



Failing Families: The Chaos of the Tax Credit System

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Summary

The administration of the tax credit system has been widely criticised since its inception, including in numerous reports from Select Committees and the Parliamentary Ombudsman. Despite this, statistics which are due to be released by HMRC on the 31st May 2006 are likely to show little if any improvement from last year when around 2 million families were shown to be having to repay on average £1,028 to the Treasury due to incorrect tax payments.

In June 2005 statistics were released which showed the failure of the tax credit system for almost a half of all claimants, who were either underpaid or overpaid and required to make repayments to the HMRC. In a written statement to the House just a few days before however Dawn Primarolo said: "For the vast majority of families the system [of tax credits] is now working well"¹ This complacency has marked the Government's approach to the chaos in the tax credits system.

Statistics released in Jun 05 confirmed that²:

- By the 5th April 2004, 1,879, 000 families out of a total of 5.6 million had their tax credits overpaid, at a total cost of £1.93 billion.
- By the 5th April 2004, 713,000 families out of a total of 5.6 million had their tax credits underpaid, at a total COST of £464 million.
- Of those families who had Tax Credits overpaid, 630,000 were overpaid in excess £1000.
- Of those families who had Tax Credits underpaid, 144,000 were underpaid in excess of £1000.
- By September 2005, 150,000 overpayments had to be written off as they were due to official error, further to this the Government estimate £961 million would not be recovered³

¹ Column 23 WS 26th May 2005

² Full statistics are available at <http://www.hmrc.gov.uk/stats/personal-tax-credits/cwtc-payments-0304.pdf>

³ PQ, 05/ 23679, The "provisions" figure of £961million relates to estimates of Tax Credit overpayments that will eventually prove to be irrecoverable [Comptroller and Auditor General, October 2005].

HMRC's administration of tax credits has been repeatedly criticised for its failure in accurately calculating tax credit payments, systemic maladministration in its attempts to recover overpayments, and the vulnerability of the whole system to fraud. The Paymaster General has presided over a tax credit system which continues to fail. She has offered lip service to reform but failed to match this with the fundamental reforms needed.

"If such a system is to meet those needs [of families eligible for tax credits] a much improved level of customer service is required... without these a sizeable group of families will continue to suffer not just considerable inconvenience, but also significant worry, distress and hardship."

Parliamentary Ombudsman's report Tax Credits: Putting things right, 22nd June 2005

"The department [HMRC] does not have sufficient information about the claimant population to enable it to provide good service to the public and avoid disruption to its own main business of tax and administration."

Committee of Public Accounts, Inland Revenue: Tax Credits and deleted tax cases, 18th July 2005

It [the tax credit system] is failing some families. That is unacceptable and we will take the necessary measures to remedy the situation.

The Prime Minister In the House of Commons 22nd June 2005

Continued failings of the Tax Credit System

Responding to criticisms of the Tax Credit system in June 2005 the Paymaster General, Dawn Primarolo said “That is why we need to move now...to ensure that the administrative and IT problems are corrected and the system delivers for all claimants the very best service”.

Investigations by the Liberal Democrats have shown however, that the HMRC has not met all the recommendations of the Ombudsman’s report and that Tax Credit payments continues to be vulnerable to system failures, maladministration and fraud. Meanwhile the Paymaster General continues to stymie legitimate investigations into the running of the Tax Credit system.

1. Poverty

The tax credit system was created to offer financial assistance to families most in need, yet the administration of the tax credit system has driven a large number of people further into debt and poverty. In one submission to the Ombudsman an individual due to repay tax credit overpayments said: “I have had to borrow money to pay my rent as the landlord was threatening me with eviction... It has caused me so much stress and depression.” Based on figures released, the Liberal Democrats have calculated that of those families who had Tax Credits overpaid in 2003/04, they are paying back an average of £1028 to HMRC.

2. Maladministration

The Revenue’s code of practice (COP 26) says: ‘We will not ask you to pay back an overpayment if it arose because we made a mistake and you could reasonably have thought your award was right.’ The Ombudsman makes the point that “in practice, and in contradiction of the Code, excess payments during the tax year (and at the end of the

tax year) are recovered by the Revenue as a matter of course, without prior investigation of either of these two key questions”⁴

The Parliamentary Ombudsman made it quite clear in her evidence to the Public Administration Select Committee on 20th October 2005 that she considers the automatic recovery of overpayments without first checking to see if the money is recoverable under their own guidance, to be ‘systemic maladministration’. Yet, in evidence to the Committee, the Paymaster General seemed unsure as to what the Parliamentary Ombudsman meant by ‘systemic maladministration’ and in a recent answer to a Parliamentary Question she made no meaningful response to this accusation.⁵

HM Revenue and Customs continue to recover overpayments automatically, not withstanding the new ability to suspend recovery once a claimant disputes the overpayment, seemingly ignoring the Parliamentary Ombudsman’s accusation of maladministration. This has led to 31,504 compensation payments being made in the last three quarters of 2005.

3. System failure

IT failure in the Tax Credit system continues to dog HMRC, despite the recommendations by the Parliamentary Ombudsman in her report that ‘different models’ were necessary to deliver a ‘better more complete service. The last available data from March 2005 to October 2005 notes that 335,000 manual payments of tax credits had to be made due to system failure, totalling some £162.3m.⁶

Further to this up to 30th September 2005 150,000 overpayments had to be written off due to official error, with a further £961 million estimated as the amount of money that will never be recovered.⁷

⁴ Pparagraph 5.14 *Tax Credits: Putting things right*.

⁵ PQ/05/22180

⁶ PQ 05/30009

⁷ PQ, 05/ 23679, the "provisions" figure of £961million relates to estimates of Tax Credit overpayments that will eventually prove to be irrecoverable [Comptroller and Auditor General, October 2005].

4. Fraud

Part of the original intention behind the new tax credits was to create a 'light touch' non-stigmatising way of delivering financial support to families with children and to increase the take up of tax credits. This 'light touch' approach may be behind the relatively low levels of security checks and corroborative documentary evidence required to make a claim.

It is clear that the system has become a target for organised criminal fraud. The NAO's Standard Report on the Revenue's accounts, paragraph 2.44, notes that the Revenue had been aware that tax credits have been targeted by organised criminals particularly over the internet where claims can be made without proof of identity. The Pre Budget Report in 2005 estimated that in 2003/04 at least £30 million had been lost to fraud.

Despite this Dawn Primarolo has been extremely reluctant to give full answers over the fraud issues in the administration of tax credits. In February 2006 The Paymaster General indicated that she had first been made aware of serious fraud in Tax Credits in November 2005⁸, yet in an answer to David Laws on the 10th January 2006 she said that she had heard of increases in "organised attacks on the tax credits system" BY June 2005.⁹

5. Bureaucratic Chaos and Ministerial incompetence

In November of last year when questioned, the Paymaster General revealed that between June 2003 and April 2005 the Tax Credit department had received 1.4 million letters from members of the public or their representatives. In 2004/5 over 50% of these letters failed to meet the 15 day reply target and over 25% (350,000) of letters were not answered within the 40 day target.¹⁰ This clearly demonstrates that the department is failing to deal with back log of claimant complaints that the Ombudsman's Report identified.

⁸ Oral Evidence to the Treasury Select Committee, 1st February 2006

⁹ PQ 05/35700

¹⁰ PQ 05/9840

In a question asked by David Laws in April this year to ascertain if there had been an improvement in response times to letters, upon “asking how many letter were received by HM Revenue and Customs between April and February 2006 on Tax Credits” the Minister responded that the “information requested [was] not available”.¹¹ In response to a letter pursuing this answer, the Paymaster General claimed that the data was not available, as David Laws had asked the HMRC - not the Tax office - on the second occasion¹², despite the fact the Tax Credit Office is a subsidiary of the HMRC and he had asked specifically about letters regarding Tax Credits!

Figures obtained by the Liberal Democrats have also shown that since April 2005 over five million calls to the Tax Credits Helpline went unanswered by staff, 22% of calls made to the helpline. This is despite claims made by the Paymaster General in October last year that figures for the year to date showed that 97% of calls to the helpline were “being answered within the target”.¹³ In fact, for the period from April to September 2005 only 74% of calls were answered. In January this year alone that meant 180,000 calls did not get through.¹⁴

Further to this it now appear the department has taken on a siege mentality, obstructing legitimate enquiries into the tax credit system. Since April 1st this year out of 77 questions regarding tax credits, almost half of them remain unanswered, referred to a previous question, or told that the requested data was not available. In the last 6 months, the Paymaster General has failed to answer 15 questions on the subject of Tax Credits tabled by David Laws alone.

¹¹ PQ 06/63045

¹² In a letter from the Paymaster General to David Laws MP 21st May 2006

¹³ Oral evidence given by the Paymaster General to the Treasury Select Committee on the 26th October 2005

¹⁴ PQ 05/20440

The Liberal Democrat 5 Point Plan for Tax Credit Reform

The Liberal Democrats are calling for a five point action plan to tackle tax credit chaos, including:

1. A return to stable, 6 month fixed, awards – ending the chaos and instability of the existing system, which is particularly damaging for families on low incomes. *Despite all the evidence that variable awards creates massive instability and a high chance of incorrect payments, no attempt has been made to return to 6 month fixed awards.*
2. Much simpler, clearer award notices. *Although there have been some improvements made to the award notices, there is still widespread criticism of the number of and the clarity of the awards notices.*
3. Action against organised criminal gangs. *The Paymaster General still seems unprepared to admit when she became aware of organised fraud let alone propose solutions on to how to run an effective system which is secure against criminal activity*
4. An immediate end to what the Ombudsman has called “systemic maladministration” – automatic recovery of tax credits by the Revenue without even checking if the overpayments are recoverable. Along side this there should be a statutory right of appeal against overpayments, with all overpayments due to official error being written off. *Despite this being one of the Ombudsman’s key recommendations, no attempts have been made to implement it*
5. Improve the tax credits IT system. Overhaul the automated payments systems which have led to constant failure, with the need for costly manual payments. *High levels of manual payments still remain showing no progress in system reform*

In order to ensure that all these reforms take place, the Liberal Democrats believe that it is necessary to have a change in leadership in the department, so that the system is run by a minister who is prepared to acknowledge the failings of the current system and willing to drive radical change through the department to tackle the ongoing problems.