

Inspection of HM Revenue & Customs

Handling of Human Intelligence Sources





**Denis O'Connor CBE QPM
HM INSPECTOR OF CONSTABULARY**

Ground Floor, Allington Towers, 19 Allington Street, London, SW1E 5EB
Tel: 020 7035 5713 Fax: 020 7035 5184 Mobile: 07901 716197
Email: denis.o'connor@homeoffice.gsi.gov.uk

The Paymaster General
HM Treasury
1 Horse Guards Road
LONDON SW1A 2HQ

24 March 2006

Dear Minister

**INSPECTION OF HMRC HANDLING OF HUMAN INTELLIGENCE
SOURCES**

Please find attached a copy of my report *Inspection of HMRC Handling of Human Intelligence Sources*. There are some issues outstanding regarding the handling and protective marking arrangements of sensitive issues within the report, which may require the drafting of a redacted version for publication.

Whilst the focus of this work was on covert human intelligence sources, the report acknowledges the success of the Department in using covert intelligence gathering techniques to tackle fraud, smuggling and improve the profiling of freight and passenger movements. It also recognises HMRC's development of a useful initiative to record contact with human sources of information (the HumInt system) and ensure HMRC officers' compliance with the law. You may recall we discussed the positioning of law enforcement in HMRC and the report highlights this as an issue. It is clear that senior management have aspirations for HMRC to be considered as a world leader in revenue protection. In order to succeed, the Department would benefit from wider recognition of the value of law enforcement in the protection of the revenue and consideration could be given to explicitly reflecting this in the Department's strategy statement.

An examination of a sample of informant files has generated concern and led me to recommend a further full and thorough audit to ensure that HMRC's informant handling capability is fit for purpose in every respect in the future. HMRC has already agreed to this, understanding the importance of this aspect of business to the Department's reputation.

I am pleased to note that HMRC has already taken a number of positive steps following submission of the draft report to the Director General, Enforcement and Compliance. I have forwarded a copy of the final report to Sir David Varney.

Yours sincerely,

Denis O'Connor

Denis O'Connor
HM Inspector of Constabulary



INVESTORS IN PEOPLE



HM Treasury, 1 Horse Guards Road London, SW1A 2HQ

Denis O'Connor CBE QPM
HM Inspector of Constabulary
Allington Towers
19 Allington Street
London SW1E 5EB

6 February 2007

Dear Mr O'Connor

Thank you for your letter of 24 March together with a copy of your report *Inspection of HMRC Handling of Human Intelligence Sources*. As you know, a redacted version of the report has now been agreed between HMIC and HMRC. Arrangements are being made to publish on the respective websites and for hard copies to be distributed to key stakeholders. Although there will have been a delay between the production of your report and its appearance in public, I think that the delay can be justified by the need to have completed and considered the follow-up audit of HMRC files before publication.

The redactions deal with covert intelligence gathering methodology, the positioning of Covert Human Intelligence Sources (CHIS) and the resilience of existing resources. I understand they have been agreed with your team.



I welcome your acknowledgement of the success of the Department in using covert intelligence gathering techniques to tackle revenue fraud and smuggling, and the recognition of the Humint system as an innovative initiative. The inspection adds impetus to HMRC aims to promote a culture of delivery to the highest professional standards in the law enforcement field, seeking and using best practice from other organisations. HMRC are proceeding to implement your recommendations.

The reputation of HMRC is vital to effective engagement with opposite numbers in key partner agencies. I was pleased to learn therefore that the follow-up audit saw no evidence of dishonest or corrupt practices and no evidence that HMRC had failed to meet its disclosure obligations under the Criminal Procedures and Investigations Act (CPIA) 1996 in relation to UK prosecutions. HMRC have accepted and will also be implementing your recommendations following this audit aimed at improving value for money and various standard operating procedures including those relating to management of duty of care to human sources.

HMRC have also accepted your recommendations about strengthening governance arrangements in the post-SOCA era to ensure both robust management systems are sustained and that CHIS are used effectively against the problems we face.

DAWN PRIMAROLO MP

Summary of the Inspection of HMRC Handling of Human Intelligence Sources

The last three years have seen a significant increase in the attacks on the tax system by organised criminality. This is currently estimated to cost £5-7 billion a year. Strategies to tackle this have been developed in the indirect tax area (the area of highest risk) and are progressively being extended across the tax system. These have delivered some successes – a reduction in the illegal market for cigarettes by 20% and reducing VAT missing trader fraud by 30%. A strong law enforcement capability is a vital part of tackling this threat and senior management in HMRC are developing a new law enforcement capability in light of challenges and legacy issues. This involves de-merging some 40% of the former HM Customs and Excise investigation and intelligence capacity dealing with serious drugs investigations and transferring it to SOCA and merging the remaining Customs and Inland Revenue function. However, the pressure from fraudsters is relentless and frauds shift and mutate. Information recently provided by HMRC indicates that despite the earlier successes, the losses to VAT missing trader fraud are currently at the same level as they were at the height of the fraud in June 2002. The Department requested an inspection of human source handling – an essential tool in combating criminality.

There is a desire to re-establish the reputation of HMRC in law enforcement and mobilise behind a strong, strategic direction. HMRC's senior management should take credit for identifying source handling as a topic for early inspection, as this displays a willing and open attitude towards confronting issues that have been cause for concern. The challenge for the Department cannot be underestimated however and will need sustained and robust leadership and direction.

HMRC's handling of Covert Human Intelligence Sources (CHIS)¹ appears to be compliant with nationally accepted operating standards in regard to policies and structures. However, when tested in depth, a number of issues were identified around the registration of CHIS and the Department's duty of care towards them. There is also room for improvement in the alignment of CHIS with business needs, and risk assessment associated with them. HumInt² is an imaginative initiative to record contact and prevent status drift³, but only fully implemented in the enforcement function of the Department.

¹ A CHIS is defined in the Regulation of Investigatory Powers Act 2000, Part II, Section 26, Paragraphs 8 a-c. Where extracts from other documents and reports are copied in this report, any reference to 'informant' should be read as CHIS.

² HumInts are defined in the HMRC Enforcement Handbook as: "all persons who give information to the Department relating to a possible criminal offence or regulatory breach (including any offences that may ultimately be dealt with under 'civil' provisions) or regulatory breach. The term HumInt covers all those who provide information to the Department whether they receive such information in the course of their trade, profession, business or employment and who, out of civic duty, volunteer information or those we categorise as ... CHIS". See paragraph 5.4

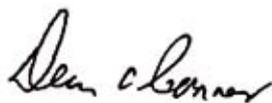
³ The change in status from a non-CHIS to a CHIS – so-called "status drift". See THE HONOURABLE MR. JUSTICE BUTTERFIELD (July 2003) *Review of criminal investigations and prosecutions conducted by HM Customs and Excise*: Paragraphs 10.47, 10.58, 10.59 and 10.77

Whilst it provides the beginning of a national database, it has not, as yet, overcome quality control issues. International source handling will change following the formation of the Serious Organised Crime Agency but if Fiscal Liaison Officers are to make a contribution in this regard in the future, they will need a significantly stronger support framework for informant handling than currently exists.

There is real scope for development if this is to be an effective tool of proactive law enforcement. The numbers of registered CHIS are relatively low. The structural costs of managing them are high, with staff costs alone amounting to several million. They are more representative of past intelligence priorities, rather than future needs, post SOCA. No evidence was found of the use of the relatively expensive Source Management Units to proactively fill in gaps in intelligence and although HMRC has some Missing Trader Intra-Community Fraud⁴ CHIS, there are gaps on other key issues. Training, such as it is, accentuates risks and compliance and has not encouraged staff to seek information and intelligence. Rewards for CHIS can be slow to come, and the information systems are not yet readily accessible for performance management purposes.

Whilst the work on CHIS represents only a relatively small slice of HMRC activity, it is an important indicator of strong investigative and enforcement activity. Following the inspection, it is recommended that a full independent audit of all HMRC CHIS files is undertaken at the earliest opportunity. Notwithstanding that audit, particular issues for improvement include: the production of Standard Operating Procedures for CHIS practitioners; improvement of the Quality Assurance and value for money processes; improvements to the rewards system; development of a structured staff succession planning process for accredited legislated posts; the production of a clear implementation plan for HumInt; the provision of further staff training which emphasises the potential value of intelligence from human sources of information; the introduction of a Quality Control mechanism for HumInt; the development of promotional campaigns to encourage the public to volunteer information and the provision of greater support for Overseas Liaison Officers.

However, CHIS handling is most likely to flourish where it is considered not simply in relation to the limited direct yield from enforcement action, but where it is a well integrated part of the compliance function and used in intelligently protecting the revenue as a whole. Some initial thoughts on the positioning and integration of an intelligent enforcement contribution to compliance are outlined.



Denis O'Connor

24 March 2006

⁴ Missing Trader Intra Community (MTIC) or 'carousel' fraud is a systematic attack by organised criminals in which large sums are obtained by the fraudulent manipulation of the VAT system.

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Chapter 1

The Origins of this Inspection

- 1.1 On 2 July 2003 the Paymaster General, Dawn Primarolo, announced the implementation of a review of the Revenue Departments *"to enhance service delivery to the taxpayer"*¹, to be chaired by Gus O'Donnell, Permanent Secretary to the Treasury. As a result of this review², in his budget statement on 17 March 2004, the Chancellor announced HM Customs & Excise (HMCE) and HM Inland Revenue (IR) would merge. The Commissioners for Revenue and Customs Act 2005 received Royal Assent on 7 April 2005 and Her Majesty's Revenue and Customs (HMRC) was launched on 18 April 2005 with a combined workforce of some 100,000 full-time equivalent (FTE)³ staff. Earlier, during the 1999-2000 session of Parliament, the Treasury Select Committee had highlighted the potential benefits of merging the two departments, stating: *"These benefits would be likely to arise from the full merger of many headquarters and support functions; the establishment of fully integrated revenue collection teams; and synergistic improvements in compliance, collection costs and the new department's revenue collection culture. We believe that the merger of the Inland Revenue and Customs and Excise would improve compliance with taxation, reduce businesses' compliance costs and reduce the Government's revenue collection costs and we recommend that such a merger should proceed and that the Government should bring forward a plan for the merger in accordance with our conclusions and recommendations in this Report"*⁴.
- 1.2 HMCE was one of the oldest government departments, with a national customs system established by King John's Winchester Assize of 1203. Income Tax was announced in 1798, and introduced in 1799, as a means of paying for the war against the French forces under Napoleon. The investigative capabilities of both HMCE and IR developed in a similar manner throughout the late 19th and early 20th Centuries. Customs officers in the 1920s were dealing with illicit distillation, illicit entertainment, duty frauds and large smuggling investigations. About the same time IR investigators were dealing with fraud and evasion.

¹ DAWN PRIMAROLO MP: Hansard, HC, written answers. cols. 270W (2 July 2003).

² See O'DONNELL, GUS (March 2004) *Financing Britain's Future: Review of the Revenue Departments*. London: HM Treasury. (Cm 6163).

³ See CABINET OFFICE (2005) *Civil Service quarterly public sector employment statistics (PSES) as at 31 March 2005* Online [Available at http://www.civilservice.gov.uk/management/statistics/publications/xls/pses_q1_2005_revised_jan06.xls].

⁴ TREASURY SELECT COMMITTEE (1999-2000) *Second Report: HM Customs and Excise* (HC 53 of 1999-2000): London: HMSO: Paragraph 45.

The Origins of this Inspection

- 1.3 In the latter part of the First World War, IR adopted a policy of granting immunity from prosecution in return for full co-operation in the majority of its potential fraud cases. This policy was formally publicised in 1923 by written answer to a parliamentary question and became known as the Civil Investigation of Fraud or 'Hansard,' procedure. This policy led to significant differences between the Departments' respective approaches to criminal investigation. HMCE developed a more proactive and aggressive law enforcement capability whilst IR reserved prosecution for only the most 'heinous' and 'exemplary' cases.
- 1.4 As a result, there were significant differences between the two departments around the proportion of staff dedicated to the investigation and prosecution of criminal cases. By the time of the merger there were just under 1,500 serving specialist investigators employed on criminal investigations in HMCE, from a total workforce of about 22,790 FTE staff. At the same time there were about 360 serving Investigators employed in criminal investigations in IR, from a total workforce of about 75,030⁵.
- 1.5 HMCE had, for some time, been a member of a number of Association of Chief Police Officers (ACPO) committees, including the National Source Working Group (NSWG), where it had been particularly active and indeed held the chair of the Source Management Training sub-group. IR had not been a member of ACPO committees and, whilst the Special Compliance Office (SCO) did employ law enforcement techniques, it did not develop its capabilities in these areas to the same extent as HMCE. Prior to merger the IR had not been afforded access to the ACPO guidance for the use of covert human intelligence sources.
- 1.6 In discharging their responsibilities for protecting their respective areas of revenue both former departments employed a range of law enforcement techniques, including the use of CHIS.
- 1.7 The use of the CHIS techniques employed by the former HMCE and associated issues were the subject of criticism following the loss of a number of high profile HMCE trials between 1998 and 2001 and subsequent abuse of process applications heard by Mr Justice Grigson at Liverpool Crown Court in 2002.
- 1.8 This led to a review of criminal investigations and prosecutions conducted by HMCE by Mr Justice Butterfield⁶. His recommendations included the need for systematic external scrutiny of HMCE law enforcement work and, following the announcement of the merger of the two departments, The Commissioners for Revenue and Customs Act 2005 introduced HM Inspectorate of Constabulary (HMIC) as the organisation to undertake that role for the newly formed HMRC.

⁵ *ibid*: CABINET OFFICE (2005).

⁶ See THE HONOURABLE MR. JUSTICE BUTTERFIELD (July 2003) *Review of criminal investigations and prosecutions conducted by HM Customs and Excise*.

Chapter 2

Methodology

- 2.1 Her Majesty's Inspector extends sincere thanks to the three police forces and the national agency for supporting this inspection and enabling field visits and interviews with key personnel. The open and honestly expressed opinions were particularly beneficial in helping to identify issues, concerns and indeed good practice that can be found in this arena.
- 2.2 This is the very first inspection of its kind within HMRC and therefore a unique event for all concerned. Her Majesty's Inspector extends sincere thanks to the Board, Directors and all HMRC staff who took part in the inspection. The inspection team were warmly welcomed at every venue and the honest and frank views of participants indicates a workforce willing to critically reflect on their own and departmental approaches to systems and procedures. The contributions of all those who met the inspection team, have facilitated the production of the final report, which sets out in detail the issues, inhibitors and enablers they have identified. Her Majesty's Inspector extends thanks to the officer in HMRC's Criminal Justice Enforcement Standards for her invaluable support in her role as HMIC Liaison Officer and her assistance in arranging the extensive programme of inspection visits across the breadth of the newly formed department's estate.
- 2.3 Her Majesty's Inspector was supported by an inspection team comprised of specialist staff officers with a wide breadth of experience of conducting and managing criminal investigations in the police service, former HMCE and former IR. The team also included officers with recent and extensive experience of source handling within a law enforcement environment and analytical support.
- 2.4 The inspection of HMRC conducted in Scotland was undertaken jointly with colleagues from HMIC Scotland.
- 2.5 In order to compare and contrast HMRC's approach to managing source handling with other law enforcement agencies – and in agreement with HMRC – the inspection team visited three police forces and another national agency.
- 2.6 The first phase of the inspection involved the collecting of over 150 documents from the forces, national agency, HMRC and other open sources that were relevant to the inspection. In addition to the related acts of parliament, this included pertinent reports and those documents relating to policy, strategy, advice and guidance. This material was then reviewed and used to identify key areas of activity that would be subject of inspection.

Methodology

- 2.7 Phase two involved the team conducting field visits to the three police forces and the national agency. A variety of site visits were undertaken that involved examination of files, documents, systems and procedures. Interviews were conducted with key personnel at all levels and a number of focus groups allowed many other officers the opportunity to share their knowledge, understanding and experience. Personnel working in the specialist arena of source handling were the initial focus, however a number of other units were included in order to assess the likelihood or otherwise of engaging with sources of information that may be potential CHIS.
- 2.8 The inspection team then conducted field visits across HMRC during October to December 2005. This process took 10 weeks at numerous locations throughout England, Wales, Scotland and Northern Ireland, with the international arm of the Department being engaged through HMIC's attendance at the Overseas Liaison Officers' (OLOs') annual conferences. Over 130 interviews or focus groups were conducted with more than 500 HMRC staff.
- 2.9 This fieldwork was complemented by examination of a sample of CHIS files retained at HMRC's SMUs in January 2006.
- 2.10 Given the sensitive nature of source handling parts of the content of this report have been redacted.

Chapter 3

Findings

"Informants properly employed – I emphasise properly employed – consistent with all the regulations laid down, are essential to criminal investigation and combating crime"⁷.

3.1 Specialist Activity – Compliance

- 3.1.1 HMRC has established dedicated Source Management Units (SMUs) in order to deal professionally with CHIS. For law enforcement agencies regularly operating in this arena SMUs are not mandatory, though they are considered good practice.
- 3.1.2 All specialist staff receive training to the requisite levels in accordance with national standards. However there was an inadequate level of understanding amongst a number of HMRC CHIS Operations (CHIS Ops) staff about several CHIS management issues⁸.
- 3.1.3 All dedicated SMUs benefit from a comprehensive range of structures designed to provide protection for both handlers and CHIS from unnecessary exposure⁹.
- 3.1.4 HMRC has adapted the guidance standards used by other law enforcement agencies to reflect departmental language and incorporate HMRC references¹⁰.
- 3.1.5 In addition, a section of the Enforcement Handbook has been produced to give instructions to all staff in the former HMCE and some in the former IR on how to deal with human sources of information. These instructions are supplemented with links to the legislation, CHIS Code of Practice and best practice guidance¹¹.
- 3.1.6 Standard Operating Procedures (SOPs), where they have been developed in other agencies, are seen as good practice because they provide practitioners with step by step advice and guidance on virtually every aspect of managing CHIS¹².

⁷ Baroness Blatch: Hansard, HL (series 5) vol.574, cols. 1261 (23 July 1996).

⁸ See Paragraph 4.11

⁹ See Paragraphs 4.7.1 – 4.7.2

¹⁰ See Paragraph 4.2.2

¹¹ See Paragraph 4.2.1

¹² See Paragraph 4.2.3

Findings

- 3.1.7 Whilst HM Inspector acknowledges the challenge presented by the SOCA de-merger, HMRC does not appear to have any structured succession planning for its SMU staff¹³.
- 3.1.8 HMRC should reinforce the circumstances in which contacts between handlers and their CHIS are permitted when relating to the same specified operation¹⁴.
- 3.1.9 There are delays in HMRC's payment of rewards to CHIS which lead to operational difficulties.
- 3.1.10 Examination of a sample of CHIS profiles held within separate HMRC SMUs revealed areas of concern around CHIS management.
- 3.1.11 The Quality Assurance Bureau (QAB) reports did not include assessments of the Value for Money (VFM) of HMRC's CHIS. Any such assessments are only conducted by local management in a number of SMUs¹⁵.
- 3.1.12 At the time of inspection HMRC was in the process of adopting an electronic system similar to the Police Management System. HMRC anticipated that its electronic system will be operational by the target date of March 2006¹⁶.
- 3.1.13 The national agency and some forces have developed SMUs to deal exclusively with CHIS. These units are separate from investigation teams, providing a useful firewall between disciplines. Additionally, the adoption of an electronic system provides management with an auditable, durable and retrievable database that is particularly useful for disclosure in accordance with the Criminal Procedure and Investigations Act (CPIA) (1996). The developments of SOPs have also provided these agencies with a supplementary guide for practitioners.

3.2 Specialist Activity – Proactivity

- 3.2.1 As at December 2005, HMRC's UK based CHIS practitioners managed a relatively small number of CHIS. The Department's ratio of SMU staff to CHIS is less than half that found in the national agency¹⁷.
- 3.2.2 The annual staffing costs of a typical SMU was considerable as at December 2005¹⁸.
- 3.2.3 Unlike the police service and the national agency, there is little evidence of HMRC utilising a formalised tasking and co-ordinating process¹⁹.

¹³ See Paragraph 4.4.5

¹⁴ See Paragraph 4.6.2

¹⁵ See Paragraph 4.12

¹⁶ See Paragraph 4.5.3

¹⁷ See Paragraph 7.1.1

¹⁸ See Paragraph 7.1.2

¹⁹ See Paragraph 7.1.4

- 3.2.4 Senior HMRC management were enthusiastic about utilising CHIS as an intelligence gathering tool; however, there is a reluctance amongst operational law enforcement officers to use CHIS in this way²⁰.

3.3 Routine Activity – Compliance

- 3.3.1 HMCE introduced the HumInt system on 1 September 2003 and established the National HumInt Centre (NHC). The system was designed to provide HMCE with a central record of all persons providing attributable verbal information relating to a possible criminal offence or regulatory breach and a monitoring process for potential status drift in response to the problems identified by Mr Justice Butterfield²¹.
- 3.3.2 The Inland Revenue did not have a national database of 'informers'^{22 23}.
- 3.3.3 Following the merger of HMCE and IR, the HumInt procedures have been introduced across areas of the former IR. However, the bulk of the former IR still operates under its former guidelines²⁴.
- 3.3.4 HMRC has yet to publish a clear implementation plan for the introduction of the HumInt system across the areas of the Department outside former HMCE and parts of the IR. The lack of such a plan has resulted in the local policies regarding the introduction of the system being developed in at least one unit²⁵.
- 3.3.5 The creation of the NHC should, in principle, ensure monitoring and control of status drift provided that everyone subscribes to the HumInt policy and instruction. However adherence to it was not consistent across the parts of the Department where it has been introduced.
- 3.3.6 NHC are receiving many Human Contact Reports (HCRs) which contain insufficient detail. The distinct lack of intelligence and supporting information make it virtually impossible to complete satisfactory risk assessments²⁶.
- 3.3.7 The HumInt system does not include any quality control process, in that there is no line management oversight of HCRs prior to their submission to the NHC²⁷.

²⁰ See Paragraphs 7.1.5 – 7.1.7

²¹ See Paragraphs 5.4.4 & 5.4.5

²² All references to 'informer' in this report relate to the former IR's use of this term to describe Human Intelligence Sources who do not fall within the definition of a CHIS.

²³ See Paragraph 5.3.4

²⁴ See Paragraph 5.5.1

²⁵ See Paragraphs 5.5.1 – 5.5.3

²⁶ See Paragraphs 5.5.8 & 5.5.9

²⁷ See Paragraphs 5.4.6 & 5.5.9

Findings

- 3.3.8 Adherence to the HumInt system's Quality Assurance (QA) programme is patchy²⁸.
- 3.3.9 HumInt awareness was delivered to staff by 'cascade' training (despite Mr Justice Butterfield's concerns about this method). This training has simply added to the confusion. In many cases it has contributed to a level of avoidance and aversion to using human sources of information that manifested itself as fear²⁹.
- 3.3.10 Although the inspection found examples of some non-specialist police officers, and even a number of specialist investigators and intelligence officers who were unclear of how to deal with human sources of information, most were aware of where to find clarification and guidance on these issues. Of greater concern was the lack of understanding demonstrated by some Police Community Support Officers (PCSOs)³⁰.

3.4 Routine Activity – Proactivity

- 3.4.1 Although an HMRC senior manager referred to intelligence as the lifeblood of the organisation, this endorsement did not extend to the Department's approach to gathering information from human contacts³¹.
- 3.4.2 HumInt training for non-CHIS Ops staff focuses on Departmental systems and processes and does not lay sufficient emphasis on the potential value of human sources of information³².
- 3.4.3 The increased use of telephone call centres has given many officers the opportunity to refer potential HumInts to Customs Confidential or the Direct Taxes Helpline, where they would be treated as anonymous callers, rather than engaging with them themselves. As a result, these HumInts are lost to HMRC for potential development³³.
- 3.4.4 Concerns have been raised with regard to the quality of intelligence reports being generated by call centre operators³⁴.
- 3.4.5 Officers posted at air and sea ports indicate that they are receiving substantially less intelligence from human sources of information than they have in the past³⁵.

²⁸ See Paragraph 5.5.12

²⁹ See Paragraph 5.5.6

³⁰ See Paragraph 5.2.2

³¹ See Paragraphs 7.2.1 – 7.2.2

³² See Paragraph 7.2.3

³³ See Paragraph 7.2.4

³⁴ See Paragraph 7.2.6

³⁵ See Paragraph 7.2.7

- 3.4.6 HMRC's recent media campaign to promote its new Direct Taxes Helpline is a positive example of how the Department can encourage members of the public to provide information. The Department is encouraged to look at utilising other ways of encouraging the public to volunteer information³⁶.
- 3.4.7 Since the 1980s the police service has promoted Crimestoppers as an invaluable means of gathering information from the public to detect crime. In addition, forces regularly utilise both local and national media campaigns to encourage the public to assist the police in protecting the community.
- 3.4.8 For many years, the police service has successfully used CHIS in support of operational requirements. More recently, particularly since the adoption of the National Intelligence Model (NIM), police forces have identified intelligence gaps and have proactively sought to fill them through the deployment of a number of intelligence assets, one of which is CHIS.

3.5 International Activity – Compliance

- 3.5.1 HMRC has OLOs deployed to posts throughout Europe and the rest of the world. They are divided generally into a Fiscal Liaison Officer (FLO) network based in the European Union and a Drug Liaison Officer (DLO) network for the rest of the world³⁷.
- 3.5.2 Job descriptions used in recent OLO recruitment exercises have not listed CHIS handling as a key activity/responsibility³⁸.
- 3.5.3 OLOs have received CHIS handling training, and feel that they should receive additional bespoke training³⁹.
- 3.5.4 As a consequence of the unique circumstances of their deployments, OLOs are unable to comply with the guidance standards⁴⁰.
- 3.5.5 HMRC has deployed a regional controller to one area of the world.
- 3.5.6 Where operations involve the deployment of CHIS, OLOs often seek opportunities to disrupt criminal operations in their host country rather than to allow them to reach UK territory. They contend that, in some instances, this avoids conflicts between UK and foreign criminal justice systems, which could ultimately lead to the withdrawal of a UK prosecution⁴¹.

³⁶ See Paragraph 7.2.11

³⁷ See Paragraph 6.1.2

³⁸ See Paragraph 6.3.1

³⁹ See Paragraph 6.3.2

⁴⁰ See Paragraph 6.2.2

⁴¹ See Paragraph 6.2.1

3.6 International Activity – Proactivity

- 3.6.1 As at January 2006, a significant proportion of HMRC's CHIS were being managed by OLOs. On average they manage more CHIS than their counterparts in UK based SMUs.
- 3.6.2 The viability of HMRC's International SMU will have to be assessed post April 2006, as the DLO network will migrate to the Serious Organised Crime Agency (SOCA)⁴².

⁴² See Paragraph 7.3.2

Chapter 4

Compliance with Standards and Adherence to Doctrine

4.1 Background/Historical Context

- 4.1.1 Until the early 1990s, the management of human sources of information by law enforcement agencies was subject to local policies, existing custom, practice and case law. In 1995, *National Guidelines on the Use and Management of Informants and Related Issues*, were issued to all police forces. In 1996, HMCE issued its own version of these guidelines which adhere to the principles outlined in the ACPO guidance. Following the introduction of HRA in 1998, the Government sought to formalise the legal basis for these investigative techniques. The Regulation of Investigatory Powers Act 2000 (RIPA), Regulation of Investigatory Powers (Scotland) Act 2000 (RIP(S)A) and the associated Codes of Practice in 2000, introduced, for the first time in UK law, legislation to define and regulate the handling of CHIS. RIPA defined a CHIS as follows: *"For the purposes of this Part a person is a Covert Human Intelligence Source if –*
- a) *he establishes or maintains a personal or other relationship with a person for the covert purpose of facilitating the doing of anything falling within paragraph (b) or (c);*
 - b) *he covertly uses such a relationship to obtain information or to provide access to any information to another person; or*
 - c) *he covertly discloses information obtained by the use of such a relationship, or as a consequence of the existence of such a relationship*"^{43 44}
- 4.1.2 In order to ensure that UK law enforcement agencies complied with the terms of RIPA, RIP(S)A, CPIA and its Code of Practice (1997) minimum standards for the handling of Covert Human Intelligence Sources have been developed and updated to move law enforcement on to yet a higher level of professionalism than that which is required by the legislation.
- 4.1.3 These standards have been adopted by all police forces in the UK, the national agency and HMCE. After the merger of IR and HMCE, HMRC adopted these standards.

⁴³ Parliament (2002) Regulation of Investigatory Powers Act 2000. Chapter 23. London: The Stationery Office., Part II, Section 26, Paragraphs 8 a-c.

⁴⁴ Scottish Parliament (2002) Regulation of Investigatory Powers (Scotland) Act 2000 London: The Stationery Office Section I, Paragraphs 7 a-c for the specific wording that applies in Scotland.

Compliance with Standards and Adherence to Doctrine

4.2 Standard Operating Procedures and Local Instruction

- 4.2.1 Access to guidance on these standards is restricted to those working within the CHIS discipline. This guidance includes a recommendation that law enforcement agencies should produce internal policies for staff [not employed in the CHIS discipline] which ensures compliance with The Act and The Codes. In 2003, HMCE produced a new section for its intranet based Law Enforcement Handbook to give instructions concerning dealings with all human sources of information. This has been updated on a regular basis since its publication and provides useful directions for generalist staff as well as fulfilling the requirements of the national standards. After the merger of IR and HMCE the former HMCE Law Enforcement Handbook was incorporated into the new HMRC Enforcement Handbook.
- 4.2.2 In 2005, HMRC created and issued a bespoke set of guidance to specialist CHIS-handling staff. This guidance is written in departmental language, covering subjects such as Public Interest Immunity, tradecraft and CHIS operating outside the UK. HMRC does not currently have guidance in the same format that SOPs provide to their counterparts in some forces and the national agency.
- 4.2.3 Although there were variations between the SOPs created in the forces and the national agency they all aimed to provide step by step guidance for specialist officers in the CHIS field.

4.3 Structure

- 4.3.1 The establishment of Dedicated Source Units (DSUs) has been recommended to police forces for the management of CHIS, but they are not mandatory.
- 4.3.2 HMCE had introduced dedicated units, called SMUs, for the management of CHIS.
- 4.3.3 At merger, HMCE had a number of regional SMUs responsible for CHIS operations in the United Kingdom. The inspection found the structure of these SMUs met the minimum standards. In addition to these domestic SMUs, the International SMU, has a remit to manage CHIS operations overseas. This SMU is not a dedicated source unit.
- 4.3.4 Historically, IR did not employ CHIS handling as a major part of its intelligence gathering activity. The former IR CHIS management capability was absorbed into the former HMCE's SMU structure.
- 4.3.5 HMRC has three nominated Authorising Officers (AOs) at Senior Intelligence Manager level. Each has a nominated geographical area for which they have responsibility. However, they each cover for their colleagues' absences as required.

4.4 Staff

4.4.1 HMRC Staff working in posts specified by RIPA are as follows:

'Authorising Officer' [AO] is the person who is designated under S.29 (1) RIPA 2000 to have power to grant authorisations for the conduct or the use of a covert human intelligence source.

'Controller' means the person designated under S.29 (5) (b) holding an office, rank or position with the relevant investigating authority who will have general oversight of the use made of the source.

'Handler' means the person referred to in Section 29(5) (a) of the 2000 Act holding an office, rank or position within the relevant investigating authority and who will have day to day responsibility for dealing with the source on behalf of that authority, and for the source's security and welfare.

4.4.2 HMRC has duly appointed officers to undertake the roles and responsibilities as described above.

4.4.3 Before December 2004, the former HMCE (Senior Intelligence Officer) SMU Team Leader acted as AO. However, AO responsibility has now been removed from them and given to the Senior Intelligence Managers who previously had no role in the CHIS authorisation chain. The team leaders are no longer within the RIPA authorisation structure, although they take responsibility for day to day supervision of handlers and controllers. They also take responsibility for QA, management and development of staff and liaising with operational teams. Whilst this additional layer of supervision may be reassuring for the Department it does appear to be surplus to requirements. Coupled with the relatively low number of CHIS that are currently active, this suggests an over managed and relatively inactive resource.

4.4.4 HMRC is due to lose over 1,200 officers when the posts are transferred to SOCA in April 2006 and over 400 of these will come from the Intelligence Directorate⁴⁵. This will have a significant impact upon the capacity and capability of SMUs. The losses across CHIS Ops are not evenly spread across each of the UK based SMUs.

4.4.5 During interviews in November 2005 neither CHIS Ops managers nor HMIC had been provided with a succession plan detailing how the Department would deal with the losses. In the absence of this, there was evidence in one SMU that a local policy had been devised whereby the AO had already sought to delay the release of those officers that had elected to transfer to SOCA until replacement staff had been recruited. Although it is not known if this policy could be applied in practice, it highlights the need for HMRC to produce a considered succession plan for its CHIS staff at the earliest opportunity.

⁴⁵ All the figures on the numbers of staff moving to SOCA in this paragraph are based on the lists of staff who had elected to transfer to SOCA and had been accepted.

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- 4.4.6 At the time of inspection all operational SMU staff were former HMCE officers. Subsequently, officers from the former IR attended CHIS training courses in 2005, but none had yet been posted to an SMU. The SMUs' priorities were still based on former HMCE commodities such as class A drugs and tobacco smuggling and they only use CHIS who provide information in respect of these Departmental intelligence requirements. The inspection revealed that HMRC's CHIS Ops are conscious of this imbalance and a recent internal report has made recommendations to recruit more officers with a broader skills base to reflect its new business priorities.
- 4.4.7 Some police forces conduct periodic mandatory welfare assessments of CHIS practitioners. HM Inspector views this as good practice. At the time of inspection, HMRC did not carry out any health assessments of its CHIS Ops officers.
- 4.4.8 Interviews with SMU staff and managers raised some concerns over the recruitment procedure for SMUs. Of the officers recently selected for CHIS-handling roles, only one successfully completed the mandatory CHIS training course. Selection is by way of an open, cross-HMRC advertisement, followed by paper-sift of competency based applications, with the option of an informal interview. Officers may be appointed who are unsuitable for the demanding roles of handler or controller. In order to ensure they recruit officers with the requisite skills and aptitude to be successful CHIS practitioners, other law enforcement agencies have found significant benefit from conducting one-day assessment centres for potential recruits. There is no real substitute for experience in the work-place and other agencies find recruitment followed by a probationary period a useful method for consistency in staff selection.

4.5 Record Management

- 4.5.1 The lack of a networked Information Technology (IT) infrastructure to support CHIS processes in the former HMCE was identified in 2002 and 2003. When HMIC inspected the Department, SMUs were still awaiting the introduction of an electronic CHIS management system.
- 4.5.2 In the absence of an electronic system, HMRC is using a paper-based record management system, similar to that being used by one of the inspected forces. Comparing these systems to the IT solutions utilised by the other inspected forces and the national agency, the latter demonstrated clear benefits:
- The use of a paper-based system is significantly more time-consuming and labour intensive than using an electronic system. One HMRC SMU expressed concern about having to re-write risk assessments for every conduct authority.

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- In the forces and national agency where Operational Security (OPSY) Officers are employed, an IT based system provides the OPSY immediate access to CHIS records without leaving a footprint. This raises levels of management oversight and intrusive supervision, leading to greater accountability and integrity of the system.
- The electronic system allows for more readily available statistical data to inform the performance management process.
- The IT systems had specific functionality whereby key dates i.e. 'use and conduct' authorities, reviews, risk assessments are all subject to an electronic prompt.

4.5.3 HMRC has been developing its own electronic system to support CHIS operations. The introduction of this system has been beset by problems and has yet to be completed. It is seen as a departmental priority and HMRC management anticipate that the system will be fully operational by the end of March 2006. HM Inspector supports this action.

4.5.4 As a temporary measure, HMRC has introduced a confidential system, but it does not have the benefits of a full CHIS management IT system.

4.6 Handlers' contact with CHIS

4.6.1 The standards for CHIS handling require that every contact with a CHIS be fully documented and recorded.

4.6.2 The application of this requirement in an operational environment has sometimes been overly bureaucratic, with areas of duplication.

4.6.3 Clear guidance on this issue and a number of other tradecraft techniques would be formalised and promulgated by the production and distribution of SOPs.

4.7 Support

4.7.1 The levels of support provided to the dedicated HMRC's SMUs were impressive. These structures took account of the requirements for handlers and CHIS to be protected from potential compromise.

4.7.2 During interview, HMRC handlers demonstrated thorough understanding of the necessary tradecraft measures required to ensure contacts and meetings were covert.

4.7.3 For logistical and other reasons, it is more difficult to fully utilise the full range of support structures when operating abroad, but HMRC are actively seeking pragmatic solutions to tradecraft issues associated with overseas activity.

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4.8 Recruitment of CHIS

- 4.8.1 A key requirement for any effective source management system is the availability of CHIS that are capable of being given intelligence gathering tasking.
- 4.8.2 CHIS were assessed for their potential to provide information in support of identified Departmental business priorities, such as Class A drugs and tobacco smuggling.
- 4.8.3 The police service and the national agency have implemented NIM in order to manage business. Strategic assessments of crime and disorder are used to direct finite resources against agreed national and local priorities. Regular tasking and co-ordinating meetings review potential opportunities for addressing intelligence gaps and direct specialist resources against them. As part of an overarching intelligence strategy, forces and the national agency make specific requests of source management units to recruit CHIS in order to support the aims and objectives of operational teams.
- 4.8.4 HMRC has embraced the principles of NIM in accordance with its Business Delivery Model and has developed a risk programme, the aim of which is to devise a national risk picture across the whole tax system and provide an overview of the resources deployed against risks.

4.9 Use and Conduct and Risk Assessments

- 4.9.1 For every CHIS authorised, the AO must set out in writing the exact details relating to the proposed 'use' and 'conduct'. In doing so, the AO must consider the relevant Human Rights Act 1998 Articles of Legislation including Article 2 right to life, Article 6 right to fair trial and Article 8 right to respect for private and family life. The AO must also consider the principles of justification, necessity and proportionality:
*"Any public authority deploying a source should take into account the safety and welfare of that source, when carrying out actions in relation to an authorisation and tasking, and to foreseeable consequences to others of that tasking. Before authorising the use and conduct of a source, the authorising officer should ensure that a risk assessment is carried out to determine the risk to the source of any tasking and the likely consequences should the role of the source become known. The ongoing security and welfare of the source, after the cancellation of the authorisation should also be considered at the outset"*⁴⁶.

⁴⁶ HOME OFFICE (2002) *Covert Human Intelligence Sources: Code of Practice*: TSO: London; Paragraph: 4.36

- 4.9.2 Specialists in source management should fully understand their responsibilities with regard to the risks involved, particularly where sources may be compromised and their personal safety is under threat. They should be familiar with the principles of 'duty of care' that are highlighted in pertinent case law such as Osman and Osman vs UK and Swinney and another vs CC Northumbria.
- 4.9.3 The RIPA Code of Practice states: "*Public authorities should ensure that arrangements are in place for the proper oversight and management of sources. Including appointing individual officers as defined in section 29 (5) (a) and (b) of 2000 Act for each source i.e. Handlers and Controllers*"⁴⁷
- 4.9.4 Handlers are responsible for bringing to the attention of their controllers "*any concerns about the personal circumstances of the source, insofar as they might affect a) the validity of the risk assessment, b) the conduct of the source and c) the safety and welfare of the source*"⁴⁸ and "*Where deemed appropriate, concerns about such matters must be considered by the Authorising Officer, and a decision taken on whether or not to allow the authorisation to continue*"⁴⁹.

4.10 Rewards for CHIS

- 4.10.1 Appropriate levels of reward payments to CHIS are a consideration in the CHIS handling standards. Reward payments are calculated accordingly to reflect the effort, risk and time taken by a source to effect a result and the value to law enforcement of that result.
- 4.10.2 In a 1996 report into police integrity, HMIC stated: "*Where informants demand payment, they usually expect it quickly and Her Majesty's Inspector is of the view it is an unacceptable burden on handlers for them to have to explain to informants the vagaries of their force accounting systems*"⁵⁰. This applies equally to HMRC as it did to the police service.
- 4.10.3 It was of concern to the inspection team, therefore, to learn of examples from SMU staff of significant delays in processing rewards. At the time of inspection, CHIS Ops managers were aware of this and were taking steps to rectify this situation. Delays in the payment of rewards were clearly evident from the examination of CHIS files in HMRC SMUs.

⁴⁷ *ibid*: Paragraph 4.33

⁴⁸ HOME OFFICE (2002) Paragraph 4.37

⁴⁹ *ibid*: Paragraph 4.39

⁵⁰ HM INSPECTORATE OF CONSTABULARY (June 1999) *Police Integrity: Securing and Managing Public Confidence*: London: Home Office: Page 24.

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- 4.10.4 One of the inspected forces also experienced delays in making payments to CHIS. In this case, handlers were having to make payments to CHIS from their own funds in order to sustain the relationship and intelligence flow. This practice, highlighted in HMIC's *Police Integrity* report as being unacceptable⁵¹, and is potentially damaging to the integrity of the individual and the organisation. Whilst delays may well tempt officers to engage in practices of this nature, there was no evidence of this taking place in HMRC.
- 4.10.5 HMRC's National Source Unit (NSU) processes all reward applications and calculates the final size of the payment. SMU officers recommend potential rewards based on precedence and experience from within their own unit. Many handlers find it very difficult to establish the reasonable and appropriate level of reward in any given circumstance. This leads to the submission of applications for inflated sums which the handlers, then expect to be bartered down by the NSU.

4.11 Training

- 4.11.1 Minimum standards of training to be achieved by all staff employed in the management and control of CHIS have been identified.
- 4.11.2 It was evident that all CHIS practitioners interviewed in the police service, the national agency and HMRC had received training to the requisite levels. However, the specific problems highlighted in paragraph 4.13 reveal an inadequate level of understanding amongst a number of HMRC CHIS Ops staff about several CHIS management issues.

4.12 Assurance

- 4.12.1 In 2002 it was recommended that HMCE establish a Quality Assurance Bureau (QAB) within Law Enforcement. HMCE created a QAB and the inspection of CHIS processes has been carried out since April 2003. All SMUs have been inspected at least once.
- 4.12.2 A number of the QAB reports on UK SMUs comment that local management conduct regular ethical and VFM audits as part of CHIS reviews. Furthermore, a QAB report on the international CHIS Ops activity questioned the value for money of some of these sources. The request for local management to conduct VFM assessments reflects the fact that HMRC has no corporate process for anyone outside the SMU structure assessing the Value For Money of its CHIS. This contrasts with the role of the independent OPSYs employed in some police forces and the national agency. The OPSYs are responsible for proactively assuring the integrity of the CHIS management system including all aspects of VFM. HMRC may wish to consider including VFM assessments as part of the QAB's remit or introducing a similar OPSY system.

⁵¹ HM INSPECTORATE OF CONSTABULARY (June 1999): Page 24.

4.13 Significant shortcomings of HMRC CHIS management

- 4.13.1 Where a source whose use has been assessed as particularly risky by the Authorising Officer of a law enforcement agency, there is a presumption that such persons will not generally be used. Such a source will only be used in the most serious cases and only following re-assessment.
- 4.13.2 The examination of HMRC CHIS files, raised a number of causes for concern regarding HMRC's ability to manage CHIS. Due to the sensitive nature of these issues, details are not specific in this report.
- 4.13.3 HM Inspector recommends that an urgent full audit is undertaken of all HMRC's CHIS files. HM Inspector recommends that the audit is conducted at the earliest opportunity by an independent team. The options are:
- i) HMIC-led team comprising HMRC Criminal Investigators or other specialists seconded to HMIC.
 - ii) A team comprising members of an external credible agency.

Chapter 5

Other Human Intelligence Sources (HumInt, Informers, 3rd Party Information and Confidential Contacts) – Systems and Compliance

5.1 Background

- 5.1.1 RIPA introduced a legislative framework for law enforcement agencies' and public bodies' relationships with CHIS. There is no parallel legislation or code of practice on how these bodies should deal with information from other members of the public, members of trades or businesses. Human contacts, particularly those who wish not to be identified and provide information to law enforcement agencies have presented significant challenges and stimulated enormous debate on how they should be handled and classified.
- 5.1.2 A category of individuals known as Confidential Contacts, are defined in the ACPO standards used by law enforcement agencies as "...an individual or member of an organisation who discloses information to the police from which an individual can be identified and there exists personal, professional or other risks by their doing so"
- 5.1.3 In his report published in July 2003, Mr Justice Butterfield also considered this issue and praised ACPO for producing the document *Confidential Contacts*. He stated that "*since ...[the production of the document]... there has been a distinct improvement in police forces, and fewer confidential contacts who might merit CHIS status have been discovered*"⁵². Mr Justice Butterfield, however raised concerns over the method by which law enforcement organisations could monitor those persons drifting towards CHIS status (status drift)⁵³.
- 5.1.4 ACPO responded to Mr Justice Butterfield's concerns around monitoring status drift. A brief section on the status drift of 'members of the public' (including what they had previously defined as Confidential Contacts) was added to the available guidance for the handling of CHIS.
- 5.1.5 However, during the course of the inspection it became evident that a lack of clarity around the issue still pervaded the law enforcement agencies visited. The following paragraphs set out these issues.

⁵² THE HONOURABLE MR. JUSTICE BUTTERFIELD (July 2003): Paragraph 10.86

⁵³ *ibid*: Paragraph 10.79

5.2 The Police Service and the National Agency

- 5.2.1 The expectation of ACPO was that there would be small numbers of people identified as Confidential Contacts. However, across the police forces inspected, there remained a disparity in the number of confidential contacts that were registered. Two of the forces were broadly in line with this guidance, however, the third had registered a significant number more than had been anticipated. This latter example raised concerns regarding sources who were potentially operating as CHIS, that were not subject of the management and oversight had they been formally registered.
- 5.2.2 Interviews of non specialist officers in police forces revealed that some were unclear how to deal with human sources of information, although most knew where to go to obtain suitable advice and guidance. The front-line interaction between the police service and members of the public on the streets, is increasingly being provided by PCSOs. A natural and highly desirable consequence of this is that these officers develop links with local communities. It is important, therefore, that these officers receive training in how to deal with the human sources of information. However the majority of PCSOs had received no training or instruction on how to do this. An example in one of the forces raised concern.
- 5.2.3 Some investigation and intelligence officers revealed that they were also confused regarding the procedures for dealing with Confidential Contacts which resulted in many failing to refer potential sources of intelligence to appropriate units. This must have a detrimental impact on the intelligence gathering capability of any law enforcement agency.
- 5.2.4 Each of the forces inspected had a system in place to identify where information had been recorded by a repeat contact. Each of the forces had a force-wide register, which was monitored regularly by a trained controller. However, due to the lack of training for some officers, already alluded to, not all contacts were being recorded on these.
- 5.2.5 The national agency also maintains regional registers in its intelligence bureaux. The impending launch of SOCA provides an ideal opportunity not only for this, but for all the precursor agencies to merge their respective registers.

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5.3 The Inland Revenue

- 5.3.1 The terms of RIPA 2000 were not restricted to law enforcement agencies, but applied to a wide range of public bodies including IR⁵⁴. Therefore, it was incumbent upon the Department that those informers that it dealt with did not drift to CHIS status. In response to this, IR produced their own guidance to RIPA 2000. In addition, the only people in the former IR dealing with CHIS (known in IR parlance as 'informers') were in the Special Compliance Office (SCO).
- 5.3.2 Although the IR guidance does not refer directly to status drift, it does clearly state the difference between an informer and a CHIS and reinforces the importance to staff of understanding these differences and the potential consequences of failing to do so.
- 5.3.3 In 2004, IR issued instructions on the practicalities of handling informer information. It deals with the initial processing and retention of third party information from informers received directly in an area or local office by post, telephone calls or counter callers. However the details of the informer are not recorded on any computerised systems to enable an independent review of all contact with informers for status drift.
- 5.3.4 Guidance on RIPA instructs staff to make a record of contact with informers.
- 5.3.5 Despite the RIPA guidance clearly defining CHIS, there is a widespread misunderstanding of the RIPA definition of a CHIS across the former IR estate. The *Covert Human Intelligence Sources Code of Practice*⁵⁵ states that CHIS authorisation is not mandatory in situations where a person is tasked to do something that does not require them to establish a personal or other relationship for a covert purpose. However, most non specialist staff incorrectly assumed that an individual who was 'tasked' would become a CHIS whilst, conversely, those who were not tasked would not qualify for CHIS status. This fundamental misunderstanding of RIPA and the Code has resulted in officers failing to ask informers to clarify or expand on information they provide, resulting in a subsequent loss of potential intelligence for the Department⁵⁶.
Of greater concern, this confusion could lead to people who volunteer information based on a covert relationship to the Department not being registered as a CHIS and therefore not being handled with the required authorisation or control.

⁵⁴ See PARLIAMENT (2002) Regulation of Investigatory Powers Act 2000. Chapter 23. London: The Stationery Office. Schedule 1, Part II.

⁵⁵ HOME OFFICE (2002) *Covert Human Intelligence Sources: Code of Practice*: TSO: London: Paragraph: 4.29

⁵⁶ See Chapter 7, on page 35.

- 5.3.6 The underlying cause for former IR officers' confusion on this issue was around training and communication. It is suggested that there was a lack of structured, dedicated training provided in respect of informers. Many focus groups of former IR staff had no recollection of ever receiving any such training on this topic. Instruction about how to deal with informers was communicated by way of memos cascaded through the line management chain. This means of communication is routinely used by management to impart instruction on a wide range of operational activity. It was evident that a majority of officers interviewed were concerned about this practice. Individuals felt unable to dedicate the requisite time and attention to these topics at their desks that they would if they were delivered in a more traditional learning environment. Moreover, management cannot guarantee that all their staff have read and understood the instructions. Staff contrasted this to the management approach to personnel issues, health and safety and statutory diversity training, accepted by all as necessary and important issues, which were not imparted by way of cascaded memos. Instead officers were sent on compulsory courses to ensure that all were sufficiently trained.
- 5.3.7 IR demonstrates an awareness of 'duty of care' by instructing staff to keep all records securely in order to protect the identity of the informer. Further security measures are set out for those maintaining the RIAT spreadsheet of third party information.

5.4 HM Customs & Excise

- 5.4.1 The failure by HMCE to manage the status drift from 'trade source' to CHIS was the subject of criticism following the loss of a number of high profile HMCE trials between 1998 and 2001 and subsequent abuse of process applications heard by Mr Justice Grigson at Liverpool Crown Court in 2002.
- 5.4.2 This led to a review of criminal investigations and prosecutions conducted by HMCE. In his report, Mr Justice Butterfield commented: *"the failure to identify the gradual drift and change in status of Alf Allington from registered warehouse keeper to participating informant was a key factor in what went wrong [in HMCE's failed London City Bond Case]. That in turn led to a failure to register Alf Allington as a participating informant, a failure to manage him in compliance with informant guidelines and a failure to maintain reliable records of his activities and the nature and extent of the information given by him"*⁵⁷.
- 5.4.3 Past inspections of HMCE have highlighted the issue of the Department's handling of human sources of information.

⁵⁷ HONOURABLE MR. JUSTICE BUTTERFIELD (July 2003): Paragraph 8.10

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- 5.4.4 In mid 2003, HMCE produced a draft policy in response to Butterfield's concerns. The policy outlined a structured system for all officers dealing with information provided by individuals that may link to criminal offences or regulatory breaches. It would enable the Department to record the details of the source of the information in a retainable, durable and retrievable form and so that technical, legal and disclosure issues could be properly assessed and dealt with. The system was designed to provide HMCE with a central record of all persons providing attributable verbal information and a monitoring process for potential status drift.
- 5.4.5 Mr. Justice Butterfield had sight of the draft HumInt policy and, in his Review, stated:
- "In my view the proposed scheme is much to be welcomed. For the Customs officers receiving information it provides clarity and simplicity. Their duty is simply to record and report what they are told. They are not called upon to make any assessment about the status of the source or the reliability of the information. Those decisions are to be made in all cases by experienced officers specialising in such work and dedicated to that task alone. If operated properly the scheme not only identifies those who might be providing information as CHIS but guards against status drift"⁵⁸.*
- 5.4.6 HMCE introduced the HumInt system on 1 September 2003 and established the NHC. HumInts are defined as *"all persons who give information to the Department relating to a possible criminal offence or regulatory breach (including any offences that may ultimately be dealt with under 'civil' provisions) or regulatory breach. The term HumInt covers all those who provide information to the Department whether they receive such information in the course of their trade, profession, business or employment and who, out of civic duty, volunteer information or those we categorise as ... CHIS"⁵⁹*. All HMCE officers who receive information from HumInts (Receiving Officers) are required to record the information in a durable, retrievable form and submit a report of the contact on an HCR form to the NHC along with any associated intelligence report forms.
- 5.4.7 The NHC is staffed by trained HMCE CHIS controller/handlers (Assessors) who consider the identifying details of the HumInt, the nature of the information, the reason why the HumInt is offering the information, and the relationship between the HumInt and the subject of the information. The NHC assessors review the contact in conjunction with any other previous HCRs for the HumInt and then

⁵⁸ HONOURABLE MR. JUSTICE BUTTERFIELD (July 2003): Paragraph 10.93

⁵⁹ HM CUSTOMS & EXCISE (20 August 2003) *LE Handbook Version 37: HUMINT*: Page 3.

make a determination as to their status. If the HumInt is considered not to be a CHIS, the assessor advises the receiving officer and their line manager of the decision, and authorises the dissemination of the intelligence. Conversely, if the assessor decides that the HumInt is a CHIS, or a potential CHIS, the HCR is referred to the appropriate SMU for consideration and further assessment. The NHC also provides advice on how HumInts should be handled and acts as a single point of contact in the Department for general HumInt enquiries.

5.5 HM Revenue and Customs

- 5.5.1 On 21 April 2005, HMRC made the following announcement on its intranet "*Following a training and education programme, the HumInt procedures will be introduced, on a phased basis, to all staff in HMRC*". It also announced that the HumInt system would be introduced in other units on their completion of the mandatory training programme, although no target dates were set.
- 5.5.2 Although the announcement refers to a plan for a phased, methodical, implementation of the HumInt system to other units in the Department, eight months later still no such plan had been finalised. In the absence of a finalised implementation plan, on 3 October 2005 an internal memo was issued by one unit to all of the unit's staff, outlining the HumInt system and instructing them to adopt it, with immediate effect. This instruction provides staff with a link to the relevant HCR on the intranet. This bespoke version of HumInt is a consequence of the lack of a structured implementation plan.
- 5.5.3 Another consequence of the lack of a developed implementation plan has been the uncertainty expressed by many officers regarding whether their units will adopt HumInt or whether they will retain their precursor systems. This uncertainty even extended to Senior Civil Service managers in some areas of the former IR.
- 5.5.4 Interviews across those units to which HumInt had been introduced, provided a number of examples of handling of information provided by members of the public that undermine HumInt policy:
 - 5.5.4.1 A number of officers stated they had received telephone calls from HumInts who complained that they had previously spoken to other HMRC officers but that officer had refused to take any information from them. Some of these people felt they had been moved "*from pillar to post*" and were almost dissuaded from supplying this information at all. The officers interviewed felt, this not only breached Departmental guidance but displayed a distinct lack of professionalism.

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- 5.5.4.2 Another common practice, identified by a range of officers in focus groups, is the referral of HumInts to confidential hotlines to avoid responsibility for submitting an HCR. There is a potential that these callers may not contact the hotline numbers, with the resulting loss of intelligence for the Department. Conversely, those who persevere and do contact a confidential hotline will be logged anonymously thus circumventing the HumInt objective of monitoring repeat callers.
- 5.5.4.3 Other officers revealed that, on occasion, the HumInt system is by-passed by obtaining witness statements. In many cases, these have no evidential value, but receiving officers believe it to be a simpler and less time-consuming process than completing an HCR and intelligence log. In other cases, officers taking a witness statement whilst conducting legitimate enquiries into an on-going investigation may receive additional information about a similar matter. If they are confident that the source will become a witness, where the information proves to be accurate, they will research the matter themselves and then may obtain a further statement.
- 5.5.4.4 During interviews, it became apparent that there was confusion amongst officers about how anonymous information is dealt with in the HumInt system. If no personal details are obtained from the person then the intelligence should be disseminated on an intelligence log but it is not necessary for the officer to complete an HCR. However, a number of officers were under the misapprehension that they were still required to submit HCRs in such cases.
- 5.5.4.5 At the time of inspection, attributable letters and e-mails from members of the public were treated as anonymous and therefore fell outside the scope of the HumInt system. HMRC management has undertaken a volumetrics exercise that indicates the quantity of written HumInt material is likely to equal the HumInt telephone contacts and are reviewing their policy in light of this. Risk assessments for such material will be necessary, within the remit of the HumInt instructions, if the Department wishes to adhere to the principle of recording contact in relation to the provision of information.
- 5.5.4.6 If the HumInt system is to provide integrity as an auditable method of recording third party contact with the Department and monitoring potential status drift, it is essential that all such contacts are recorded by NHC.

Evidence from VAT assurance officers revealed that most were not submitting HCRs even though some received attributable information on a regular basis. These officers decided that this information was malicious and of no value to the Department. In addition to monitoring status drift, the HumInt system's purpose is to log all third party allegations received by the Department to provide a comprehensive record of such contacts for disclosure purposes. Therefore, even if the content of the information passed to the receiving officer may appear to be of no intelligence value, the fact the contact is made may need to be disclosed in court at a later date. If this practice is not rectified, it could undermine the foundations of the HumInt system.

- 5.5.5 No individual or organisation can, under UK law, guarantee an individual absolute confidentiality from disclosure of their identity by a UK court. As the HumInt Instructions in the Enforcement Handbook rightly state "*A promise of complete confidentiality cannot be given to any individual who provides information to the Department, whether an authorised CHIS or not. The Department will seek to protect them and their information within our own systems but ultimately the Court may order disclosure*"⁶⁰. However, the majority of officers who had attended HumInt training seminars felt that the instructors over-emphasised the need to warn potential HumInts about this. Consequently, rather than stressing disclosure would be very unlikely, and that in most instances confidentiality would be protected by the Department, some officers' stark warnings have dissuaded potential HumInts from passing on their information. This is analogous to the safety briefing airline staff must give to passengers to advise them of the use of appropriate safety equipment in the 'unlikely event of an emergency'. In any event, concerns over the identification of confidential sources of information can be dealt with under Public Interest Immunity procedures.
- 5.5.6 Throughout the inspection, issues of the marketing of, and training for, HumInt were raised as causes for concern. Although those who have developed and manage the HumInt system are enthusiastic about it and the benefits it will bring to the Department, this enthusiasm has not permeated the whole organisation. CHIS Ops management have themselves reflected on this and have concluded there is a consequent lack of awareness and fear amongst many officers. Few officers displayed any understanding of the potential value that HumInt can contribute to the intelligence system and operational effectiveness of the Department. The delivery and content of HumInt training is largely the cause of this.

⁶⁰ HMCE LE Handbook – Humint Appendix A: Para 7.

Other Human Intelligence Sources

- 5.5.6.1 Shortly after the decision had been taken to introduce HumInt to the former HMCE in 2003, a series of awareness seminars were arranged, at short notice. These seminars were aimed at those in the former Law Enforcement Directorate who were designated as having the highest priority. They were attended by the former HMCE pay band 7s and 9s, who, due to the large numbers of staff who needed training in a short time, were expected to take away the message and impart it to their colleagues by way of cascade or fountain training. Instructions were also included in the Law Enforcement Handbook on the HMCE intranet. Subsequently more seminars were arranged for representative officers across HMCE's units and then in 2005 for representative officers from parts of the former IR. Interviews across these units have also confirmed that those officers who attended the seminars were tasked with cascading the training to their colleagues. The inspection has found that Butterfield's concerns that cascade training "*... may save on cost but undoubtedly carries the risk of dilution and distortion of essential messages*"⁶¹ are justified.
- 5.5.6.2 Evidence from focus groups revealed that staff who attended the seminars were not trained trainers, and many said they had concerns over the content. Some officers who did not have a law enforcement background, stated that because no exemplars were given from their areas of work, they neither understood the HumInt system nor saw how to apply it to their work. Other officers felt that the focus of the training was on the historical problems HMCE had experienced and spent too much time on the completion of the form rather than focusing on the benefits of the system. The combined consequence of all these factors was that officers who were cascade trained received diluted or distorted messages, which they then passed on to their colleagues. Many officers, who received either the seminar or cascade training, came away with the message that if they made a mistake in their handling of a HumInt their jobs would be on the line. During interviews a majority of officers stated the training had made them more fearful of dealing with human sources of information.
- 5.5.6.3 HumInt training has now been incorporated into all induction and 'upskilling' courses given to officers in those directorates that have introduced HumInt.

⁶¹ HONOURABLE MR. JUSTICE BUTTERFIELD (July 2003): Paragraph 10.112

Other Human Intelligence Sources

- 5.5.6.4 CHIS Ops management have recognised that the previous training was ineffective and are developing a new HumInt training package that will be given progressively to those units to which HumInt is being introduced for the first time. It will also be given to those units that already use the HumInt system. This compulsory training package will be IT-based, supported by a DVD, and will include exemplars for a wider range of Departmental activity and will necessitate the completion of an auditable pass or fail test. Although delivery dates have not been finalised, training materials are due to be accessible by late 2006, when HumInt managers recommend that the rest of HMRC will adopt the system.
- 5.5.7 The HumInt instructions include an aide memoire that briefly outlines the HumInt procedures. A small number of detection officers had been issued with a durable pocket-sized version of this, which they referred to during the course of their duties. Although the majority of officers interviewed had not been issued with the aide memoire, there was a consensus that it would be a useful aid for them in circumstances where they could not access the on-line HumInt instructions.
- 5.5.8 Some IR Call Centre managers said that under present Service Level Agreements (SLAs) and performance indicators their operators would have insufficient time to complete HCRs. Interviews at former HMCE call centres showed that a more pragmatic approach had been adopted. In order to ensure sufficient time is allocated to deal with the small number of HumInt calls, all time-consuming calls (including HumInt) are identified by the operators and re-directed to their team leaders, who are not subject to the same stringent targets. This approach has been shown to work with a small number of HumInt calls, but the Department has to address the issue of SLAs to build in sufficient time for its operators to deal with the necessary documentation.
- 5.5.9 There was a consensus amongst the HumInt assessors interviewed at the NHC that the majority of HCRs they received were of a poor quality and contained insufficient information. There is no requirement for these to be subject to any quality control process prior to submission. Many of the HCRs received by NHC contained such a dearth of information that it was not possible for the assessors to conduct detailed risk assessments and in some cases the information could not even be entered onto the system. HM Inspector recommends that HMRC consider the introduction of a quality control regime.

Other Human Intelligence Sources

- 5.5.10 To manage the performance of the HumInt system, it is necessary to monitor which units are submitting HCRs and those which are not. The HumInt instructions elaborate on this: *"The National HumInt Database (NHD) can supply a variety of management reports, which may assist the assurance process"*⁶². However, it is possible to submit the form incomplete. As a consequence, the NHC are unable to provide any meaningful comparative performance information. The NHC should explore whether the current form can be amended so that it cannot be saved and submitted until all the mandatory fields are completed.
- 5.5.11 In order to address omissions and inconsistencies on the HCR, the Department should develop a structured Quality Control (QC) process. In the absence of this, the inspection revealed that local managers were adopting a wide range of methods to monitor HumInt referrals within their own offices. These vary from asking all receiving officers to copy them into the emails sent to NHC to merely noting the result of the assessment from NHC. Most kept some form of establishment file with either an electronic or paper spreadsheet showing the numbers and results of HumInt referrals. As there is no requirement for the receiving officer to refer any material for scrutiny before making the NHC referral, the contents are not subject to QC before submission. Evidence from a series of interviews in one office showed that the manager's records of the number of HCRs submitted to the NHC were at variance to the recollection of the staff. Another office visited, where an ex-CHIS handler was in a supervisory position, displayed markedly greater oversight than had been seen elsewhere.
- 5.5.12 The HumInt instructions state: *"Assurance programmes should be agreed within individual businesses commensurate with the frequency of contact that staff have with HumInts and the level of assessed risk"*⁶³. These assurance programmes were intended to provide an internal audit of the HumInt system in each branch of the former HMCE LE and the instructions continue *"Band 11's in Law Enforcement have a responsibility to ensure that an annual internal assurance programme is conducted in each Branch. Any recommendations proposed must be reviewed for implementation within 4 months of the date of the assurance report"*. LE branches' compliance with the requirement for branches to undertake annual internal assurance is patchy.

⁶² HM CUSTOMS & EXCISE (20 August 2003): Appendix B.

⁶³ HM CUSTOMS & EXCISE (20 August 2003): Appendix B.

- 5.5.13 HMIC requested copies of all former HMCE LE Branch/Region assurance reviews/reports. HMRC only provided two reports, one produced in March 2004 relating to the five London Region branches of LE Investigation and one dated July 2005 pertaining to an LE Intelligence branch. Most of the recommendations made in these reports were proposed improvements of the HumInt system itself and it would be expected that these would have been forwarded to CHIS Ops management for consideration. CHIS Ops management have recently stated, however, that they had not had sight of the reports produced until the last few months, over a year after the London Region composite report was produced. As these assurance reports contain valid recommendations to improve HumInt, HM Inspector welcomes the belated decision by Criminal Justice Enforcement Standards to ensure that future reports are copied to CHIS Ops management.
- 5.5.14 Front-line officers have consistently praised the HumInt assessors for the assistance they have provided and their efficiency in completing assessments.
- 5.5.15 If the HumInt system is applied across HMRC, the improvements proposed by CHIS Ops implemented and the areas of non-compliance addressed, it will provide the Department with the safeguards it requires to prevent status drift. However, there is potential for the HumInt system to have a stronger role in developing and streamlining HMRC's information management processes. For instance, at present, receiving officers are required to submit an HCR, together with a draft intelligence log to NHC. If a decision is taken that this intelligence can be disseminated, the responsibility *"to identify the 'customer' for the intelligence, and ... ensure that the Intelligence is copied to the relevant ... [National Intelligence Unit]"*⁶⁴ is delegated back to the receiving officer. They are also required to complete and submit a number of different forms, in addition to the HCR to be able to enter the intelligence on the former HMCE intelligence database. The wider issue of intelligence management across HMRC was not considered as part of this inspection, but would be an area worthy of further consideration in due course.

5.6 Overview

- 5.6.1 Within HMRC, the national agency and police forces, there remains significant confusion concerning the use of human sources of information who are not CHIS. Such confusion would be largely eradicated by the production of a separate manual of standards dealing with this type of information.

⁶⁴ HM CUSTOMS & EXCISE (20 August 2003): Page 6.

Chapter 6

The International Dimension – Compliance

6.1 Background

- 6.1.1 The Act and The Code apply to the activities of UK officers employed overseas, the source they handle and the sources of overseas agencies when deployed in the UK. The management of any source overseas brings with it additional and unique challenges. Adherence to the general principles in the guidance for handling CHIS within the UK can often assist in the effective management of these challenges abroad.
- 6.1.2 In addition to the HMRC SMUs that handle UK based CHIS, there is a SMU that has responsibility for managing those CHIS based outside the UK. These are handled by OLOs, as one of their duties. As of January 2006, HMRC had OLOs posted across the globe. They are divided generally into a FLO network based in the European Union and a DLO network for the rest of the world. NCIS also manages a DLO network in the European Union and, although HMRC officers are seconded to these posts, these do not form part of this inspection.
- 6.1.3 The SMU managing CHIS based overseas comprises of a team leader and controllers, based in London. They share the responsibility for the management and oversight of CHIS activity undertaken by the OLOs geographically. From 1 May 2005, this SMU has been managed by a former HMCE Senior Intelligence Manager AO, who has additional responsibility for other SMUs.
- 6.1.4 With the spreading of organised crime across the world, the DLO and FLO networks provide an invaluable link within host countries. The OLOs develop networks with local governments, local law enforcement agencies and other agencies in order to exchange intelligence on criminal organisations, particularly those that involve UK citizens or impact upon UK interests. They also develop an understanding of the local cultural, legal, and procedural norms. They can facilitate UK investigations overseas, initiate upstream interdiction or indeed co-ordinate the various international aspects of an operation that may come to fruition within the UK. Whilst specific operations are sensitive, HM Inspector is aware of some outstanding results that have been achieved in recent times.
- 6.1.5 The DLO posts will transfer to SOCA on 1 April 2006; the FLO posts will remain with HMRC.

6.2 Compliance with RIPA and Code of Practice

- 6.2.1 HMRC seeks to adhere to the UK legal framework detailed in RIPA, CPIA, the ACPO and HMCE guidance and the Codes of Practice. However, there are inherent constraints as a result of operating in foreign countries. OLOs are of the opinion that UK legislation regulating or impacting on the handling of CHIS should take precedence over the judicial processes of the host country when these are in conflict. OLOs gave a number of examples where conflicts have occurred following judicially authorised covert law enforcement activity in the host country. In such cases, UK courts have made requests for full disclosure of material relating to the operation but the foreign judiciary have refused to comply. In order to avoid such difficulties in UK courts, especially where there is CHIS involvement, they look for opportunities for the law enforcement agencies in their host country to take 'upstream intervention'.
- 6.2.2 OLOs provided details of their CHIS handling practices. A number of these are not in accordance with the guidance for the handling of CHIS in the UK.
- 6.2.2.1 This is driven by the impact of host nation legislation, operating environment factors, resource constraints, logistical reasons and security contexts that can apply overseas.
- 6.2.2.2 In common with UK based handlers, OLOs expressed concerns over the significant delays in the processing of reward applications.
- 6.2.3 The problems that were evident from the examination of CHIS files (detailed at paragraph 4.13) were also found in some of the overseas CHIS files. The recommended audit of CHIS files should therefore include those retained at the SMU handling overseas CHIS and OLO posts abroad.

6.3 The Role of the OLO in CHIS Handling

- 6.3.1 Unlike UK based handlers, OLOs are not working in an SMU environment and they are not dedicated to CHIS handling. Of the six key activities/responsibilities in the job descriptions used in recent OLO recruitment exercises, none specifically referred to CHIS handling. There was a consensus amongst OLOs that they were expected to undertake too many wide-ranging tasks, source handling was not a significant priority and they had not received any instruction to say that it should be.
- 6.3.2 All OLOs have received accredited CHIS handling training, although these courses are designed for law enforcement officers operating in the UK. OLOs feel strongly that the complexities of operating abroad are worthy of a separate, bespoke training event, however, they feel they are considered a low priority for training and cited, as an example, that HumInt training was delivered to them over 12 months after its introduction.

Chapter 7

Proactivity

7.1 Specialist Activity – Proactivity

- 7.1.1 As of 1 December 2005, HMRC's SMUs covering the United Kingdom comprised of specially trained staff. Between them they were managing a relatively few number of CHIS. Whilst quantity should not be an isolated factor of assessment, this ratio is less than that of similar units in the national agency. One SMU in HMRC comprising a team leader, controllers and handlers was actually managing few CHIS. HM Inspector acknowledges that HMRC was re-assessing the continued authorisation of its legacy CHIS in advance of the formation of SOCA and as such it would be reasonable to expect that those SMUs, which were to lose the majority of staff to the new Agency may have reduced the number of authorised CHIS.
- 7.1.2 The annual staff costs alone for an operational SMU such as the example given in the previous paragraph would be considerable.
- 7.1.3 Although specialist staff within SMUs were aware of departmental objectives, they felt that business priorities were frequently changing, sometimes weekly. To be proactive, specialist units need clear direction in order to develop assets around well considered intelligence requirements in line with the departmental control strategy.
- 7.1.4 Even though there was an awareness of HMRC business priorities within SMUs, there was little evidence of a formalised tasking and co-ordinating process in order to exploit intelligence opportunities and provide additional support for operational requirements. Both established (police) and developing (SOCA) law enforcement agencies in the UK have adopted an intelligence-led approach to law enforcement. A core element of this is an increasingly robust tasking and co-ordinating process, whereby an analysis of problems identifies intelligence gaps that are then addressed through the exploitation of investigative assets.
- 7.1.5 HMRC Law Enforcement officers who have had experience of drugs investigations were well aware of the role and responsibility of dedicated SMUs. However, the majority working in other fields had less exposure to operations involving CHIS deployments and were often unaware of the potential benefits. Senior managers across the Intelligence and Criminal Investigation Directorates espoused the use of CHIS as an investigative tool, but this contrasted with the views of operational staff within their command.

- 7.1.6 Many officers employed in law enforcement were clearly reluctant to have any involvement with CHIS as an aid to intelligence gathering and said categorically they would avoid CHIS deployments in any of their operations. This was due to a variety of reasons relating to HMCE's use of CHIS, including concerns over failed prosecutions, knowledge of internal investigations and warnings by some senior managers over potential adverse effects the mismanagement of CHIS could have on their careers.
- 7.1.7 Even a number of highly experienced investigators who had in the past reaped the benefits of CHIS deployments now say that they would much prefer alternative intelligence gathering techniques in support of operations and would avoid the involvement of CHIS at virtually all costs.
- 7.1.8 In the last 12 months CHIS Ops have provided information and support that has led directly to the very significant seizures of drugs (heroin, cocaine, amphetamine and cannabis), cigarettes, laundered fuel and cash.
- 7.1.9 HMRC's Intelligence Directorate recognises the value of CHIS deployments and in its draft strategy highlights the need to enhance its specialist capabilities (such as CHIS and analysis). Whilst senior managers and a number of specialist staff were enthusiastic and committed to the concept of enhancing intelligence gathering through CHIS activity, the remainder of officers' attitudes ranged from ambivalence to aversion and fear.

7.2 Routine Activity – Proactivity

- 7.2.1 Although the use of human intelligence was endorsed at senior management level in the Intelligence Directorate, HMRC does not place sufficient emphasis on the business benefits of gathering information and intelligence from human contacts. There is no clear, publicised message to encourage staff to be more proactive. In contrast one police force visited has produced a leaflet for all its officers that advises: "*You have a duty to obtain as much information about criminal activity from anyone you can*".
- 7.2.2 One senior officer described intelligence as "*the lifeblood of the organisation*". This view was not replicated outside the intelligence environment where many officers did not perceive their day to day business as being intelligence led. In fact one senior officer in a former IR business stream commented "Revenue do not do intelligence".

- 7.2.3 HumInt training was described by non specialist staff as focusing on departmental systems and process. It had not provided any emphasis on the potential value of human source intelligence in support of business aims and objectives and did not equip them with sufficient knowledge to confidently seek intelligence. As a consequence of inadequate training most interviewees believed that if they 'tasked' a person providing information to find out any further information, regardless of how they would seek to obtain this, the HumInt would become a CHIS. This left most under the impression that they could not ask a HumInt for more information, resulting in missed opportunities to obtain more intelligence.
- 7.2.4 The Customs Confidential hotline and Direct Taxes Helpline are clearly beneficial in enabling HMRC to obtain intelligence from callers who want to provide information anonymously. However, officers across a significant number of focus groups saw the presence of these hotlines as providing them with an opportunity to avoid engaging with members of the public at all. Examples were given of both telephone and personal callers seeking to volunteer information being discouraged from elaborating on the nature of their intelligence by the 'first contact' officer and being directed to telephone one of the hotlines. Clearly a number of these callers were willing to provide their details and therefore should have been recorded on to the HumInt system, rather than being directed to the hotlines.
- 7.2.5 The instructions given to IR staff do not bar them from making further contact with informers but they are not encouraged to do so. However, one RIAT, with a high percentage of management from a SCO background, appointed a Single Point of Contact (SPOC) for informer matters and provided local training to the officers designated to deal with informers. Despite working to the same instructions, they displayed a significantly more positive approach to intelligence gathering with no sense of fear in speaking to informers. This is in stark contrast with all the other RIATs visited.
- 7.2.6 Intelligence officers complained about the poor quality of intelligence logs emanating from call centres and hotlines. They lacked sufficient, comprehensive detail to enable proper assessment and research to be undertaken. The officers attributed this to the operators having insufficient knowledge and experience of the subject matter. Examples were also given of callers having difficulty in making themselves understood, because their dialect was fundamentally different from that of the operator, who was based in another part of the country. As a consequence, opportunities to explore and exploit intelligence were lost. Call Centre managers acknowledged that there were some problems, however they felt hamstrung by caller processing targets.

- 7.2.7 Air and sea ports have traditionally been rich picking grounds for intelligence gathering. There was a consensus amongst detection and intelligence officers at air and sea ports that this flow of information has, however, drastically reduced in recent years. To some extent, the withdrawal of certain full time Customs posts and their replacement by more mobile, focused deployments may have reduced opportunities to develop working relationships and generate intelligence. Officers have additional concerns that disproportionate emphasis is placed on the likelihood that personal details of potential sources of information may ultimately be disclosed. Potential HumInts are being 'warned' before they provide any information that they may have to provide a witness statement and could be required to give evidence in court. The officers believe, as a result, that they have alienated traditional relationships to the extent that intelligence has dried up.
- 7.2.8 In one HMRC region there was a surprising anomaly, whereby mobile detection officers were afraid to proactively gather intelligence from members of the travelling public with whom they had daily contact. Yet office based intelligence officers in the same location had been trained in how to de-brief members of the public. In contrast to the detection officers, the intelligence officers were confident and enthusiastic about their intelligence gathering capabilities and unafraid to interact with the public.
- 7.2.9 Detection officers working on the National Strike Force are being encouraged to increase the number of human contact reports (HCRs) and intelligence logs they produce. Performance indicators have been drafted to reflect this initiative.
- 7.2.10 Whilst it is imperative not to contravene legislation or departmental guidance, the majority of officers appeared to be overcautious in their dealings with HumInt. Apart from examples detailed in previous paragraphs, there was little evidence of any concerted effort by management to recover confidence in using human sources of information.
- 7.2.11 HMRC would benefit from a more proactive approach to encourage members of the public to provide information. Although HMRC has occasional publicity campaigns advertising its hotlines, there should be more visible messages at the points where members of the public would expect to come into contact with the Department. This could include posters at ports, airports and on the front page of the HMRC website. A very positive example of HMRC's commitment to tackling fraud is the media campaign to promote the new Direct Taxes Helpline.

7.3 International Activity – Proactivity

- 7.3.1 HMRC's Overseas Liaison Officers are posted around the world. They undertake a variety of duties, one of which is CHIS handling. Whilst not dedicated to full time handling, the CHIS/handler ratio compares more than favourably with UK based SMUs.
- 7.3.2 From 1 April 2006, the DLO network will be subsumed in to SOCA leaving the FLO network under HMRC's direction. HMRC will need to consider re-invigorating international CHIS operations or re-assess the viability of its SMU handling overseas CHIS.
- 7.3.3 International CHIS Ops activity has in the past been responsible for very significant contributions to class A drugs seizure levels.

Chapter 8

Improving HumInt and CHIS Handling

- 8.1 HM Inspector acknowledges that HMCE developed a range of covert intelligence sources in addition to CHIS. HMRC is continuing to utilise these successfully to tackle fraud and smuggling, as well as further developing the profiling of freight and passenger movements to provide better intelligence to aid deployment of resources.
- 8.2 Furthermore, from 2000, HMCE developed specific strategies for tackling indirect tax fraud, by first measuring the indirect tax gap and then setting out how it was going to deploy its resources on prevention, compliance and law enforcement. These strategies have had considerable success in reducing tax losses as a consequence of MTIC fraud, tobacco smuggling, oils and alcohol fraud. In its 2004-05 Annual Report, HMRC estimates the application of the MTIC strategy has reduced this type of fraud by 30% from its peak in 2001-02⁶⁵.
- 8.3 HMRC is presently producing a National Picture of Risk to give it an overview of the key risks across the whole tax system and the resources it is deploying against them and is further developing the strategy-based approach. In April 2005, the Department produced a document in which the first steps were taken to estimate the tax gap for direct taxes. HMRC is now in the process of producing further specific strategies for all areas of compliance, including Tax Credits. HMRC should be commended for these efforts.
- 8.4 Whilst acknowledging that these strategies have had an impact, in common with other law enforcement agencies, HMRC faces a future where organised criminals evolve. For example, although the estimated losses attributable to MTIC fraud have fallen, there are recent indications that they may be on the rise again. In addition, the Tax Credit system had been under attack for 18 months which led to the suspension of the e-portal on 1 December 2005. Criminals will attack areas of vulnerability and will not be bound by the same limits of present law enforcement agencies' responsibilities. Imminent technical developments will stretch the capability of law enforcement organisations in the near future and they will have to invest in a wide range of covert techniques and make use of skilled assets. The bar is rising and the law enforcement effort must be up to the challenge.
- 8.5 CHIS could play a much stronger role in contributing to the law enforcement effort of HMRC. The Department receives a very limited return on its considerable financial outlay on CHIS management.

⁶⁵ HM REVENUE & CUSTOMS (19 December 2005) *Annual Report 2004-05 and Autumn Performance Report 2005*: TSO: London: Page 54.

Improving HumInt and CHIS Handling

Staff costs to the Department for SMUs alone are in excess of several million pounds per annum. HMRC has been unable to provide HM Inspector with figures quantifying its expenditure on accommodation and other SMU support costs. Nevertheless, this appears to be a disproportionately high cost for the number of CHIS. In terms of outcomes, during 2005, HMRC's UK SMUs yielded very significant seizures of:

- Cash,
- Class A Drugs,
- Cigarettes,
- Laundered Fuel.

Moreover, there is no obvious plan to increase productivity or to improve the alignment of CHIS management with HMRC priorities.

- 8.6 The significance and benefits of utilising CHIS as a tool in the law enforcement toolkit was downplayed on a number of grounds by many of the non CHIS practitioners interviewed. Firstly, the aftermath of the London City Bond case and subsequent criticism of HMCE by the judiciary and the media have created a real sense of apprehension towards the use of CHIS. This is prevalent amongst former HMCE officers and includes those who would not previously have been averse to using CHIS intelligence. These criticisms have also confirmed the suspicions about the use of CHIS that pervaded the former IR.
- 8.7 Secondly, the profusion of information and intelligence available to HMRC, and the abundance of cases that do not require CHIS intelligence, offer HMRC's criminal and special civil investigators other less risky options of engaging with avoidance, evasion, and attack on the revenue. However, they do not enable the same flexible active targeting of gaps in intelligence that CHIS can provide.
- 8.8 Finally, the diversion of management time and energy into the merger of former HMCE and former IR and the impending de-merger towards SOCA, has diluted attention to discrete areas of specialism.
- 8.9 To some extent the reasons for HMRC's under-utilisation of CHIS are understandable. There should be a willingness, on the part of the Department, to deploy CHIS in combination with other well controlled covert law enforcement tactics not just to targets of opportunity, but also to targets of choice. This will enable disruptive interventions or enforcement activities that are capable of achieving disproportionately beneficial outcomes. It could be argued that CHIS handling represents a very small slice of HMRC's investigation, intelligence and detection effort and may not reflect other obvious strengths, such as a tangible desire to succeed amongst operating staff and some first class leaders at director level. Nevertheless, CHIS activity must be a crucial element of any serious sustained attack on criminality, and is not a strong component at present.

- 8.10 The limited contribution that CHIS make to HMRC's law enforcement capability would be less of a concern, perhaps, if the criminality the Department was facing was less challenging. However, as recent events around Tax Credits and the evolving nature of MTIC fraud graphically illustrate, that is far from the case. It is estimated by HMRC senior management that organised crime accounts for £7 billion of the tax gap: it requires a vigorous, integrated and proactive endeavour by law enforcement to tackle this. CHIS are part of the suite of techniques that HMRC could be able to utilise to achieve 'compliance' outcomes whether through the criminal justice system or by other means.
- 8.11 The concerns highlighted in this report about the registration and management of CHIS require urgent action. A comprehensive audit of all HMRC CHIS files retained in the UK and abroad should be undertaken as a matter of urgency.
- 8.12 Further to this audit, HM Inspector recommends that HMRC should consider:
- 8.12.1 producing Standard Operating Procedures for CHIS practitioners, to provide these officers with step by step advice and guidance on managing CHIS;
 - 8.12.2 introducing a quality control regime for HCR submissions;
 - 8.12.3 ensuring its Quality Assurance Bureau integrates value for money and integrity assessments into the SMU reports;
 - 8.12.4 giving handlers access to rewards calculations, in order to reduce delays in processing rewards for CHIS;
 - 8.12.5 developing a structured succession planning process for SMU staff;
 - 8.12.6 whether the ratio of CHIS to handlers represents value for money;
 - 8.12.7 adopting a more proactive approach to CHIS who can provide intelligence in-line with the new Department's priorities;
 - 8.12.8 producing a clear implementation plan for HumInt and at the earliest opportunity, introduce the system to the whole Department;
 - 8.12.9 providing further staff training that improves compliance whilst emphasising the potential value of intelligence from human sources of information;
 - 8.12.10 introducing line management oversight of Human Contact Reports prior to their submission to the National HumInt Centre;
 - 8.12.11 ensuring that all branches comply with the Quality Assurance programme, as described in the HumInt instructions;
 - 8.12.12 developing promotional campaigns, posters and other methods of encouraging the public to volunteer information;
 - 8.12.13 providing OLOs with a level of support commensurate with risks, as are provided to their colleagues in UK based SMUs and providing a bespoke training package to take account of their unique position in CHIS handling.

Improving HumInt and CHIS Handling

- 8.13 However, significant improvement is unlikely to come solely from particular technical or functional management interventions. Experience elsewhere suggests such improvement is most likely to occur where the organisational climate and systems foster an enterprising but well controlled approach to tackling criminality.
- 8.14 There has been limited time, in this first inspection, to consider the ingredients of such an environment but some thoughts to illustrate the point are set out below and arise, at least in part, from conversations with staff at all levels within HMRC. The building blocks may be as considered below.
- 8.15 An explicit statement of the role of law enforcement in protecting the revenue in the next iteration of the HMRC strategy**
- 8.15.1 Prior to merger both IR and HMCE employed law enforcement techniques to support their tax collection regimes, but placed a different emphasis on case selection in line with their separate prosecution policies. HMCE developed a more proactive and aggressive law enforcement capability, whereas IR reserved prosecution for only the most 'heinous' and 'exemplary' cases.
- 8.15.2 Following the establishment of HMRC, a Consultative Committee was set up (including tax experts, business representatives and others who reflect the range of the Department's customers) to review the Department's powers, deterrents and safeguards. An analysis of the responses to the initial consultative document, whilst being cautious about the need for strong powers across the whole Department, has revealed that there was widespread support for HMRC to take a positive approach to tackling the serious fraudsters as follows: *"Respondents strongly believe that life should be made easier for the compliant and harder for the non-compliant. Some saw closer working with other enforcement agencies as a way to catch more of the seriously non-compliant. And there was recognition that HMRC would need strong powers to combat complex evasion and fraud..."*⁶⁶ Furthermore, the results of the Law Enforcement Stakeholder Audit which were published in October 2005 revealed the following points: *"recognition of the vital role that Customs played; hard working, courageous, committed and expert staff; good law enforcement results; important to the future plans for tackling serious organised crime"*⁶⁷.

⁶⁶ HM REVENUE AND CUSTOMS (July 2005) *HM Revenue and Customs and the Taxpayer: Modernising Powers, Deterrents and Safeguards: Summary of Responses to the Consultation*: London: HMRC: Page 3.

⁶⁷ HM REVENUE AND CUSTOMS (October 2005) *Law enforcement stakeholder audit: Findings and Response*: London: HMRC: Page 2.

8.15.3 Post merger, HMRC management have not elaborated upon the role that law enforcement and the prosecution of offenders will have in achieving the Department's statutory objectives, in the Departmental Strategy. The strategy provides an understated message: "*We will tackle non-compliance while minimising the effect on the majority of our customers who want to comply*". Arguably, this is an opportunity for a more robust approach given the potential contribution of law enforcement to the Department's future. It is interesting to note that one of the United States' Internal Revenue Service's strategic goals, outlined in its current Strategic Plan, is to "*Enhance Enforcement of the Tax Law*."⁶⁸ Consideration should be given to a more explicit message, for both internal and external consumption, that the Department will use enforcement techniques to frustrate and prosecute those who attack the system.

8.16 Encouraging staff on the competitive advantage offered by the information/intelligence they can gather in the course of their work

8.16.1 In his 2003 review of HMCE Mr Justice Butterfield was critical of the use of 'cascade training' to deliver important information to its staff. Throughout this inspection, there was evidence of the continued use of 'cascade training' to impart information about HumInt. There was a consensus amongst those who had received the cascaded training that the message they received focused too strongly on the dangers inherent in the use of HumInt, to the exclusion of the positive benefits of gathering this type of intelligence. Many officers felt the time was now ripe for additional training of a more 'up-beat' nature to encourage officers to more proactively utilise their links to the public. The Department has a diverse workforce spread over a large geographical area. Its officers have regular contact with a wide range of the public and business community. Although there have been issues that have had a marked impact on the Department's reputation, it could take the opportunity to gather as much intelligence as is available to it. Use of a well-trained and motivated workforce is the most effective way of achieving this aim.

8.17 The whole-hearted operation of a single business focus model, designed to deal with targets of choice as well as opportunity

8.17.1 In 2000, NCIS produced NIM on behalf of the ACPO Crime Committee to professionalize the intelligence discipline within law enforcement and it has latterly been implemented across the service.

⁶⁸ INTERNAL REVENUE SERVICE (2004) *IRS Strategic Plan: 2005-2009* Washington DC: Department of the Treasury: Page 4.

In 2004, the former HMCE, recognising the benefits of NIM, adopted the principles. Post-merger, a working group recommended: *"HMRC should formally endorse the adoption of the NIM principles as a means of supporting corporate decision making by the controlled acquisition, development, dissemination and application of intelligence"*. HMRC's Executive Committee (Excom) accepted the recommendation and the Department has created a bespoke Business Delivery Model (BDM) based on NIM principles. This now forms part of the corporate risk strategy and will provide knowledge and intelligence that senior managers can use to provide strategic direction, make tactical resourcing decisions and manage risk.

8.17.2 Whilst HMRC has embarked on BDM development, post-merger, other issues have taken precedence and this has slipped down the list of priorities. Moreover, the development of autonomous business unit strategies does not provide a fertile ground in which to develop an overarching single business focus model. The deployment of an intelligence-based approach across the Department would utilise the capacity and capability of HMRC as a whole, to identify targets and to achieve disproportionate impact and greater compliance.

8.18 A developing self improvement process that moves beyond providing assurance and helps leverage improvement

8.18.1 The decision by HMRC to conduct a Law Enforcement Stakeholder Audit demonstrates a desire to improve its reputation and recover lost ground. Further steps could be taken to improve its performance by use of a well designed self inspection regime. HMRC could introduce a more robust system to record why cases succeed or fail and learn from the experience by taking steps to improve performance. Inspecting against performance will enable assessment of the business workstreams in support of departmental priorities. Experience in other countries has shown that both internal and external inspectorates have a crucial role to play in improving performance. By working together with the departments they can focus the areas for inspection over the coming year and the departments can be tested against them. The RCPO has produced a document that contains a list of questions that all prosecutors must ask in each case referred to them by HMRC. The questions are intended to improve lawyers' knowledge of the genesis of the investigation, in particular, questioning the source and history of the intelligence that underpins it. This is a good example of RCPO taking a positive step to aid self-improvement.

8.19 A route map for developing law enforcement capability to operate most effectively against criminality in a new national landscape

8.19.1 It is clear from interviews with senior personnel that, at the early stages of merger, the Chairman and ExCom had decided that when each of the 36 new directors were appointed, they would be empowered to invoke organisational change within their own directorate. Therefore, no overarching departmental strategy on the integration of law enforcement was created. Directors were charged with producing their own strategies for their business streams.

8.19.2 Differences could be expected in the approach to draft strategies produced by Criminal Investigation, Serious Civil Investigation and Intelligence Directorates, but given their common focus on evolving criminality it is surprising to find that there is not a common agenda on some key issues and risks:

- The importance of rebuilding the Department's reputation.
- The development of a broader intelligence capability to reflect the changing nature of attacks on the revenue.
- The development of stronger partnership working across the Department and with external stakeholders including SOCA.
- Establishing inter-directorate development, including forensics and training needs.

8.20 These issues may generate discomfort within HMRC management regarding the retention of CHIS operations in the Department. However, radical changes of that nature need careful thought. There are problems but they are not insurmountable. Once they have been addressed, properly managed CHIS, used proactively to fill specified intelligence requirements, should be a major component of any future departmental law enforcement strategy.

Glossary of Acronyms and Abbreviations

ACPO	Association of Chief Police Officers
AO	Authorising Officer – RIPA
BDM	Business Delivery Model
CCC	Cost Centre Code
CEDRIC	Customs & Excise Departmental Reference & Information Computer
CHIS	Covert Human Intelligence Source
CHIS Ops	Covert Human Intelligence Source Operations
CJES	Criminal Justice & Enforcement Standards (HMRC)
CPIA	Criminal Procedure and Investigations Act 1996
DLO	Drugs Liaison Officer
DSU	Dedicated Source Units
FLO	Fiscal Liaison Officer
FTE	Full Time Equivalent
HCR	HumInt Contact Report
HIS	Human Intelligence Source
HMCE	Her Majesty’s Customs and Excise
HMI	Her Majesty’s Inspector (of Constabulary)
HMIC	Her Majesty’s Inspectorate of Constabulary
HMRC	Her Majesty’s Revenue and Customs
HRA	Human Rights Act 1998
HumInt	Human Intelligence [Sources]
IR	Inland Revenue
ISR	Intelligence Source Register
IT	Information Technology

LE	Law Enforcement
MLRO	Money Laundering Reporting Officer
MTIC	Missing Trader Intra-Community
NCIS	National Criminal Intelligence Service
NHC	National HumInt Centre
NHD	National HumInt Database
NIM	National Intelligence Model
NSU	National Source Unit
OLO	Overseas Liaison Officer
OPSY	Operational Security
PCSO	Police Community Support Officer
PII	Public Interest Immunity
PNC	Police National Computer
QA	Quality Assurance
QAB	Quality Assurance Bureau
QC	Quality Control
RCPO	Revenue & Customs Prosecution Office
RIAT	Research Intelligence & Analysis Team
RIPA	Regulation of Investigatory Powers Act 2000
RIP(S)A	Regulation of Investigatory Powers (Scotland) Act 2000
SLA	Service Level Agreement
SMU	Source Management Unit
SOCA	Serious Organised Crime Agency
SOPs	Standard Operating Procedures
SPOC	Single Point(s) of Contact
VFM	Value for Money

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Notes

