Office for National Statistics

Article

Challenges of measuring the effects of the coronavirus pandemic on tax receipts: June 2020

Useful background information underlying the Public sector finance statistical bulletin, explaining the challenges we face in measuring the effects of the coronavirus (COVID-19) pandemic on tax receipts.

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1 . Background

To estimate borrowing, tax receipts are recorded on an accrued (or national accounts) basis rather than as cash receipts. In other words, we attempt to record receipts at the point where the liability arose, rather than when the tax is actually paid.

This means that accruals-based tax receipts for the current period depend on information from both current cash payments and on projections of future tax receipts, which are "accrued" (or time adjusted) back to the current month. For this purpose, we use official forecasts of future cash receipts, produced by the Office for Budget Responsibility (OBR).

2 . Estimating future tax receipts

Future tax receipts used in our accrued estimates are based on those in the Office for Budget Responsibility's (OBR's) Coronavirus Reference Scenario (14 May 2020). The reference scenario assumes a three-month lockdown period followed by a gradual return to normal over the subsequent three months. It also suggests a significant reduction in future revenues compared with the earlier, official forecast published on 13 March 2020.

On 14 July 2020, the OBR published their 2020 Fiscal sustainability report setting out long-term projections for spending, revenue and financial transactions, and assessing whether they imply a sustainable path for public sector debt. Alongside this report, OBR published an update to their Coronavirus Reference Scenario (14 May 2020). Due to the time constraints the Coronavirus Reference Scenario (14 July 2020) is not yet reflected in the accrued (or national accounts) based estimates of tax receipts included in this bulletin. We plan to incorporate these new data in our 21 August 2020 publication.

3 . Exceptional adjustments

The Office for National Statistics (ONS) and HM Treasury have been working with both HM Revenue and Customs (HMRC) and the Office for Budget Responsibility (OBR) to determine whether there is enough information to make exceptional adjustments that estimate COVID-19 effects.

Where data are available, we have adjusted the recording of accrued tax receipts (on a national accounts basis) for June and earlier periods. These adjustments are described later in this article. These exceptional adjustments, and their underlying assumptions, will be revisited over the coming months as more information becomes available.

Pay as you earn Income Tax

Pay as you earn (PAYE) Income Tax is normally recorded on an accrued (or national accounts) basis by time-adjusting cash receipts using a one-month lag, which means that, for example, accrued PAYE receipts for June are based on forecast July cash receipts.

The amount of cash received for PAYE Income Tax in June 2020 was lower than usual, with much of that weakness likely attributable to lower earnings and employment and non-payment of liabilities. June 2020 receipts recorded on an accrued basis are estimated based on the Office for Budget Responsibility (OBR) Coronavirus Reference Scenario (14 May 2020).

We currently assume that most non-paid tax from April and June 2020 will still be paid, but in a later period than originally expected. We have included a 7% adjustment to reduce expected PAYE receipts on a national accounts basis to account for possible non-payment of PAYE. This assumption is based on the information set out on tax debts and losses in HMRC's annual report and accounts, and is based on average losses for the most recent three years of data.

In estimating PAYE receipts on an accrued basis for June 2020, we have used additional cash receipts information for May and June 2020 to inform a judgement on the repayment of arrears (or debt).

Value Added Tax

Value Added Tax (VAT) data for any month are normally recorded on an accrued (or national accounts) basis by time-adjusting the average cash receipts expected in the following three months. This means that, for example, VAT receipts on an accrued basis in June depend on forecast cash receipts for July, August and September. These are updated as actual receipts become known.

The government announced a deferral scheme for Value Added Tax payments, enabling UK businesses to pay VAT due between 20 March 2020 and 30 June 2020 at a later date (though before 31 March 2021). As a result, cash VAT receipts are lower than usual in this period.

The initial assumption is that all the deferred tax owed will still be paid, but in a later period than originally expected, as is permitted under the deferral scheme. We have therefore made an exceptional adjustment to prevent the effects of the deferral scheme on VAT receipts from impacting accrued receipts. Receipts forecasts are based on the OBR's Coronavirus Reference Scenario (14 May 2020), adjusted to account for the impacts of the deferral scheme.

The existence of this deferral assumption within accrued VAT means that they are subject to revision once further intelligence is gathered on deferred VAT. VAT on an accrued basis should be considered as provisional from December 2019 onwards until a final determination has been made on the deferrals.

There are not enough data available yet on which to estimate the amount of VAT that will not be paid because of lower economic activity or businesses ceasing to trade.

Corporation Tax

Corporation Tax data for any month are normally recorded on an accrued (or national accounts) basis by time-adjusting cash receipts for the subsequent 2 to 21 months, depending on the profits of the company.

As with pay as you earn (PAYE) and Value Added Tax (VAT), estimates of future months' cash receipts are currently based on the Office for Budget Responsibility's (OBR's) Coronavirus Reference Scenario (14 May 2020).

We are not yet able to estimate the amount of Corporation Tax that will not be paid, for example, because of reduced trading activity leading to lower profits, firms deferring tax payments to a future date or firms going out of business. The OBR Coronavirus reference scenario assumes a non-payment rate of 10% and therefore this is our current assumption.

The national accounts estimates of accrued corporation tax relies heavily on forecast cash receipts, however in making these forecasts there remains uncertainty regarding the amount of corporation tax revenue that may never be received. Both cash receipts and accrued receipts should be viewed together for additional context.

Air Passenger Duty

As with the taxes outlined above, estimates of future months' Air Passenger Duty (APD) cash receipts are currently based on the Office for Budget Responsibility's (OBR's) Coronavirus Reference Scenario (14 May 2020).

In estimating APD receipts on an accrued (or national accounts) basis for June 2020, we have used additional cash receipts information for May and June 2020 to inform a judgement on the repayment of arrears (or debt).

Other taxes

Limited information has meant that those taxes not collected by HMRC (such as business rates) are currently likely to be overestimated. Such taxes will be reviewed over the coming months when more information becomes available.