporation Tax liabilities from LBS groups plus the TuC on avoidance risks and technical risks subject to litigation.

7.5 Table 7.1 shows estimates of the Corporation Tax gap for LBS groups for accounting periods ending in 2005-06 to 2009-10 as at July 2013 and projected estimates for 2010-11 and 2011-12. Projections are based on the change in the Corporation Tax receipts of LBS groups (see note 1 in Table 7.1). Using tax receipts ensures that the projections reflect changes to corporate tax rates and taxable profits and assumes a stable level of underlying compliance. This is applied to the latest year's estimate to produce projections of £1.4 billion for 2010-11 and for 2011-12.

7.6 The estimated tax gap has fallen steadily from £2.6 billion in 2005-06 to £1.1 billion in 2009-10 (see Figure 7.2). As a proportion of estimated Corporation Tax liabilities the tax gap has also declined from 8 per cent to 5 per cent over the same period. The main rate of Corporation Tax was reduced from 30 per cent in 2007-08 to 28 per cent in 2008-09. Although it is difficult to quantify changes in taxpayer behaviour and compliance due to the reduction in rate, it is estimated that the rate change would lead to a fall of approximately £0.2 billion in the LBS CT tax gap estimate.

Figure 7.2: Corporation Tax gap, TuC and yield for avoidance risks and technical risks subject to litigation in LBS groups: accounting periods ending in 2005-06 to 2011-12*



* UK recession quarters taken from the revised ONS GDP estimates, ONS GDP estimates, ONS (2013) 'Quarterly National Accounts – Q1 2013'. The recession started in the 2nd quarter of 2008-09 and lasted five quarters in total.

Table 7.2: Average value of Corporation Tax risks for LBS groups: accounting periods ending in 2005-06 to 2009-10 (£ million)[1]

	2005-06	2006-07	2007-08	2008-09	2009-10
Average TuC from technical risks not subject to litigation	1.7	2.8	4.0	3.2	4.8
Average TuC from avoidance risks and technical risks subject to litigation	7.3	9.0	8.3	9.5	7.5
Average TuC from all risks	**3.3**	**4.7**	**5.3**	**5.1**	**5.5**

[1] The average value of each risk is calculated on the estimates before adjustments for risks recorded in future accounting periods because the adjustments only increase the TuC and do not produce estimates of the number of additional risks.

7.7 As shown in Table 7.3, the tax gap can be split according to the type of risk identified; into the gap due to avoidance risks and the gap due to technical risks subject to litigation. Avoidance risks contribute nearly 90 per cent of the latest tax gap estimate (£1.0 billion); this is a similar proportion to previous years. The tax gap due to technical risks subject to litigation as a proportion of the overall gap has again remained around 10 per cent of the LBS Corporation Tax gap.

Table 7.3: Estimated Corporation Tax gap for LBS groups: by type of risk and accounting periods ending in 2005-06 to 2009-10 (£ billion)[1]

	2005-06	2006-07	2007-08	2008-09	2009-10
Tax gap for avoidance risks	2.2	2.0	1.6	1.6	1.0
Tax gap for technical risks subject to litigation	0.4	0.2	0.3	0.1	0.1
Total tax gap	**2.6**	**2.2**	**1.8**	**1.7**	**1.1**

[1] Figures may not appear to sum due to rounding.

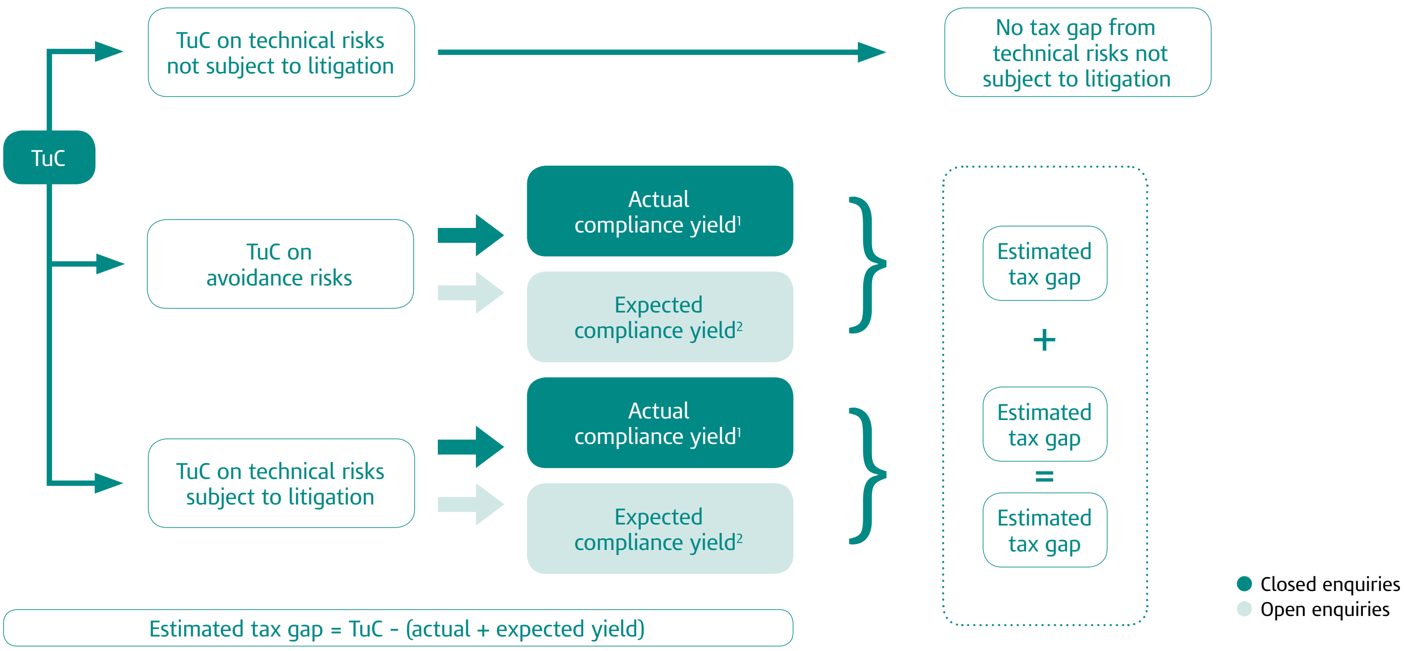
Methodology and data issues for the Large Business Service

7.8 Estimates of the Corporation Tax gap for businesses managed by the LBS come from information captured on HMRC's case management system. Where HMRC tax specialists identify risks for further consideration, the initial estimate of the tax associated with these risks is recorded on the system as the tax under consideration (TuC). TuC is not tax owed or unpaid – it is a tool which helps managers to better direct resources in order to produce the best results. Systems and the process for estimating TuC have been modified over time; current estimates may not necessarily be directly comparable to numbers published in previous years.

7.9 The LBS case management system allows the classification of risks into two broad categories; avoidance and technical risks. The avoidance category relates to the use of disclosed avoidance schemes or other suspected avoidance identified by HMRC tax specialists. Technical risks cover a wide range of risks: from cases where there is genuine uncertainty about the correct tax treatment, through mistakes to culpable errors in, or omissions from, the company tax return.

7.10 The tax gap estimates are calculated as the total TuC minus the total actual and expected compliance yield for avoidance risks and for technical risks subject to litigation. The risks will be worked until resolution in line with HMRC's Litigation and Settlement Strategy. There is assumed to be no net tax gap on technical risks settled by agreement. The flowchart at Figure 7.3 shows the process for arriving at the tax gap estimate.

Figure 7.3: The process for estimating the Corporation Tax Gap for LBS groups by category



[1] Actual compliance yield refers to closed risks only.
[2] Expected compliance yield refers to forecast yield from open risks.

7.11 Identified risks can take a number of years to be resolved. Table 7.4 shows the proportion of risks that have closed from accounting periods ending in 2005-06 to 2009-10. While all these risks will be closed over time, in the interim it is necessary to estimate the yield that will result from open enquiries. Differences between the estimated yield and the actual yield will lead to revisions to the tax gap estimates when calculated for subsequent publications. As the proportion of risks closed is lower for later years, and estimates of the yield for more risks is required, the tax gap estimates for these years are more likely to be subject to revision.

7.12 LBS reports compliance yield on a year of settlement basis, whereas tax gap estimates are based on a financial year accounting period basis. Tax gap compliance yield is calculated as the total yield from closed avoidance or litigated technical risks relating to that accounting period plus the estimated compliance yield from open avoidance risks and technical risks in litigation. LBS does not include estimated compliance yield in reported figures.

7.13 As more data have become available since the methodology was first devised, it became apparent that new risks for the accounting periods presented here can be identified in subsequent accounting periods. This information has been used to estimate an appropriate increase to the TuC to reflect these additional risks that are expected to be identified at a later point. Additional TuC will result in additional tax gap. In general, larger adjustments to TuC are made to recent accounting periods than to older accounting periods (see note 7 in Table 7.1).

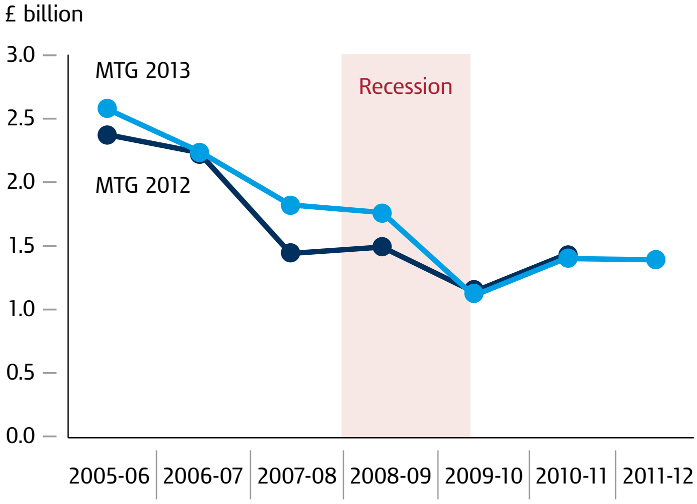
Table 7.4: Proportion of Corporation Tax risks for LBS groups closed by the number and value of the risk and accounting periods ending in 2005-06 to 2009-10 (per cent)

	2005-06	2006-07	2007-08	2008-09	2009-10
Percentage of risks closed	91	88	81	73	64
Percentage of Tax under Consideration closed	87	87	81	54	64

Revisions

7.14 Tax gap estimates for accounting periods ending before 2009-10 have been revised since the publication of MTG 2012 to account for the latest information available. The estimates this year are broadly in line with those in MTG 2012 (Figure 7.4).

Figure 7.4: Corporation tax gap for LBS groups as in 2012 and 2013 'Measuring Tax Gaps' (MTG) publications: accounting periods ending in 2005-06 to 2011-12*†‡



* UK recession quarters taken from the revised ONS GDP estimates, ONS GDP estimates, ONS (2013) 'Quarterly National Accounts – Q1 2013'.

† Estimates for MTG 2013, 2010-11 and 2011-12 are projected using factors of 1.26 and 1.25 respectively, based on the trend in Corporation Tax receipts for LBS groups.

‡ Estimates for MTG 2012, 2009-10 and 2010-11 are projected using factors of 0.76 and 0.96 respectively, based on the trend in Corporation Tax receipts for LBS groups.

7.15 Minor changes result because a more recent snapshot of the data is used each year. For example, the 2008-09 estimate of the tax gap was £1.5 billion using the April 2012 snapshot and £1.7 billion using the July 2013 snapshot. Where time has elapsed between data snapshots, differences between the initial and latest tax gap estimates are expected for the following reasons;

- More risks may be found, leading to additional TuC in any category.
- A larger proportion of the tax gap estimate will be based on actual yield numbers, replacing the values previously forecast.
- The forecast values may change as the conversion ratio calculation is based on a larger sample of closed cases.
- HMRC's judgement on the TuC of a risk or its classification as avoidance or technical may change where better information has emerged.

Limitations

7.16 The main source of error in these estimates is that HMRC may not identify all risks – which will lead to an underestimation of the tax gap. It is difficult to quantify the extent to which this source of error impacts upon the estimates.

7.17 As it can take many years to close every risk identified in a particular year, the yield expected from open cases must be forecast to be able to produce estimates of the overall tax gap. Differences between forecast yield and actual yield may lead to some degree of error, and as such, estimates are provisional until every risk is closed.

Results and tables for Large and Complex businesses

7.18 Tax gap estimates for businesses dealt with by L&C remain illustrative at present because they fall outside of the scope of the Corporation Tax Self Assessment (CTSA) random enquiry programme which is used to derive estimates of the tax gap for SMEs and, until recently, were not covered by the case management system used by LBS (as detailed above). As a result, neither the SME nor the LBS methodology can be applied to produce a tax gap estimate for L&C businesses. However, L&C began to use the same case management system as LBS in April 2012 for their customers.

Methodology and data issues for Large and Complex businesses

7.19 An illustrative estimate of the Corporation Tax gap for L&C businesses can be produced by assuming that the tax at risk will represent a similar proportion of liabilities to businesses managed by the LBS. Applying this 'tax at risk assumption' to the liabilities data produces an estimate of the tax at risk for L&C businesses for 2009-10. This estimate is projected to 2010-11 and 2011-12 based on the trend in L&C Corporation Tax liabilities. This produces illustrative estimates of under-declared liabilities for 2010-11 and 2011-12, respectively, from which compliance yield is then subtracted and an estimate of losses from non-payment is added. This produces illustrative estimates of the tax gap for L&C businesses of £1.3 billion for 2010-11 and £0.9 billion for 2011-12. The £0.4 billion reduction in the tax gap from L&C businesses is mainly due to an increase in compliance yield.

Table 7.5: Estimated Corporation Tax gap for L&C groups: accounting periods ending in 2007-08 to 2011-12 (£ billion)[1]

	2007-08	2008-09	2009-10	2010-11	2011-12
Estimated tax at risk	1.6	1.6	1.2	1.4	1.4
Compliance yield	0.3	0.3	0.3	0.3	0.6
Non-payment	0.1	0.2	0.2	0.2	0.1
Tax gap	1.4	1.4	1.1	1.3	0.9
Total theoretical liabilities[2]	8.2	7.8	7.1	8.1	7.7
Tax gap as a proportion of theoretical liabilities	**17%**	**18%**	**16%**	**16%**	**12%**

[1] Figures may not appear to sum due to rounding.
[2] Total theoretical liabilities = the estimated Corporation Tax liabilities from L&C businesses plus the estimated tax gap.

Revisions

7.20 The L&C Corporation Tax gap was estimated to be £1.2 billion for 2010-11 in 'Measuring Tax Gaps 2012'. This has been revised to £1.3 billion in 'Measuring Tax Gaps 2013' mainly due to an increase in the estimate of tax at risk. The £0.1 billion increase in tax at risk is driven by a combination of an increase in the estimate of Corporation Tax liabilities for L&C businesses that is slightly offset by a reduction in the tax at risk assumption inherited from the LBS methodology (see above paragraph).

Avoidance

7.21 Using information that HMRC holds on avoidance schemes, it is possible to estimate the Corporation Tax gap from avoidance by L&C businesses. The same methodology used to produce an estimate of the IT, NICs and CGT tax gap due to avoidance (as outlined in Chapter 6) can be applied. Using this methodology it is estimated that within the overall L&C tax gap of £0.9 billion for 2011-12, approximately £0.2 billion is due to avoidance of Corporation Tax (also £0.2 billion in 2010-11). This is an illustrative estimate only. A small uplift (less than £0.1 billion) was applied to the L&C CT avoidance estimate to account for risks that are likely to be identified in subsequent years.

Results and tables for small and medium-sized businesses

7.22 Estimates of tax gaps from incorrect returns in this section come from the CTSA random enquiry programme and data on compliance yield and non-payment. Incorrect returns are those tax returns which, upon enquiry, are found to have under-declared tax liability. The programme covers SMEs, which in this context means those businesses not managed by the LBS or L&C.

7.23 Table 7.6 shows estimated tax gaps for businesses with accounting periods ending in financial years 2005-06 to 2011-12. The projected Corporation Tax gap for SMEs is £2.3 billion in 2011-12. The latest programme data available is for the 2010-11 financial year, with the estimates for 2011-12 based on a projection of the year-on-year change in estimated total SME Corporation Tax liabilities.

7.24 The 2010-11 estimate of £2.0 billion has been revised up by £0.6 billion from the projected estimate for 2010-11 published last year.

7.25 The estimate for the tax gap as a proportion of estimated total SME Corporation Tax liabilities has stayed broadly stable over the period from 2005-06 to 2011-12 at between 11 per cent and 13 per cent, with the exception of a low of 9 per cent in 2009-10 (see Table 7.6).

Table 7.6: Estimated Corporation Tax gap for small and medium-sized businesses (£ billion)[1]

	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12[2]
Under-declared liabilities due to incorrect returns[3]							
Point estimate	2.0	1.9	1.8	1.8	1.1	1.9	2.2
Lower estimate	0.9	0.8	0.7	0.7	0.5	0.9	1.1
Upper estimate	3.9	3.9	4.0	3.8	2.2	3.6	4.1
Compliance yield[4]	0.4	0.4	0.4	0.4	0.3	0.4	0.3
Non-payment	0.2	0.2	0.3	0.4	0.5	0.4	0.4
Net total tax gap[5]							
Point estimate	1.8	1.7	1.7	1.9	1.3	2.0	2.3
Lower estimate	0.8	0.6	0.6	0.8	0.8	1.1	1.2
Upper estimate	3.7	3.7	3.9	3.9	2.4	3.7	4.3
Total CT SME theoretical liabilities	14.0	15.0	15.9	16.1	15.6	17.2	19.6
Proportion of theoretical liabilities	13%	11%	11%	12%	9%	12%	12%

1 Figures rounded to the nearest £0.1 billion. As a result components may not appear to sum.
2 Projection factor applied to gross tax gap estimate for 2010-11 to produce a projected estimate for 2011-12. This is based on trend in estimated total SME Corporation Tax liabilities.
3 Ranges for under-declared liabilities are 95 per cent confidence intervals.
4 By period of settlement of enquiry.
5 Includes avoidance estimates for 2009-10, 2010-11 and 2011-12.

7.26 Table 7.7 shows that between the years 2005-06 to 2009-10, the proportion of SMEs submitting an incorrect CTSA return leading to a loss of tax declined from 42 per cent to 26 per cent before increasing to 36 per cent in 2010-11. However, this latter figure is based on the assumption that all open cases will be discovered to be non-compliant, whereas it is likely that some of these cases won't produce any under-declared tax liability. The 36 per cent figure for 2010-11 is therefore provisional, as it is likely that it will be revised downwards in subsequent publications when more of these currently open cases have settled.

7.27 The proportion of annualised additional liability over £1,000 declined from 19 per cent in 2005-06 to a low of 14 per cent between 2007-08 and 2009-10, before it increased back to 18 per cent in 2010-11. The proportion of annualised additional liability under £1,000 has followed a similar trend across the period. It fell from 23 per cent in 2005-06 to a low of 11-12 per cent between 2007-08 and 2009-10 before subsequently increasing to 19 per cent in 2010-11. However, the 2010-11 proportions should be regarded as provisional as they are based on all open cases producing under-declared tax liabilities and are probably over-estimates (as outlined in 7.26 above).

Table 7.7: Small and medium-sized businesses: incorrect CTSA returns where additional liability established (per cent)[1]

	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
Proportion	42%	32%	25%	26%	26%	36%
of which, under-declared liability per annum						
£1 to £1,000	23%	15%	11%	11%	12%	19%
over £1,000	19%	18%	14%	14%	14%	18%

1 Figures rounded to the nearest 1 percentage point. As a result components may not appear to sum.

Avoidance

7.28 The tax gap arising from the avoidance of Corporation Tax by SMEs can be estimated by applying the same methodology used to estimate the IT, NICs and CGT tax gap due to avoidance (Chapter 6). The illustrative estimate is £0.1 billion for 2011-12. The avoidance estimate is included within the net total tax gap estimate shown in Table 7.6.

Methodology and data issues for small and medium-sized businesses

7.29 The CTSA random enquiry programme allows HMRC to estimate the extent of under-declaration of liabilities arising from the submission of incorrect returns. The random sample used for the programme is selected from SMEs issued with a notice to file a CTSA return.

7.30 Enquiries are taken up into the sampled returns. The results of the enquiries are then extrapolated to the population to produce estimates of the compliance of SMEs.

7.31 As enquiries can take a number of years to settle, it is necessary to make assumptions about any enquiries that are still open at the time of analysis. Therefore, figures are subject to revision until all enquiries are settled. Estimates have been revised since the previous publication to include information on the outcomes of enquiries which have since settled.

7.32 Based on US research, a multiplier of 1.4 is applied to account for non-detected non-compliance.

7.33 A projection factor based on the trend in estimated total SME Corporation Tax liabilities is applied to the latest available estimate (2010-11 financial year), to produce an illustrative estimate of the under-declared liability for 2011-12.

7.34 Compliance yield is then subtracted and losses from non-payment added. This results in estimates of the tax gap for SMEs of £2.0 billion for 2010-11 and £2.3 billion for 2011-12, as shown in Table 1.1 and Table 7.6.

7.35 Last year, results for 2007-08 and 2008-09 were not published due to concerns over data quality. Now that more data is available the results for these years have become suitable for publication.

Revisions

7.36 Tax gap estimates for accounting periods ending before 2009-10 have been revised since the publication of MTG 2012 to take account of the latest information available.

7.37 The estimate for 2009-10 has remained in line with the one published last year in MTG 2012. However the estimate for 2010-11 has been revised up by £0.6 billion to £2.0 billion from the projected estimate of £1.4 billion published in MTG 2012. Last year's estimate for 2010-11 was based on projecting forward the 2009-10 estimate based on the trend in estimated total SME Corporation Tax liabilities. Now that actual data for 2010-11 is available the estimate has increased.

7.38 A revision has been made to the allocation of compliance yield between SME's and L&C businesses. The estimates of compliance yield which are used in the derivation of the CT SME tax gap estimates have been reduced by around £0.1 billion to £0.2 billion across all years – resulting in corresponding increases to the overall CT SME tax gap estimates. However, there is no net impact from this revision as there will be an offsetting decrease to the CT L&C tax gap estimate.

Chapter 8 – Other tax gaps

Key findings

- The illustrative tax gap estimate for Stamp Duty Land Tax is £0.2 billion.
- The illustrative estimate of Stamp Duty Reserve Tax is £0.02 billion.
- The illustrative tax gap estimate for Inheritance Tax is £0.4 billion.
- The illustrative estimated tax gap for the other indirect taxes is £0.4 billion in 2011-12.

This chapter describes how the tax gap has been estimated for components not covered elsewhere. A 'direct' tax is imposed on a person or a business, as opposed to an 'indirect' tax which is imposed on a transaction. All estimates are illustrative.

Table 8.1: Other direct and indirect tax gaps (£ billion)[1,2]

		2007-08	2008-09	2009-10	2010-11	2011-12
Direct						
Stamp duties	Stamp Duty Land Tax	N/A	N/A	0.2	0.2	0.2
	Stamp Duty Reserve Tax	N/A	N/A	0.03	0.03	0.02
	Total	**1.4**	**1.4**	**0.2**	**0.2**	**0.2**
Other direct taxes	Inheritance Tax	0.2	0.2	0.3	0.3	0.4
	Petroleum Revenue Tax[1]	0.03	0.05	0.02	0.03	0.04
	Total	**0.2**	**0.2**	**0.3**	**0.3**	**0.4**
Indirect						
Other excise duties	Betting and gaming Cider and perry Spirits based ready-to-drinks Biofuels	0.2	0.2	0.2	0.1	0.1
Other indirect taxes	Custom duties and levies Air passenger duty Insurance premium tax Climate change levy Aggregates levy	0.7	0.6	0.5	0.5	0.4

[1] See Chapter 5 for details.
[2] Figures rounded to the nearest £100 million, or the nearest £10 million if they are less than £50 million. As a result components may not appear to sum.

Methodology and data issues for stamp taxes

8.1 The Stamp Duty Land Tax (SDLT) gap is estimated using a combination of top-down and bottom-up methodologies. The estimate includes both commercial and residential transactions.

8.2 The estimate for 2011-12 sees a reduction from the corresponding figure for 2010-11 published in 'Measuring Tax Gaps 2012'. This reflects the progress HMRC has made in tackling SDLT avoidance.

8.3 An illustrative estimate of the tax gap for Stamp Duty Reserve Tax has been produced making the assumption that the tax at risk is approximately 1.5 per cent of receipts, from which compliance yield is subtracted and losses from non-payment of stamp duties are added. This results in an estimate of the tax gap for Stamp Duty Reserve Tax of £0.02 billion for 2011-12.

8.4 The proportion of Stamp Duty Reserve Tax receipts that are at risk has been reduced from 10 per cent to 1.5 per cent. This is a change to the methodology used in previous years as HMRC believes that the risks of non-compliance is much lower than previously projected. Stamp Duty Reserve Tax is a tax largely collected at source through the CREST computer system (the London Stock Exchange's electronic share settlement system) making the risk of non-compliance very low.

Methodology and data issues for Inheritance Tax

8.5 The assumption underlying the methodology for estimating the size of the Inheritance Tax gap has been improved following further consultation with operational experts and appraisal of departmental information. The estimate is now calculated on the assumption that the tax at risk is 20 per cent of receipts. Compliance yield is subtracted and losses from non-payment of Inheritance Tax are added to produce an illustrative tax gap of £0.4 billion for 2011-12.

8.6 Work is ongoing to investigate whether further improvements can be made to the estimate.

Methodology and data issues for other excise and indirect taxes

8.7 A proxy indicator for the scale of revenue losses across other excise taxes has been produced based on the estimated percentage tax gaps for GB oils, spirits duty, beer duty and cigarettes duty. Hand rolling tobacco and the Northern Ireland oils gaps have not been used to produce the proxy indicator. This is because:

- Northern Ireland estimates include losses from legitimate cross-border shopping and therefore overestimate the true tax gaps
- it is clear from operational evidence that none of the unmeasured indirect taxes are subject to the high levels of fraud found in hand rolling tobacco.

8.8 For other indirect taxes, the indicator has been calculated by treating the unknown tax gaps as if they had the same simple average percentage loss as the selected measured excise gaps. By calculating the alcohol component separately, using known alcohol tax gaps, the calculation should be more representative.

8.9 The average percentage revenue losses should not be considered estimates of the true percentage loss across the taxes listed in Table 8.1 under 'Other excise duties' and 'Other indirect taxes' as this is unknown. Many of the indirect taxes listed are very different from one another in their nature, each being subject to different rules. The true percentage tax gaps are therefore likely to vary widely across the various taxes listed.

Glossary

Accounting period	The period for which a business prepares its accounts and in respect of which a Corporation Tax assessment is raised. It cannot be more than 12 months in length, although it can be shorter.
Central estimate	The most likely estimate of the true value.
Compliance activity	An intervention by HMRC, such as a direct tax enquiry, Employer compliance review or VAT assurance visit, designed to ensure that the correct amount of tax is being accounted for and paid.
Compliance yield	Additional tax charged, resulting from compliance activity.
Confidence interval	A range of values that has a specified probability of containing the true value of interest.
Cross-border shopping	Legal importation of goods for personal use.
Estimates	Approximate results calculated from approximate or incomplete data.
Evasion	The deliberate omission, concealment or misrepresentation of information, or the false or deceptive presentation of circumstances, to fraudulently obtain a fiscal advantage, whether temporarily or permanently.
Fraud	Deliberate, dishonest evasion of tax.
Gross Domestic Product (GDP)	GDP is the market value of all final goods and services made within a country in a year.
Illicit market	The part of the market on which due taxes and duties have not been paid.
Legitimate consumption	Consumption of goods for which the correct duty has been paid.
Litigation	A lawsuit seeking a legal remedy to a question or dispute.
Lower estimate	The value below which the true value will not lie.
Mid-point	Average of the upper and lower estimates.
Non-payment	Tax debts that are identified but never paid off. Eventually this debt will be written off by HMRC as uncollectable.
Non-UK duty paid	Any product that has not had UK duty paid on it.
Official Statistics	All statistics produced by the Office for National Statistics, government departments, the devolved Administrations and other Crown bodies, are automatically deemed to be Official Statistics.
PAYE scheme	Each employer operating PAYE registers a PAYE scheme with HMRC, which allows for the issue and monitoring of returns.
Risk Register	A list of identified tax risks, together with information such as estimated value, nature and status. Registers are used to track and monitor the risks they cover.
Self Assessment (SA)	A system for reporting income and capital gains to, and claiming tax allowances from, HMRC.
Settlement	Closure of a direct tax enquiry, resulting in the agreement of any additional tax liability.
Small and medium-sized enterprises (SME)/business	Any employer/business that does not fall within the EU Large definition.
Smuggling	In this document this covers all activity that results in goods entering the UK market without the correct duty being paid.
Stamp Duty Reserve Tax	Stamp Duty Reserve Tax is a tax on shares and securities when you buy through the stock market or a stock broker.
Tax under Consideration (TuC)	The value of an issue is the amount of TuC. The TuC in an enquiry is an estimate initially made before any consideration of the specific facts has taken place. It does not represent the tax owed or unpaid. The TuC for a given risk is updated when the Department's view on the possible outcome of the enquiry changes, for example, because new facts are established or legal advice is obtained.
Upper estimate	The value above which the true value will not lie.
Write-offs	Debts that are considered to be irrecoverable.

Abbreviations

CGT	Capital Gains Tax
CT	Corporation Tax
CTSA	Corporation Tax Self Assessment
EU	European Union
GB	Great Britain
GDP	Gross Domestic Product
GLF	General Lifestyle Survey
HMRC	Her Majesty's Revenue & Customs
IRS	Internal Revenue Service (United States)
IT	Income Tax
LBS	Large Business Service
LCF	Living Costs and Food Survey
MTIC	Missing Trader Intra-Community fraud
NI	Northern Ireland
NICs	National Insurance Contributions
ONS	Office for National Statistics
PAYE	Pay As You Earn
PRT	Petroleum Revenue Tax
SA	Self Assessment
SDLT	Stamp Duty Land Tax
SME	Small or medium-sized enterprise/business
UK	United Kingdom
VAT	Value Added Tax
VTTL	VAT Total Theoretical Liability

Feedback

We are looking to improve the quality, timeliness and the presentation of tax gap statistics, and would welcome your feedback. Please contact:

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Issued by
HMRC Corporate Communications