

Money with your name on it?

CAB clients' experience of tax credits

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Summary

1. Tax credits are one of the government's flagship policies. Most hard working families with children now receive tax credits to supplement their income, but many of the poorest families rely absolutely on them. Our purpose in publishing this report is to draw attention to evidence from Citizens Advice Bureaux which shows that tax credits are not currently working effectively for many of the people who rely most heavily on the additional income. We firmly support tax credits as a vehicle for directing substantial extra money towards lower income families, and we want the system to work effectively for all who are entitled to the extra help.
2. The Government's reforms of tax and benefits in recent years have been based on making work pay, and tackling poverty. The government is committed to halving child poverty, and wants to ensure that 70% of lone parents are in work, by 2010. These are objectives that Citizens Advice welcomes. There needs to be rapid improvement to administration and adjustment to the way in which overpayments are recovered, to ensure that the tax credits system helps achieve anti-poverty objectives and does not frustrate them.
3. 6.1 million families, containing 10.3 million children have been awarded tax credits. This includes 0.8 million families who receive social security benefits for children but not tax credits. The total amount paid out last year was valued at £13.6 billion. For those on the lowest incomes a tax credit award, including childcare can be worth a substantial part of their weekly income. A lone parent with one child, working 20 hours a week earning the minimum wage and paying £80 a week for childcare would be entitled to over £8,000 a year in tax credits. Families on higher incomes receive about £10 a week. A family with income of £25,000 a year would receive £545 a year.
4. Tax credit administration has been subject to a completely unacceptable level of error. In delivering tax credits, the Revenue has failed to live up to its own standards of information clarity and efficiency of service.
5. Tax credits are intended to provide a guaranteed and stable income. It is well known¹ that people on the lowest incomes budget on a weekly, and not an annual basis, so stability of income from week to week is just as important as paying the additional amounts that tax credits now offer.
6. It is also well known that families on the lowest incomes, especially lone parents and non-homeowners, some of the key groups intended to benefit from tax credits, are the most over-indebted and the most at risk of debt problems arising if their work or personal circumstances

¹ For example, *How people on low incomes manage their finances* ESRC 2002

change.² DWP research has also shown that falls in income of as little as 10% have a large impact on savings behaviour.³

7. Many people suffer from a lack of basic literacy and numeracy skills, yet claiming and renewing tax credits, and keeping the Revenue informed about material changes of circumstance means people must be capable of handling complex information and maintaining full household records. We do not think this is realistic, even if the system is administered correctly.
8. People on low incomes, lone parents and people with disabilities are all the focus of key government policies designed to reduce poverty and to encourage work and saving. This means that the stakes for the success of tax credits as a policy are high, if the tax credits system is to work well for those that rely on it the most. These families are also amongst those most likely to seek advice from Citizens Advice Bureaux.
9. High quality delivery of tax credits is absolutely vital. Tax credits should be delivering leading edge public sector customer services. This report, which is based on CAB evidence from across the UK, finds that it has a long way to go to deliver.
10. The key things going wrong are these:
 - The complexity of tax credits makes it difficult to understand;
 - Information to claimants is complex, yet there are financial penalties for not complying with rules on claims and renewals.
 - Substantial levels of error have diminished confidence in tax credits;
 - There are lengthy delays in resolving problems;
 - High levels of over and underpayments have arisen, causing considerable ongoing problems;
11. The consequences and impacts of these problems are that:
 - We have received reports of people whose jobs are at risk, because they cannot continue to pay for childcare after losing the support they were getting from tax credits;
 - We continue to see people whose actual incomes are below the level of income support, and who are by definition living in poverty, often as a result of a tax credit error that was not their fault;
 - We have seen people whose homes are at risk, because they are in arrears with rent or mortgage payments after tax credit income was stopped or severely reduced.

² *Overindebtedness in Britain, a report to the DTI*, Kempson, 2002

³ *Savings and Life events*, McKay and Kempson DWP Research Report 194 October 2003

- Some people have been wrongly advised to take out loans to repay tax credits
 - Our evidence shows there is loss of confidence in tax credits amongst the hardest to reach groups.
12. Our concern is based on the evidence we continue to receive from Citizens Advice Bureaux which shows that the tax credits system is failing for large numbers of our clients, by causing poverty and reducing their ability to work. For CAB advisers, resolving problems is also far too protracted and difficult, because of poor administrative systems.
 13. The scale of the problems faced by clients, and the difficulties our advisers have had in resolving even relatively simple errors and problems, have been very substantial. It is noticeable that tax credit problems are causing *disproportionate* levels of concern amongst our clients and advisers. Bureaux have been asked to advise on around 150,000 client problems with tax credits in the year from April 2004 to the end of March 2005. In the past two years, Citizens Advice has received more than 12,000 reports and complaints about problems with tax credits from bureaux.
 14. Whilst this is not an extraordinary number of client problems (compared with almost two million benefit problems bureaux deal with each year, or 500,000 employment-related problems), CAB advisers are saying that tax credits is their number one policy concern. This appears to be because tax credit cases are extremely complex and advisers find resolving them time-consuming. Also in many cases the problems facing their clients are often very serious indeed.
 15. Many clients are seeking advice from Citizens Advice Bureaux because they cannot understand their award notices, or need a simple error corrected and have not been able to resolve matters directly with the Revenue.
 16. We welcome the statement made on 26 May 2005 by the Paymaster General, announcing that steps would be taken to improve tax credit administration:
 - A review of effectiveness of information, including clarity of award notices and duplication;
 - Information targeted towards people most at risk of overpayments;
 - Better quality of service from the Tax Credits Helpline;
 - Faster identification of IT problems and errors;
 - Innovative working with the voluntary sector to provide advice to families receiving tax credits;
 - A review of the operation of the code of practice on recovery of overpayments.

17. We look forward to further discussion with the Revenue about the exact timing and nature of their detailed proposals, which may go some way towards addressing the problems we highlight in this report. There need to be rapid improvements in administration and communication, and we hope that our report is useful in reforming the system.
18. We also believe that many existing overpayments caused by Revenue errors will need to be written off, and that there must be changes to the rules governing the way overpayments are recovered, and payments adjusted. These changes would serve to restore confidence in tax credits, and ensure that the system cannot reduce income to below poverty levels and remove work incentives.
19. We welcome the determination that is now being shown to secure improvements in tax credit administration. In order to improve accountability and transparency, we would welcome publication of more performance and other information. It is important that more information is provided about errors in tax credit awards, complaints and response times, waiting times for appeals, and especially about the extent of adjustments to awards that leave families on incomes below weekly or monthly entitlement.
20. Our main recommendations are designed to ensure that understanding of the system amongst claimants is improved, and that changes to tax credit payments do not cause the very hardship tax credits are designed to prevent.

Key recommendations

Quality of administration

21. It is vital that claimants are able to understand tax credits and can obtain accurate information. We are disappointed that planned changes to award notices will not be introduced until April 2006, and urge faster implementation.
22. Tax Credit helpline advisers must be able to explain award notices to claimants.
23. In order to improve accountability and transparency, we would welcome further published performance and other information on complaints, correspondence response times, appeal clearance times, and numbers of award adjustments that leave families on incomes below their weekly or monthly entitlement.

Recovery of overpaid tax credits

24. Huge amounts of overpayments and errors have occurred as a result of system failings. Urgent action needs to be taken in order to restore

confidence in the system. **A new approach is needed, and we recommend the following five steps:**

- All adjustments to payments should be limited to ensure that claimants cannot be left with weekly incomes below minimum levels.
- Where there is an overpayment from a previous year and from a current year recovery must not be compounded, so that maximum reductions in payments apply.
- In the light of the historic high level of administrative errors, more overpayments should be written-off. All overpayments being recovered from final awards or adjustments, where the overpaid amount has arisen through no fault of the claimant or through fraudulent activity, should now be waived.
- There should be a proper independent right of appeal against Revenue decisions, in cases where mistakes were caused by the Revenue, whether or not it was reasonable for the claimant to spot the error on a complicated award notice.
- We believe the childcare element of working tax credit should always be paid in full, in order to enable families to remain in employment.

1. Tax credits: policy objectives

- 1.1 This chapter briefly describes the main policy objectives for tax credits. It notes the additional financial support which they offer as well as the high levels of overall take-up.
- 1.2 Tax credits claim to provide:
- Higher levels of financial support, for families with children and for working people;
 - A guaranteed minimum income for all families;
 - Seamless support for families, whether they are in or out of work;
 - A responsive system that adjusts to reflect family income and circumstances.
- 1.3 Tax credits can, and do, provide additional financial support for families on lower incomes. In the year 2003/04, £13.6 billion was paid out. According to the Secretary of State for Work and Pensions, tax credits have contributed strongly to income gains. By October 2005 families with children will be receiving after inflation average gains of £1,400 per year since 1997. The poorest fifth of families will be an average £3,200 better off.⁴
- 1.4 The 2005 Budget included a commitment to increase the child element of the Child Tax Credit in line with average earnings up to 2007-08. There is a strong level of take-up. Figures for April 2005 show that 6.1 million families containing 10.3 million children were tax credit recipients, or were receiving the equivalent child support through benefits.⁵ 0.8 million families with children are estimated to be receiving benefits but not child tax credit, paid at the same rate as child tax credit. This means that until families receiving benefits for children are transferred onto tax credits, there are 5.3 million families receiving tax credits.
- 1.5 There are 337,000 families receiving working tax credit who get an average £51 per week towards childcare costs. There are also 91,000 families receiving a disabled worker element of working tax credit exceeding £2000, and 306,000 families getting CTC received a baby addition to the family element, receiving over £1000. **Appendix 1** gives details of take-up of tax credits and shows the types of families receiving tax credits and the value of payments.
- 1.6 Tax credits were ostensibly designed to provide seamless support for families whether they are in or out of work. In March 2000 the

⁴ DWP press release 16 May 2005

⁵ *Child and Working Tax Credit Statistics April 2005* Inland Revenue Analysis and Research 2005 www.hmrc.gov.uk/stats/personal-tax-credits/cwct-quarterly-stats.htm)

government said it would replace working families tax credit and disabled persons' tax credit, and create a "seamless mechanism for channelling support to children" by integrating financial support for children, merging children's tax credit and income support payments for children, helping pay for childcare for lower-income working parents, all built on a foundation of universal child benefit.

1.7 The new tax credit structure would provide:

- "a more transparent system of support for children"
- "a portable and secure income bridge spanning welfare and work"
- "a common framework for assessment and payment".⁶

1.8 The press statement encouraging families to claim new tax credits in September 2002, emphasised the security and continuity of child tax credits:

"a continuous stream of income for families with children, which does not depend on the work status of the parents, creating a stable income bridge when families move into work."⁷

1.9 The Treasury series of papers on modernisation of tax and benefits, pre-2003, set out convincingly how getting a job lifts people out of poverty. The subsequent introduction of working families tax credit and later child and working tax credits introduced the concepts of the "income guarantee" and the "integrated and seamless system of financial support".

1.10 Many of the risk factors identified by the extensive pre-legislative research carried out by the government are now in practice affecting the 'work incentives' of CAB clients, and causing the very poverty tax credits should remove. For many of our clients, tax credits have re-created the very insecurities they were intended to remove. Our evidence points to the following problems being common experiences for many tax credit claimants today:

- A lack of transparency about awards and payments;
- Insecurity and instability of income;
- Financial stress, rather than additional income.

1.11 Figures on finalised awards for 2003/04, the first, problematic, year of tax credit operation, show that 46% of all awards were under or overpaid. Administrative problems are known to have affected thousands of awards. Many people also failed to report changes affecting their entitlement, demonstrating a need for increased understanding of the system.

⁶ *Tackling poverty and making work pay – tax credits for the 21st century* HM Treasury, March 2000

⁷ *Money with your name on it – the Chancellor urges families to claim new tax credits*, HM Treasury press release, 16 September 2002.

- 1.12 In the rest of this report, we discuss these and other problems. **Chapter 2** describes the serious administrative problems that have beset the tax credit system, and calls for further information about the nature and extent of errors and delays to be published. It also urges the Revenue to take greater responsibility for the mistakes it makes in people's tax credit awards, and to pay more compensation.
- 1.13 **Chapter 3** looks at the quality of information provided on tax credit awards, and at the difficulties CAB clients and advisers have had in resolving problems with tax credits.
- 1.14 **Chapter 4** urges 'user-proofing' the service provided by the Tax Credits Helpline to ensure improved customer service, and stresses the need for increased provision of face-to-face advice, whether through Her Majesty's Revenue and Customs (HMRC) or the voluntary sector.
- 1.15 **Chapter 5** sets out how, even in cases where overpayments arise through its own mistakes, the Revenue relies on tests of 'reasonableness' to determine whether people should repay, and has used formal compliance interviews to suggest that people should take out loans to repay overpayments. It notes that there is no independent right of appeal. People can only challenge decisions to recover if they know they can ask the Revenue to reconsider, and if they can show genuine hardship.
- 1.16 **Chapter 6** examines CAB evidence on clients' experiences of being paid tax credits and the problems and hardship faced by families whose payments are disrupted. It acknowledges that the government has long recognised that poverty and low incomes have severely damaging impacts and has done an enormous amount towards eradicating poverty. It argues that the government has yet to fully appreciate that tax credit income needs to be guaranteed, secure and stable, and that tax credit policy objectives have yet to be met in full.

2. Quality of administration

2.1 This chapter describes the serious administrative problems that have beset the tax credit system, and calls for further information about the nature and extent of errors and delays to be published. It also highlights the need for improvements in the complaints process.

2.2 The delays and poor administration of tax credit claims that occurred at the start of 2003/04 have been well documented and acknowledged. The Paymaster General said in a written statement on 26 May 2005 that "HMRC will take a series of important steps to improve the administration of tax credits".

2.3 The general quality of administration and number of errors has been frightening. It has resulted in families who depend on tax credits for half their weekly income left with nothing for months, for example because the computer does not recognise the existence of their children, or because earlier double payments have led to future payments stopping with no advance warning or explanation.

2.4 The lack of sophistication of the computer system has led to huge overpayments as calculations been made based on incompatible data, and there have been random and undue payments. Both these things have led to the high level of overpayments. Figures for 2003/04 show that ⁸:

- 46% of all tax credit families were over- or under-paid (2.59 million awards out of 5.67 million);
- A third of all families were overpaid (1.88 million awards out of a total of 5.67 million);
- 713,000 families were underpaid, a total of £464 million. 60% of these families had annual incomes below £15,000;
- Over half of all overpayments were in excess of £500, and a third exceeded £1000. More than 300,000 families effectively owed the Revenue between £2000 and £5000;
- Overpaid tax credit amounted to £1.9 billion.

2.5 The exact scale of the problems is still difficult to estimate. The Revenue has not yet published an analysis of the delays and errors. We do know that:

- Delays in processing awards led to 500,000 "interim payments" by sending out giro cheques throughout 2003/04, with a total value of 170m.⁹ these led to widespread in-year overpayments as these payments were duplicated;

⁸ *Child and Working tax credits finalised awards 2003-04*, HMRC analysis team, June 2005

⁹ *Report of the Comptroller and Auditor General 2003/04*, December 2004. This figure includes 65,000 payments with a value of £20m made to prevent hardship following reduction of an award.

- A computer error caused 450,000 households to be overpaid (a total of £94 million)¹⁰; of which 82,000, or 25%, were asked to repay several months later;
 - An computer input error led to the deletion of the income of one partner in a couples income leading to thousands of families being overpaid;
 - There have been delays in 'migrating' people receiving payments for children through income support and jobseekers allowance to child tax credit.
- 2.6 CAB evidence shows that many of these problems continued throughout 2004/05. Bureaux reported delays in the processing of initial applications, in responding to their reported changes of circumstance, in dealing with appeals or responding to correspondence. For example, one client had to wait over five months for her new baby to be added to her award and another had to send details of his new employer four times before it was finally recorded as having been received.
- 2.7 Claimants also experienced problems with getting payments as their cases became 'stuck' in the system. All too often they failed to be offered hardship or clerical payments and consequently experienced severe gaps in their income streams. Other claimants were paid too much as random amounts appeared in their bank accounts. The poor administration of tax credits also affected receipt of other social security benefits.

A couple, both working full time, received no tax credits between August 2004 and January 2005. They relied on tax credit payments to help pay for childcare, and the woman was worried that she would have to give up her job. The helpline advised that they, along with thousands of others were victims of a computer problem that caused payments to 'drop off the schedule', and could not say when it would be fixed.

A woman changed jobs in November 2004 and was advised that her working tax credit would be paid direct, rather than through her wages. By January 2005 no payments had been received. The client was advised to call back a month later. There was no recognition of the importance of the money to the client, who after three months with no payments was beginning to experience real financial problems.

One couple received 34 letters from the Revenue in a short time. Their award had been based on two children, although they had three. They were then told they had an overpayment of £500; the clients believed the correct figure was only £200. The Revenue assessed it again and came up with £1000.

¹⁰ *Inland Revenue Annual Report and Accounts for the year ended 31 March 2004*
<http://www.hmrc.gov.uk/pdfs/report2004.pdf>

Resolving cases

- 2.8 Response times to letters are very long indeed - CAB advisers are regularly told they will wait 6 to 8 weeks for replies, and, in practice, are having to wait very much longer than that. One bureau described writing to the Tax Credits Office about their client's problem getting child tax credit for one of her children:

10.06.04 - Initial letter

17.06.04 - They reply stating they will aim to respond within 6 - 8 weeks

18.06.04 - They send us a complaints leaflet

17.08.04 - We write to ask the TCO for an update on the position

01.09.04 - We write again

24.09.04 - TCO reply states that they will aim to respond within 6 - 8 weeks

13.10.04 - We address a letter of complaint to the Director of the TCO

28.10.04 - TCO reply states they will aim to respond within 6 - 8 weeks

- 2.9 We continue to receive numerous heartfelt pleas from advisers to do everything possible to secure improvements in tax credit delivery. One adviser recently complained to us saying,

“how many of these do you want before something changes? I am sick and tired of having to deal with IR problems. My fingers are so sore from having repeatedly to type the same thing.”

- 2.10 This adviser had been trying to assist a woman who had received a bill for £4,600 in overpaid tax credit – overpayment which appeared to have arisen through a mistake made by the Revenue, according to a letter the client had received. The client had been in tears during the interview.

- 2.11 There are thousands of similar examples in our files each showing a terrible catalogue of errors. Advisers frequently send us reports with accompanying statements like “I've picked these three because they're varied and I happen to have had time to write them up, rather than because they're exceptionally bad cases”:

A lone parent with one child left work in June 2004 and claimed Income Support. The Tax Credits Office had been sending giro cheques to the client at the wrong address, so the client had not been receiving working tax credit.

The client notified the tax credits office in July, and was then left to survive on income support payments of £55 per week plus child benefit until October 2004. The bureau gave the client food vouchers. The client also had the expense of several trips to Revenue offices and numerous phone calls. The client and the bureau were repeatedly told that the client had not notified the Revenue that she had stopped work, and later that computer problems were affecting the claim. The client and the bureau were assured several times that no overpayment would be recovered. During this time, the client was told that her tax credit payments were “just around the corner”. She now has numerous substantial debts and is being threatened with legal action.

In another example, a woman called at a CAB late one Friday as her weekly child tax credit payments had stopped. She found this out when she called at her bank to withdraw some cash, and found there was none. The client had just £2 to get home, and buy food for two children and herself. The client was suffering with a brain tumour. The client’s personal circumstances were changeable; she was a lone parent, but a working partner moved in during the year to help the client look after the children. The client’s hours of work also reduced because of her ill-health. The client’s tax credit claim was in a total mess, even though the client had made contact with the Tax credit office on several occasions. Her payments dried up overnight. The bureau has been trying to resolve the problems for several months, but has been constantly frustrated by lost correspondence, the TCO not recognising the bureau’s authority, and lengthy delays.

- 2.12 Matters are made much worse than they ought to be because our advisers are finding that resolving any problem with even the slightest degree of complexity can be almost impossible.
- 2.13 Even simple errors, such as claimants being recorded as having no children or one partner in a couple in work being recorded having no income, can prove difficult and time-consuming to resolve. Another adviser wrote to us recently after trying to advise a lone mother with two children, working part-time during school term time, who had come in because of an overpayment problem. The adviser described the impact on the client as

“despair. The client has gone from normality to a constant stream of award notices that no-one can understand. The client has still not established if the overpayment has been looked at again or if it has to be paid back. We wrote to Tax Credits in October 04, December 04 and January 05. I still have not received a reply to my letters. I can do no more. Anything I do disappears.”

- 2.14 The Revenue claims that it generally responds to correspondence within its target times. This is at odds with the experience of CAB clients and advisers. The Revenue frequently tells us that problems in many of the cases we have seen “should not have happened”, i.e. that the system

should not be allowing them to happen. **We would therefore welcome an investigation of a number of cases, to establish in detail what did happen including response times. The information produced should be published.**

- 2.15 It would be wrong to suggest that it is *only* people whose circumstances have changed over the course of a tax credit year who have been affected by problems. Errors do appear to be more likely to affect people whose circumstances change, but there has been an appalling history of errors affecting tax credit awards, which have been compounded by extremely poor communication with claimants, both via award notices and other written material, and through the Tax Credits Helpline.
- 2.16 We welcome the determination that is being shown to secure improvements in tax credit administration. **In order to improve accountability and transparency, we would welcome further published performance and other information.** This information should include:
- Numbers of complaints and the response times
 - Details of response times to correspondence
 - Waiting times to deal with appeals
 - Errors
 - Numbers of payments that have to be made clerically due to computer problems
 - Award adjustments that leave families on incomes below weekly or monthly entitlement.

Complaints and compensation

- 2.17 The standards of service that the Inland Revenue aim to provide are set out in their Code of Practice¹¹. Claimants who experience a bad service from the Inland Revenue can complain and should be able to receive reimbursement for costs incurred. Many clients have had to borrow money, pay bank charges, default on credit repayments or simply incur telephone and travel costs as they call the helpline or visit their local Inland Revenue enquiry centre to pursue emergency payments. If they are not happy with the outcome they can complain to the Adjudicator's office or to the Parliamentary Ombudsman.
- 2.18 Even where compensation is achieved, the process and payment can be inadequate.

A computer error caused the gender of a client's wife to be changed - as a result their tax credits suddenly stopped. For nearly three months, including the Christmas period, their income was reduced by £80 a

¹¹ *Code of Practice 1: putting things right – how to complain.*
www.hmrc.gov.uk/leaflets/cop1.htm

week – a loss of over a third of their total income, which also caused health problems. They applied for compensation and were awarded £20 costs and £80 compensation. They felt that this was completely inadequate.

- 2.19 We are concerned that many people have been put off claiming by the lengthy procedures they are required to go through. It is perhaps the most complex cases where compensation is most warranted, where it will be most difficult to attain. Claimants may struggle to explain what has gone wrong and will be likely to have already spent a significant amount of time just getting their payments established correctly. They may well have little energy left to pursue the complaint through the complaints process.

Several months after helping a client with her tax credit problems and lodging a complaint the bureau learned the outcome: "...I received a letter of apology and compensation of just £35, which did not even cover the expenses I had been caused. I was not impressed; in fact, I felt quite insulted and debated for a long time whether to take it further but decided in the end that it has all gone on too long. I did not have the time or energy to fight further and really I just wanted to put it behind me. Consequently I just accepted what had been offered and did not do anything more.'

- 2.20 By the end of 2003/04, the Inland Revenue had made 10,800 compensation payments to the value of £370,000. The new tax year saw a sharp increase in these payments and by the end of September 2004 a further 10,200 payments had been made to the value of £670,000. CAB evidence suggests that the complaints process can be long and arduous with many claimants getting 'complaint weary' long before they are satisfied that their problems have been fully recognised by the Inland Revenue.

- 2.21 Citizens Advice believes that the Revenue needs to take greater responsibility for errors made in calculating claimant's awards and issuing payments. Current Revenue practice results in all the fallout of errors being felt by the claimant, as all the responsibility, for spotting errors and getting them put right, is on claimants.

- 2.22 Whilst the Revenue has significantly increased the number and value of the compensation payments it has paid out in recent months, there needs a more proactive system for issuing compensation payments. There are compensation payments for poor administration to reflect individual circumstances. In the context of the substantial level of administrative errors affecting tax credits, **we recommend an additional fixed compensation payment for claimants whose awards have been disrupted by Revenue error or delay.**

3. Understanding tax credits: information and advice

- 3.1 This chapter looks at the quality of information provided on tax credit awards, and at the difficulties CAB clients and advisers have had in resolving problems with tax credits.
- 3.2 Claiming tax credits, renewing awards and interpreting award notices and other written tax credit communications is not an easy task. Claimants must be able to understand their entitlement and how prospective changes to their circumstances will affect their entitlement – particularly the benefits of moving into work.
- 3.3 Citizens Advice Bureaux regularly assist people with tax credit claims and associated needs. People frequently seek advice if they have insufficient income, are struggling to deal with debts, or if they are looking to start a job. Around 150,000 people have also come into bureaux across the UK in each year the new tax credit system has operated, seeking help and advice because of difficulties with their tax credit claim.

Understanding annual entitlement

- 3.4 The new tax credits system was a tremendous change from its predecessors family credit and working families' tax credit. CAB clients have found the annual system very difficult to understand. Tax credits are always provisional until awards are finalised after the end of the tax year. Payments, as set out on award notices, will only remain unchanged if people's household or work circumstances and income do not change. Significantly, this point is not made sufficiently clear to recipients, nor is it generally understood.
- 3.5 Family credit, and the working families tax credit and disabled persons tax credit, were 'snapshot' systems that made awards which were then fixed for six months, regardless of changes in income and circumstances. These systems were unresponsive to falls in income, or even to people leaving jobs. They were paid at lower rates than the new credits, and could not be increased if people's incomes dropped. Nevertheless they offered considerable certainty and stability.
- 3.6 Tax credits were intended to provide continuity of support, as well as responsiveness to changed circumstances. The Treasury paper that preceded the Tax Credits Act, issued in March 2000¹², discussed design issues for new tax credits and considered how annual awards could be beneficial:

¹² *Tackling poverty and making work pay – tax credits for the 21st century* Modernisation of Britain's tax and benefits system Paper 6 HM Treasury March 2000

“basing awards on income during the year could ensure that credit payments match families actual needs. An annual system would minimise administrative work for both the public and the government.”

- 3.7 The Treasury paper went on to accurately summarise (and forecast) many of the actual difficulties that subsequently arose:

“Responsiveness

However a longer award would require greater potential responsiveness within year to changes in circumstances to ensure a safety net if family income fell significantly or the household’s composition changed, for example on the birth of a child. It might also need to adjust in-year so that families did not face significant under or over-payments at the end of the award. There would be issues about how far the credits should reflect less dramatic increases and falls in income.

Allowing greater responsiveness could involve more contact with the Inland Revenue for some families, but it would mean that support more accurately reflected their situation. **A key issue will be how to combine this responsiveness with a system that is simple, and in which people can understand both their entitlements and responsibilities.**” (Emphasis added.)

- 3.8 Considerable effort was put in to learn how tax credits in the US, Australia and Canada dealt with responsiveness. Features in the UK system were designed to remove potential problems – such as the substantial overpayment problems in Australia, where families were required to estimate their income for the coming year. Tax credits legislation introduced the welcome disregard of income rises up to £2,500 a year, and defined the changes in circumstance that were necessary or desirable for claimants to report.
- 3.9 The April 2002 Treasury paper gave the clear impression that there would be continuity of support and responsiveness to changes, including through the annual renewal process:

“new tax credits will provide continuity of support for those who are not experiencing significant changes in income, with the ability to adjust quickly for those who are facing major changes...the new system will achieve this without imposing unnecessary burdens on those claiming tax credits or cutting across their incentives to work.”¹³

- 3.10 Annual renewal forms would allow awards to be finalised, by ‘picking up’ any changes not notified. Any “adjustments on account of the credit already paid out can be made as part of that calculation”.

¹³ *The child and working tax credits* Paper 10, HM Treasury, April 2002

- 3.11 Falls in income risked making families better off leaving work. The proposed solution was to allow people whose income dropped to inform the Revenue that they expected their annual income to be lower, and to receive a higher tax credit award. As initial awards would be based on the previous year's income, people would only need to forecast income if they'd experienced a drop in income.
- 3.12 The purpose of the tax credits system is to boost family incomes in and out of work, in order to promote employment and reduce child poverty. Yet the current tax credits system has an unlimited capacity to adjust payments and as a result can leave claimants with little or no income for large periods of the year. For example, if a person stops work or falls below 16 hours a week and entitlement to working tax credit stops, any payment over entitlement for the year is recoverable, either during the tax year as an 'adjustment', or after the year end as an overpayment recovery.
- 3.13 It is readily apparent from the evidence we receive that understanding of the system amongst CAB clients is variable. In many cases, clients have reported all changes in their circumstances diligently, often several times. In other cases, there may have been a delay or failure to report a change in circumstance. This could be for a variety of understandable reasons - people who stopped working through illness, whose childcare costs changed or were going through the break-up of a relationship.
- 3.14 People are even expected to know that if they don't report that a child is continuing in education after age 16, their child tax credit payments will stop. These are matters of communication, but are also more fundamental - it is extremely difficult for families on low incomes to understand tax credit reporting requirements and the impacts that not reporting changes can have. It is also unreasonable to expect low-income families to budget across a full tax year, and to forecast whether they will experience any relevant changes over the year.
- 3.15 There is also very little understanding of the penalties which the Revenue can (and does) impose on people it thinks have deliberately made a negligent, or fraudulent, claim or statement. There are penalties of up to £3000 in such cases. Failure to provide information or evidence can result in a penalty of £300 plus daily penalties of up to £60. Interest may also be charged on all penalties. There can be serious consequences for failure to comply exactly with the complex system.

Basic skills

- 3.16 We do not believe it is reasonable to expect people to cope easily, or in many cases at all, with the current tax credits system, not least because of acknowledged problems with basic literacy and numeracy skills. The government's own National Strategy for Improving Adult Literacy and Numeracy Skills found in 2001 that "a shocking 7 million adults in

England cannot read and write at the level we would expect of an 11-year-old. Even more have problems with numbers.”¹⁴

3.17 The government noted that amongst the seven million, there are “around half a million or more who struggle with English because it is not their first language”. It was also noted that a priority for the Strategy was to “improve the skills of those groups where literacy and numeracy needs are greatest and where we can make most impact”. These groups included many of those now most likely to be eligible for child and working tax credits:

- Unemployed people and benefit claimants;
- Public sector employees;
- Low-skilled people in employment; and
- Other groups at risk of social exclusion.

3.18 The present tax credit system takes insufficient account of the needs of vulnerable claimants. As one CAB adviser commented,

“20% of the adult residents of the area have little or no numeracy skills and cannot be expected to take on the Inland Revenue when there is an error in their favour”.

3.19 Clients have certainly sought help from Citizens Advice Bureaux because English is not their first language, they have literacy or numeracy problems; they struggle with complex issues or form filling. It appears though that tax credits has caused a wide range of people to seek advice. Bureaux have advised many people who would normally deal with their own affairs, but have had real difficulties resolving tax credit problems. A CAB adviser commented that one of their clients had made twenty-two contacts with the Revenue themselves, before they finally sought assistance from the bureau.

Claims and renewals

3.20 The tax credits system now means that many people are expected to fill in forms and keep records of their own and their partner’s income, hours, childcare payments and other details that could potentially affect their claim. The shift from benefits to tax credits means that more people are filling in something closely akin to a tax return.

3.21 The claim form for tax credits is long, with an accompanying notes booklet that runs to 56 pages. Filling in the claim form can require a lot of information, whether the form is completed online or in paper form. The Revenue website suggests people may need:

- payslips or P60, to provide details about employer, income and National Insurance number;

¹⁴ *Skills for Life: the National Strategy for Improving Adult Literacy and Numeracy Skills*, DFEE 2001

- Self employed people will need their unique tax reference number;
- Details of social security benefits received in the previous and current tax years;
- Child Benefit details and Child Benefit reference number;
- Approved childcare provider's information;
- Bank details.
- Details of other income for example from savings, pensions or rental income

3.22 Renewals forms provide summary information which reflects the initial information provided by claimants, together with any changes recorded during the year. There is a 33 page booklet of notes to go with the annual review. It is a complex and potentially daunting process, especially for people who are in work, who may also be using childcare, have a disability, or who are also in receipt of social security benefits. For example the renewals notes say:

“to estimate your annual income if you are paid on a regular basis, and the amounts are roughly the same each time, take a single payment and multiply it by:

52 if you are paid weekly

12 if you are paid monthly

13 if you are paid every four weeks.

3.23 People with disabilities will need to know not only whether they usually work for 16 hours a week, but also whether their illness or disability puts them at a disadvantage in getting a job, and whether they satisfy the ‘qualifying benefit test’ or the ‘fast-track rules’.

3.24 Childcare costs are assessed as an average and not as actual weekly amounts paid. The renewals notes expect people to check their average costs using arithmetic and to be familiar with rules on childcare. There are penalties which may be applied for failing to tell the Revenue within three months:

- if childcare costs (that are eligible for childcare tax credit) are not paid for four consecutive weeks;
- if costs go down by at least £10 a week for four consecutive weeks, or;
- if no childcare costs are incurred.

3.25 This degree of complexity places considerable expectations on people who may be the least able to comply with rules, which may result in them incurring financial penalties after being accused of being negligent.

Award notices and other correspondence

- 3.26 Award notices are issued when a claim is made, and when changes are recorded that alter the award.
- 3.27 The overwhelming feedback from CAB advisers is that there is simply not enough information on the award notice for the claimant or the adviser to understand their entitlement or to check it's accuracy.
- 3.28 Some award notices contain 18 or more separate figures, which are a mixture of entitlement, overpayments, recoveries, and payments. They do not show how any of these figures have been calculated.
- 3.29 Deciphering notices can therefore be a challenge even for many specialist CAB advisers, let alone for our clients. In addition, at present Tax Credit Helpline Advisers do not have access to claimants' award notices on their computers, and so cannot easily explain them to claimants or to CAB advisers.
- 3.30 The transparency of award notices is significantly reduced, at present, by the following problems:
- Award notices generated when a change of circumstances has been reported state that they result from 'recent information', but do not state what the information is. This prevents claimants knowing whether the change they reported has been taken into account correctly;
 - Income figures do not distinguish between earnings, benefits or other income, which makes it difficult for claimants to check accuracy;
 - Award notices do not indicate all the elements of tax credit a claimant is entitled to, the periods they relate to, or the amounts involved. Child tax credit cannot be distinguished from the childcare tax credit;
 - Relevant dates are not shown – for example children may be listed but it is not apparent if the award relates to them for the whole or part of the year. Similarly, the dates of changes to hours which affect entitlement to WTC are not shown – claimants must retain all award notices to have a history of changes. This also leads to difficulties when people need to claim housing benefit;
 - The award notice does not tell the claimant whether they are entitled to maximum child tax credit – which is the 'passport' to a range of additional help including free prescriptions and school meals;

- The baby and family elements to tax credits are not identified as such. Awards that include amounts above the family element can entitle claimants to other help;

3.31 Citizens Advice has welcomed the opportunity to participate in the re-design of award notices and it is encouraging that many of these issues will be addressed in future designs. We are disappointed that they will not be introduced until April 2006.

3.32 In the interim the Revenue should recognise that not all claimants will fully understand or be able to check their entitlement. **It is essential that Tax Credit helpline advisers are better able to explain notices to claimants and that a lighter touch is taken when expecting claimants to understand their responsibilities for checking award notices, reporting errors or changes of circumstances.**

3.33 The history of administration and system problems also affected award notices. Children were 'lost' in the system: award notices would sometimes give no entitlement. Also thousands of awards presented contradictory messages which led DWP¹⁵ to issue specific housing benefit guidance explaining how to interpret apparently contradictory statements in award notices, such as:

"Child tax credit £2507

This award is based on the information given by you. You have no qualifying children and are receiving a qualifying benefit".

3.34 When couples reported a partner's income change, the computer system reset the other partner's income to nil, resulting in large overpayments. These errors were difficult to spot on award notices, since the 'change' was something that had not been reported. Worse still, in some cases the award notice did not even correspond with the information held on the computer – it showed the correct income when a 'nil' income had been used in the calculation.

3.35 This problem led to tens of millions of pounds in overpayments¹⁶ and the Revenue wrote to all claimant households affected in late summer 2004. The letter advised that the Revenue had incorrectly calculated the award and acknowledged responsibility:

"I am writing to let you know that your tax credits have been overpaid since April because we calculated your award incorrectly, to apologise for our mistake and to explain the arrangements for repaying this money. We estimate that the incorrect payments currently amount to £4293.19"

¹⁵ Housing benefit guidance, DWP, Summer 2003

¹⁶ *Uncorrected oral evidence to the Public Accounts Committee, Q.5 24 January 2005*

3.41 In another example, a letter received with two award notices on the same day (both showing tax credit entitlement) read:

“if you are no longer receiving tax credits we will contact you again when we know your final tax credits entitlement for 2003/04 to make arrangements for repayment.”

3.42 Manually produced letters do not depend on changes to the IT system. **Therefore we recommend that manually produced letters should be improved without delay.** We welcome the review of correspondence that the Tax credit office is currently undertaking and expect to see marked improvements in the near future.

4. Tax credits helpline

- 4.1 CAB advisers need to be able to contact tax credit staff who are able to provide accurate information about claimants' tax credit claims or awards, within a framework which protects personal information. A dedicated phone number was provided for the use of third party advisers, but did not work as well as intended. The Revenue made considerable efforts to improve things, once it became apparent that large numbers of people were seeking help with tax credit problems from Citizens Advice Bureaux. A team was assigned to staff the adviser helpline, and a system was put in place to ensure that bureaux could register themselves and transmit evidence that they were acting with their clients' permission.
- 4.2 Resolving the substantial number of problems has also been made very difficult because of poor systems, and consequent delays. CAB advisers tell us it is frequently problematic trying to contact the Revenue about their clients' cases. It can prove extremely difficult to correct mistakes made on awards by phone, even though CAB advisers have been given procedures by the Revenue to allow them to act on their client's behalf.
- 4.3 The move to a call centre service (with only limited face to face service available through a small network of Revenue Enquiry Centres) has proved difficult. Citizens Advice has previously reported that call centres do not work well for people trying to resolve problems with any degree of complexity, or for people who have learning disabilities or do not speak English. Our report *Hanging on the Telephone*, published in September 2004, noted that:

“Critical problems about money, debts and benefits, often affecting people on low incomes, just do not get resolved as quickly or effectively as they should.”

- 4.4 We urged that service providers should fully 'user-proof' all their call centre operations, undertaking regular audits of accessibility, usability and performance from the perspective of users and intermediaries, such as Citizens Advice Bureaux. Evidence from bureaux suggests that the quality of service provided by the tax credits helpline has fallen short of desirable or acceptable standards. One of the most frequent reports by advisers has been that they can't get to speak to someone who can help with their query. The following are typical examples:

“It should be possible to speak to the relevant officers by telephone to resolve straightforward errors quickly”.

“Both client and the bureau have contacted sections of the Revenue but problems are still not resolved as no-one person or department are willing to accept responsibility to resolve the matter.” “The helpline are unable to contact the Appeals section as they don't have a telephone number.”

“Helpline advised that the Appeals section was not contactable by telephone so we wrote a letter. When they called the helpline the following month there was no record of their letter and the only way this could be chased was by writing again.”

4.5 One of the main current problems with the tax credit helpline is that there are essentially no caseworkers for advisers or claimants to be put through to – all the information on the system should be available for the helpline advisers to access. It is very common for advisers and claimants to be told by helpline advisers that there is a problem with their case but they do not know when it will be resolved and payments will be resumed.

4.6 The Paymaster General’s statement of 26 May 2005 suggests that there are some more basic problems to address:

“HMRC will develop options to improve the quality of service on the helpline, in particular to ensure that helpline operators can track the progress of individual cases in the system, reducing the need for families to contact the helpline on multiple occasions.”

4.7 This is welcome, but the quality of service available through the helpline needs to improve rapidly. Citizens Advice has argued that call-centres should be user-proofed by focussing carefully on how services perform, especially for the most complex cases, and for those people who find using the service the most difficult. **We recommend that user-focussed principles, as set out in *Hanging on the Telephone*, form the basis for the options being developed for the tax credits helpline.** Citizens Advice would be keen to assist with user-proofing the helpline from the perspective of CAB clients and advisers.

Advice on more complex issues

4.8 With around 3000 staff on the helpline and the number of varied calls they individually deal with, it is perhaps not surprising that in the more complex aspects of entitlement the helpline invariably seems unable to assist. CAB evidence shows poor advice given to claimants on:

- working tax credit when on sick leave;
- help with childcare costs when looked after by a relative in their home who was a registered child minder; and
- entitlement to the 50 plus element.

4.9 The following examples show some of the difficulties the Tax Credit Helpline has had in providing correct information:

A woman was on sick leave following the death of her husband in an accident. The helpline advised her that she would not be entitled to working tax credit until she returned to work. Without seeking a second opinion she would have lost out on over £70 a week.

A lone parent was told by the helpline that she could claim childcare costs when her mother, a registered childminder was looking after her children in her home. Three months later she was visited at work to ask about her childcare. She was then told she would have to repay the monies already paid. She called the helpline again, and was told by three different advisers that someone in her circumstances could claim help with childcare.

A woman phoned the helpline to inform them of a change of circumstance – her self-employed husband was temporarily not working – he had applied for incapacity benefit. She was told incorrectly that they would no longer be entitled to working tax credit. The Helpline did not realise that he would count as working for the first 28 weeks of sickness.

A client wanted advice on whether he would be better off in work. He was over 50 and would have been entitled to the additional 50+ element of WTC, and would only have had to work 16 hours to be entitled to WTC. The Helpline misinformed him that he would have to work 30 hours. When the bureau called back, they acknowledged the error.

- 4.10 There are now some indications that bureaux advisers and other intermediaries are developing better relations with tax credit helpline advisers, through regular contact. The Revenue has also now established a 'complex issues' team. Helpline advisers can, after seeking the agreement of a supervisor, take details and pass the case on to this team. The Revenue is aiming to contact claimants by the end of the next day to acknowledge receipt of the query.
- 4.11 We welcome the introduction of a new complex issues team. CAB evidence suggests this was long overdue. It is infinitely preferable for helpline staff to say "this case is beyond me" rather than giving incorrect information. We are not entirely clear what criteria will be used other than a helpline adviser and supervisor deciding that the case merits onward referral, but the fact that the need has been recognised is a step in the right direction.
- 4.12 The Revenue has indicated that tax credit helpline advisers speaking to Citizens Advice Bureaux and others on the Intermediary Helpline will be able to seek information from the complex issues team, and call CAB and other advisers back to deal with their query. We recommend that the system of referral to specialist tax credit staff is reviewed after a short period of operation with a view to allowing calls to the intermediary helpline to be transferred direct to the specialist section.
- 4.13 The Paymaster General's statement of 26 May 2005 recognised the need for improved information and advice, and noted the crucial role of the voluntary sector:

“Tax credits are working well for millions of families but the system is new and requires active engagement from claimants. The role of the voluntary sector in providing advice to families receiving tax credits is crucial. I have asked HMRC to develop innovative ways of working with the sector to target more active support on vulnerable families.”

- 4.14 Citizens Advice Bureaux are already providing advice to thousands of tax credit claimants, and we will welcome discussion about further partnership working with HMRC. **The government must also recognise that face to face advice will always be necessary for many claimants, and consider the need for improved provision of this channel of advice through HMRC.**

5. Official error, reasonableness and compliance

- 5.1 The acknowledged need for improved communication with claimants makes it difficult to understand why the Revenue approaches recovery of overpaid tax credits on the assumption that communication with claimants is always clear, or why compliance interviews alleging negligence have taken place.

'Reasonableness'

- 5.2 In many cases, the Revenue has maintained that it was "reasonable" to expect claimants to have noticed the errors in their award, and consequently that they should remain liable to repay an overpayment.
- 5.3 The definition of official error is twofold: where the Inland Revenue has made a mistake and where in addition, it was "reasonable" for the claimant to believe that their award was correct.
- 5.4 The Revenue's Code of Practice on overpaid tax credit refers several times to 'reasonableness' when describing circumstances when overpayments might not be recovered. The Code says:

"We may decide that you should not be asked to pay back all or part of an overpayment if you were paid too much because of a mistake by us and it was reasonable to think your award was right... "

- 5.5 The Code goes on to say:

"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. It would have to be reasonable to think that your tax credit award was correct.* For example, if we were paying you tax credits on the basis of the wrong number of children, that is the sort of thing we would expect you to spot on your award notice and tell us about. And we would also expect you to tell us if your employer was paying you more tax credit than your award notice said you were entitled to. In deciding whether it was reasonable to think your award was correct, we will consider all the circumstances of your case. We will take the same approach where the mistake that led to the overpayment was made by another Government Department." [emphasis added]

- 5.6 All overpayments are automatically recovered until challenged by the claimant either on the basis of official error or on hardship grounds. In the latter case, repayment arrangements may recoup tax credits over longer periods (and people receive 'hardship' payments). But as at the end of February 2004 the Revenue had not written off any overpayments on grounds of hardship either fully or in part.¹⁷

¹⁷ Hansard 23 Feb 2005, Column 643w

5.7 Decisions to recover overpayments are made at the discretion of the Revenue in accordance with their Code of Practice. There is no formal right of appeal about whether or not it is reasonable to recover, though there may be discussion about the rate of recovery. Claimants can only appeal against decisions about their entitlement. The Revenue takes decisions about the client's circumstances, and whether or not it was reasonable to expect them to notice an error on their tax credit award notice. Independent assessment of these decisions is only possible if the claimant goes through the complaints procedure and then goes to either the Revenue Adjudicator or the Parliamentary Ombudsman.

5.8 A claimant may expect to receive several of these notices in a year. In one example, on one day a client received a letter informing her of an overpayment of nearly £400, plus two award notices, one of which said she had an overpayment of over £1000. Within the next few days she received three more award notices, all with different overpayment figures, and listing different rates of weekly payments. As the Parliamentary Ombudsman said to a Select Committee in December:

“If you have six different award notices and you have no real idea which of those, if any, is right, having a debate about whether you reasonably believed that that was the right figure is not helpful in those circumstances”.¹⁸

5.9 Our view is that the layout of 4-page award notices, the accuracy and relevance of the information they contain, and the issue of multiple notices, will frequently make it highly *unreasonable* to expect people to notice errors in all cases. Even if there was significantly greater clarity and accuracy in award notices, the expectations of financial and actual literacy amongst all tax credit recipients are in many cases unrealistically high. We do not think it is reasonable to rely on award notices as the basis for recovery and compliance action because:

- There has been a long history of problems with award notices;
- It was necessary to devise a ‘crib sheet’ (Form TC602PE) for issue with award notices in order to try to help claimants comprehend them, following pressure from Citizens Advice and other groups;
- Award notices (and other written tax credit communications) are now subject to further revision in order to secure greater clarity and comprehension;
- CAB evidence shows continuing difficulties for clients in reading and understanding award notices.

5.10 Even where claimants have spotted errors they have found it difficult to have them corrected. Our files contain frequent examples where people

¹⁸ Ann Abraham, Health and Parliamentary Ombudsman in evidence to the Commons Public Administration Committee, 2 December 2004.

queried manifestly incorrect payments or substantial lump sums paid into bank accounts. Many were informed that the payment was correct, was theirs to keep, and that they should go out and spend it. In such cases we would argue that it would not be reasonable to recover and the two-pronged approach to recovery is not fair.

Just after the 2003/04 year end a woman was paid a lump sum of £3,500 by the Revenue. She returned the money as she didn't believe she'd been underpaid. The Revenue insisted it was due and paid it a second time. When she returned it a second time the Revenue contacted her insisting it was hers and paid it a third time. A couple of months later she was notified that she had been overpaid by £4,900.

- 5.11 In order for any overpayments to be written off on grounds of official error, claimants must take action to dispute the recovery.
- 5.12 Decisions to recover overpayments should be capable of challenge, both informally and formally, in the interests of fairness. Claimants must have the right to appeal against decisions that hold it was 'reasonable' for them to have spotted an error. **We recommend that HMRC takes steps to contact everyone who has been overpaid as a result of an official error, in order to give people the chance to challenge the decision to recover.**
- 5.13 We do not accept that the current application of the Code of Practice is fair to claimants. **Citizens Advice recommends the introduction of a proper, independent right of appeal to a social security tribunal against decisions to recover tax credit overpayment on the grounds of official error.**

Compliance

- 5.14 As noted in previous sections, there is also very little understanding of the penalties which the Revenue can (and does) impose on people it thinks have deliberately made a negligent, or fraudulent, claim or statement. There are penalties of up to £3,000 in such cases. Failure to provide information or evidence can result in a penalty of £300 plus daily penalties of up to £60. Interest may also be charged on all penalties.
- 5.15 Citizens Advice Bureaux are now advising clients who have been subject to investigation, and face accusations of negligence. In several examples, it is at least arguable that the client was not negligent, but perhaps just insufficiently aware of the importance of being scrupulously accurate. The Revenue has said that "negligence" can simply mean "not taking sufficient care". In a letter to an adviser helping clients to challenge a decision to charge them a £500 penalty plus interest, as well as to recover an overpayment, for making a mistake on their claim form, the Revenue compliance manager said:

“Negligence is not defined within the Act, but rather carries its ordinary day to day meaning. Simply put they did not take sufficient care when completing the application.”

- 5.16 In the above case, the clients were a couple with five children, one of whom is disabled and receiving disability living allowance, middle rate care and low rate mobility. The man earns about £11,000 a year, and the woman has just started low paid part-time work. According to the compliance interview notes the clients did not know of any incorrect details on their application form, but were receiving a severe disability element for child tax credit. The clients agreed that a mistake had been made, but did not consider they had been negligent.
- 5.17 In another example, a lone mother had entered £150 as childcare costs on her claim form. This amount was only in fact applicable during school holidays, and the client had stated this on her form by writing on the form. She was investigated, and the Revenue Compliance Officer stated in his note of the interview that “IT was XX’s responsibility to complete her form correctly and check the award when it was received. [The officer] said that the amount of the overpayment was £5000. [The client] accepted that she had been negligent in not checking her award.”
- 5.18 In fact, the client had written a correction onto the agreed notes of the interview. The client wrote: “ I made an error when filling in the form – I misunderstood what I had to do – negligent I feel is a very strong word. I believed the award to be correct.” The client subsequently wrote to the Revenue saying,
- “on receiving my award statement with my entitlement listed it is not clear what sum is being paid for the childcare element. I do not understand or know the figures the government sets out for a single parent working mother so I did not think the figure on my award was wrong. Nobody in the Revenue checks that these forms are filled out correctly before being scanned if they were I am sure this error would not have occurred.”
- 5.19 The client was told that she was liable to repay the £5000, and that she could also be charged a penalty of up to £1000. She was told that she should take out a loan to repay the debt, and that she would need to produce three loan refusals to show this was not possible. If she did not get loan refusals a further penalty of £250 could be applied, and repayment with interest added would be spread across current awards.
- 5.20 Citizens Advice has received several other reports where clients have been informed by local compliance officers right across the UK, that they must take out loans in order to repay tax credit overpayments, and must produce copies of loan refusals before any other repayment plan will be considered. For instance, a letter from an area compliance team concluded:

“In the meantime, if you are not in a position to settle the debt in full, please try and obtain finance. If you are not able to obtain a loan then please get at least three letters of refusal from loan providers.”

The interview notes signed by a compliance officer noted that she had ‘suggested that she try to obtain funds via interest free credit cards or loans from a financial establishment, or family or friends to provide funds to pay off her overpayment and briefly explained the ramifications.’

A man interviewed about declaring an incorrect income figure on his tax credit claim was asked by a Revenue compliance officer to approach his bank for a loan so he could repay the overpayment in a lump sum. When his bank refused him a loan he visited the CAB for advice.

- 5.21 Actions of this sort run completely counter to wider government policy which aims to control levels of debt, encourage responsible lending and borrowing, and increase financial literacy.
- 5.22 The Revenue Tax Credits compliance manual lists ways in which people can be asked to raise funds to repay tax credits. The Revenue policy team responsible for compliance issues has confirmed that advising clients to take out loans to repay tax credit overpayments is not policy.
- 5.23 Our evidence suggests that wrong advice has been given out by local compliance teams in more than ten different regions of the UK. **We welcome the steps that have been taken to prevent this happening, but would like to see the correct procedures properly enforced. Requiring people to apply for loans which they may not be able to repay is unacceptable practice.**

6. Income from tax credits – is it guaranteed and stable?

- 6.1 In this chapter we examine CAB evidence on clients' experiences of being paid tax credits. The government has long recognised that poverty and low incomes have severely damaging impacts, but has yet to fully appreciate that tax credit income needs to be guaranteed, secure and stable.
- 6.2 The reality of claiming and receiving tax credits has been extremely disappointing. The system has not proved capable of providing a secure income for many CAB clients. Large numbers have now become disillusioned with tax credits, because they have discovered that the income they thought was guaranteed can disappear. There have been:
- Administrative errors and IT system failures;
 - Difficulties for claimants and advisers in resolving problems;
 - 'Adjustment' of tax credit awards during the tax year, leaving families with inadequate income;
 - Recovery of overpayments after the year end.

The impact on clients

- 6.3 There are now almost 6 million families in receipt of tax credits, but not all are dependent on tax credit income to pay rent, feed their children or to pay for childcare in order to stay in work. There are 3.6 million families who receive more than the £10.45 a week child tax credit family element. These are families who cannot afford to face sudden significant reductions in income, or delays in payment.
- We have received reports of people whose jobs are at risk, because they cannot continue to pay for childcare after losing the support they were getting from tax credits;
 - We continue to see people whose actual incomes are below the level of income support, and who are by definition living in poverty, often as a result of a tax credit error that was not their fault;
 - We have seen people whose homes are at risk, because they are in arrears with rent or mortgage payments after tax credit income was stopped or severely reduced.
- 6.4 In 2003/04, there were 3.5 million children living in households in poverty using an after housing costs measure and 2.6 million before housing costs. Children living in lone parent households, a household with no adult in work, or in a household in which one or more member has a disability are more at risk of poverty¹⁹. The tax credit system is designed to take these factors into consideration. Extra support is aimed at these households through the disability elements and access to working tax

¹⁹ *Households Below Average Income Statistics 2003/04*, DWP, March 2005

credit at 16 rather than 30 hours. These families stand to benefit the most from tax credits and consequently have the most to lose if things go wrong.

- 6.5 CAB evidence suggests that most families who have experienced the now recognised problems associated with the administration of tax credits are very likely to be those living in, or most at risk of, poverty. Those who are most dependent on the system are most likely to suffer when things go wrong.
- 6.6 CAB users are more likely to be on benefits and in low paid work, have a long term illness or disability or live in social housing than the UK population as a whole²⁰. Therefore although CAB tax credit clients may be a relatively small percentage of total tax credit claimants, they form a much higher percentage claimants who depend on tax credit as a core part of their incomes.

A guaranteed income?

- 6.7 Tax credits were designed to provide an *income guarantee* and an *integrated* and *seamless* system of financial support. Stability and continuity of income are vitally important to families who have to manage on very tight budgets and for those for whom the option to take up or remain in paid work, to stay out of poverty and out of debt, depends on fine calculations and security of income.
- 6.8 Adjustments in year and recovery of overpayments, affect both working tax credit and child tax credit and can cause sudden and substantial reductions to tax credit payments - for many people there is no *certainty* about in-work income, and also less *stability* of out-of-work income for families receiving child tax credit.
- 6.9 Income from tax credits can be less secure than income from social security benefits which can only ever reduced by a fixed percentage. Social security entitlement is typically determined by current income and other qualifying criteria. Weekly benefits are paid on the basis of weekly entitlement. Tax credits are totally different. Entitlement to tax credits is only confirmed after the end of the tax year. Payments made during a year are based on income during the previous year or an estimate of income for the current year.
- 6.10 In addition, the Revenue's recovery powers differ from social security rules, and allow the Revenue to recover any overpayment however it occurred – even where it has resulted from a Revenue error.
- 6.11 Working tax credit provides support for people in work, child tax credit for people both in and out-of-work. Changes that affect working tax credit entitlement can also affect child tax credit payments. This means families that lose entitlement to working tax credit, for example through

²⁰ *Unmet Demand for Citizens Advice Bureaux*, MORI 2003/04

stopping work, can potentially lose support for their children if an overpayment has accrued. This is because no distinction is made between the two credits when adjusting tax credit payments during the tax year to avoid overpayments.

6.12 Problems can arise because entitlement to tax credits is for the tax year – and therefore cannot guarantee to provide even, or regular, weekly or monthly payments.

Overpayments

6.13 Figures published in June 2005 show there were very high levels of overpayments in tax credit awards during 2003/04²¹:

- One third of all families awarded tax credits were overpaid in 2003/04;
- Over half of all overpayments were over £500 and one third were over £1000;
- Over 300,000 families effectively owed the Inland Revenue between £2000 and £5000;
- £1.9billion was overpaid in tax credits;
- Over 700,000 families have been paid less than they were entitled to totalling £464 million and 60% of these families have incomes below £15,000.

6.14 For the last 18 months, overpayments and recovery of overpayments from tax credit payments has been the number one tax credit enquiry dealt with by bureaux. Bureaux across the UK have seen thousands of claimants who have been overpaid and face severe hardship as their ongoing payments have been cut.

6.15 In most cases where families have ended up living on income support, receiving child tax credit significantly below their entitlement arose because there was an overpayment of working tax credit when someone in the family was in work or left work. This problem has been particularly serious in relation to in-year adjustments, as small overpayments can push claimants well below poverty levels particularly if they arise near the year-end. For example:

A lone parent was left with weekly income of £55.65 income support and £9 child tax credit due to an in-year overpayment. The client's partner, who had looked after the children, had died and the client had given up work as she couldn't find affordable childcare. She reported the change and claimed income support. At the end of February she received a letter from the Revenue informing her

²¹ *Child and Working tax credits finalised awards 2003-04*, HMRC analysis team, June 2005

that she had an overpayment of £185 and as a result her child tax credit payments would be reduced by over £30 a week for the remaining six weeks of the year.

A lone mother with two children was left living on income support at the adult rate of £55 per week, with no payments for her children. She'd had to give up work when she was no longer able to pay her childminder. The client had been overpaid and payment of WTC had been stopped.

A woman with two children was living on £139 incapacity benefit each fortnight after stopping work. The client had notified the Revenue that she had stopped working but the change had not stopped payments. The client was having trouble feeding her family and had multiple debts.

- 6.16 The recovery of overpayments is not covered by legislation. Instead it is set out in the Revenue's *Code of Practice 26 What happens if we pay you too much tax credit?*²² This code states that the Revenue will not recover an overpayment that arose from official error. The definition of official error is twofold: where the Inland Revenue has made a mistake and where, in addition, it was reasonable for the claimant to believe that their award was correct.
- 6.17 As noted above, the Revenue will seek to recover in cases where it considers it was not reasonable for the claimant to assume the award was correct. In practice unless a claimant disputes it, recovery will be made in full.
- 6.18 Even where claimants do dispute the recovery on grounds of official error, recovery continues for long periods whilst the matter is resolved.

A lone mother was running up credit card debts to buy food for her four children because her tax credit payments dropped from £200 to £20 a week to recover an overpayment that originated from Revenue error. The overpayment resulted from calculation errors and an emergency payment. The helpline advised that it would take between two weeks and six months to get a decision on whether it would be written off.

In July 2004 a client was informed she'd been overpaid £1200 in working tax credit. It was being recovered from her child tax credit at £10 a week. The adviser found it was due to a backdating error and helped the claimant to dispute the recovery. After six weeks, they were told it would take six to eight weeks to resolve. After further correspondence the overpayment was written off in May 2005, ten months after it was originally disputed.

²² Code of Practice 26 (an extract is shown in Appendix 3)
www.hmrc.gov.uk/leaflets/cop26.htm

6.19 Figures for Spring 2005 show that 214,000 families had disputed the recovery of their overpayments and £14 million had been written off, but 125,000 families were waiting for decisions on whether their overpayments would be written off. In the last year the team dealing with these disputes has increased from around one hundred to five hundred staff with administrative costs rising to £7.6 million in 2004-05. In addition to deal with the backlog, the Revenue has introduced streamlined procedures which we believe are likely to result in writing-off more overpayments. We welcome this decision.²³

6.20 We have concerns about how the Revenue decide what it is reasonable for the claimant to have understood about their awards and the lack of rights for them to formally appeal their decision (see section 5 on reasonableness).

6.21 Overpayments can occur when²⁴:

- Income rose by more than £2,500 in the previous tax year, and the claimant did not inform the Revenue (whether intentionally or not);
- The claimant did not tell the Revenue in time about a change of circumstances that reduced entitlement, or the Revenue does not implement a notified change;
- Incorrect information was given to the Revenue;
- An error is made by the Revenue.

6.22 'Overpayments' can occur during the year and at the end of the year. The impact on families will be more severe if identified during the year, especially if near the end of the tax year, as there will be less time within which to adjust payments to 'recover' the likely overpayment.

6.23 If an overpayment is not discovered until the end of a tax year, it is usually recovered by reducing ongoing payments by a low, fixed percentage. If a change to a household's circumstances leads the Revenue to project that they will be overpaid they can reduce or stop all further payments, in order to ensure that by the end of the year they will have received the 'right' amount.

6.24 Claimants can also find they have an overpayment even when they inform the Revenue of a change in their income immediately. For example, a parent may start the tax year on a very low income and have entitlement to working tax credit including the childcare element. On moving into a full-time higher paid job a few months into the tax credit year, they could end up with a large overpayment, and cease receiving any tax credits altogether.

²³ *Hansard*, 6 June 2005, c298-300w

²⁴ from *Tax Credits: one year on*, Marilyn Howard CPAG 2004

6.25 It is quite possible for the current system to pay a family's full tax credit entitlement between April and October, and then nothing further for the rest of the year. Automatic adjustments within a tax year can result in families losing all their tax credit payments until the start of the new tax year. This is a basic problem that has not been solved by design features such as minimising the number of compulsory changes that affect awards, nor by the complex formulae that exist to limit in-year and year-end recovery.

Poverty caused by recovery of overpayments during a tax year

6.26 There has been, and continues to be, real hardship resulting both from errors and from recovery action. From Autumn 2003 bureaux began reporting clients facing severe reductions in payments that left them in hardship and confused about what had happened. There were substantial percentage adjustments to tax credit awards during the year left people – mainly lone parent families – on incomes below benefit levels.

6.27 Citizens Advice began to monitor all the cases reported by bureaux to discover what had caused reduced payments, to what extent they caused hardship and whether the Inland Revenue had explained the reduction to claimants. Between August 2003 and April 2004, bureaux reported the cases of 781 claimants who had been informed that they had been overpaid in the year. Of these cases:

- 82% had experienced their payments reduce or stop without advance warning;
- almost half (44%) had their payments cut to at least 50% of their entitlement;
- 34% of claimants saw their payments stop completely;
- Nearly a third (29%) of those whose payments were reduced were in receipt of income support or jobseeker's allowance. The reduction therefore put their income well below the poverty level set by the Government and recognised as the minimum amount required to live on;
- In 75 cases, families on income support lost all their child tax credit payments.

6.28 In some cases, overpayments had resulted from increases in household income which hadn't been reported, but many others resulted from errors made in calculating their award, or from delays in the Inland Revenue responding to changes in the claimant's circumstances. Many CAB clients were shocked to find themselves with large overpayments and a big drop in their future payments as their awards were both

reduced to the new 'correct' level and reduced further to recover the overpayment from the previous year.

6.29 For families on the lowest incomes, any reduction in payment below their entitlement will mean their incomes will fall below the poverty level set by the Government – that is, income support. On top of this reduction, a claimant could also be having a fixed rate reduction for the recovery of an overpayment from a previous tax year, or for a social fund loan or other deduction from benefit.

6.30 The table below shows examples from CAB cases where family incomes were left drastically reduced because of recovery of overpayments. Percentage reductions in child tax credit ranged from 19% to 93%. These cases resulted in considerable hardship.

Case	Family composition	Total income inc. child tax credit £	CTC lost £	% CTC reduction	New weekly income £
1	Couple and 3 children	217.00 (CTC 93.70)	67.00	(72%)	150.00
2	Lone parent 4 children	224.40 (CTC 121.45)	23.59	(19%)	200.81
3	Lone parent 3 children	185.90 (CTC 93.70)	86.73	(93%)	99.17
4	Lone parent 2 children	147.40 (CTC 65.95)	30.70	(47%)	116.70
5	Lone parent 1 child	108.90 (CTC 38.20)	32.87	(86%)	76.03
6	Lone parent 1 child	108.90 (CTC 38.20)	35.17	(92%)	73.73
7	Lone parent 1 child	108.90 (CTC 38.20)	24.90	(65%)	84.00
8	Lone parent 1 child	108.90 (CTC 38.20)	27.88	(73%)	81.02
9	Lone parent 1 child	108.90 (CTC 38.20)	30.00	(79%)	78.90
10	Lone parent 2 children	147.40 (CTC 65.95)	26.95 + 22.14 Social fund	(41%)	98.31

6.31 There were several reasons for these problems in the first year of tax credits:

- Emergency payments made because of severe delays in processing claims, which resulted in duplicate payments;
- Increases of income between 2001/02 and 2003/04;
- Errors

6.32 Examples of the amounts, causes and apparent explanations for these overpayments are shown in the table below.

Case	Amount	Cause	Explanation
1	£3108	IR did not respond to reported changes in circumstances.	Client no longer working and partner also reduced hours
2	£1995	Error – and incorrect advice.	Award too high, but when queried numerous times was incorrectly informed it was correct.
3	£2100	IR error and delay in correcting incorrect childcare costs	Childcare down as £3100 a week instead of £250 a month. Reported change, new award notice after four weeks, but still wrong so had to report again.
4	£4000	Changes of circumstances and errors.	Client had had lots of changes to his circumstances and had also received lots of incorrect award notices.
5	£2300	IR error, deletion of partner's income	When baby born reported change and received new larger award. Did not notice income recorded as nil as had not reported change in income details.
6	£2380	IR error and change of circumstances	Clients husband stopped work due to illness. She informed the IR and a lump sum was paid into his account in error.
7	£2800	Interim payment	Clients experienced delays in the processing of his award at the beginning of the year.
8	£3000	Error and poor advice incorrectly confirming award correct.	Paid £7000. Called the helpline a number of times to check award was correct. Was later told she'd been overpaid and was frightened to tell her husband.
9	£5000	IR income error.	Award said working 45 hours with income of nil.
10	£9000	Client didn't inform IR that she'd left work and planned to go back.	Client continued to receive WTC for four months after she'd left work.

6.33 The actual experience of 'responsiveness', for CAB clients, has had drastic effects on tax credit payments and has caused considerable hardship and damage to work incentives. The problems described above do date from the first year (2003/04) of tax credit operations - but we are still seeing evidence of identical problems relating to the second year (2004/05) of severe hardship being caused by in-year adjustments to people's tax credit payments.

6.34 The following cases are typical examples taken from many thousands we have received. All are relatively recent, dating from February and March 2005. They represent typical examples of problems that are replicated nationwide:

Work incentives

A woman had to *cut her hours* to look after her children after WTC payments were reduced and she couldn't pay for childcare.

A lone mother client owed £1200 in unpaid childcare charges and *was worried she'd have to stop work*. The client was told she'd been overpaid tax credit of over £4000.

Client separated from husband. She had kept the Revenue informed. Received demand for repayment. "They have other debts. They both work long hours but a debt of £2300 is worrying for them."

"Clients have changed circumstances and have always notified TCO. Various different calculations have been received, sometimes on the same day. They have been told there are overpayments, then underpayments. Repaying the alleged overpayment has caused severe financial hardship and the husband has given up his job *as they feel he is better off not working*."

Hardship

A lone mother with two children was left with no money for three weeks when CTC stopped. The woman had sent her children to stay with friends, as she could not put money in her gas and electricity meters, nor could she make any calls on her phone. She applied for a social fund crisis loan, but was told that money could not be offered "to bail out another government department".

A lone parent with three children was left with income comprising £55.65 *income* support and £39.65 child benefit when tax credits stopped. The client had received a lump sum of over £4000, queried it, and was assured she was entitled. The client used the lump sum to clear outstanding debts. The client had told the Revenue her job had come to an end.

"Young couple with two young children. Husband developed back problems *and* could not continue work as scaffolder. They are struggling to live on £114 a week for the four of them. Bureaux queried recovery and Revenue reinstated payments less 10%. When I queried how they could just cancel such a significant amount which left the family without enough money for food, they said they could do this."

Family, two children, both parents working. "We are currently at a loss to explain overpayment as income has diminished." Childcare costs to enable both to work are £550, but currently no help being received. Clients face repossession.

"The clients are receiving no child tax credit. They are surviving on JSA for a couple. They have a mortgage to pay" [Couple with one year old *child*, husband made redundant, had discovered large amounts of tax credit in account. Rang helpline three times – each time told award

was correct] “Lone parent one child. Gave up work and informed IR. Client now receiving only child benefit to support child”. Norwich

Lone mother left in severe financial hardship. WTC stopped for two months. Has one child and rent of £75 per week.

A lone mother was overpaid by almost £500 when she stopped working 16 *hours* a week. Child tax credit was cut by over £20 per week, leaving the client with income support of £52, plus CTC of £19. The client had rent arrears and was being taken to court.

A client *was* left with only income support, child benefit and £3 in child tax credit to live on causing severe hardship.

‘Top-up’, ‘hardship’ or ‘additional’ payments

- 6.35 The Revenue has discretion to adjust payments to recover likely overpayments²⁵, but the computer, adjusts payments automatically to eliminate or reduce as far as possible an overpayment because it is designed to pay the ‘right’ amount by the end of the year. Alternative decisions not to recover, or to recover at a slower rate to prevent hardship cannot be made until a claimant contacts the helpline and requests a top-up payment.
- 6.36 In the event, the Inland Revenue decided to use its discretion not to recover all overpayments within the year, by making additional payments available to all who contacted them expressing hardship. These payments would ‘top-up’ their awards back to the level at which it was feasible to expect someone to live.
- 6.37 The fact that a supposedly responsive system has required a facility to make emergency payments in order to avoid reducing family income too drastically when ‘debts’ are recovered illustrates how the system has failed many families. Nevertheless, the harsh nature of adjustment and recovery of overpaid tax credits has meant that hardship payments have been needed to provide basic levels of income security for families. This is a perverse outcome for an anti-poverty, ‘pro-opportunity’ system.
- 6.38 Top up payments (together with any payments still being received) limit recovery to either 10% or 25% of weekly payments – the aim is that claimants with lower household incomes should be left with 90% of their payments. (See extract from Code of Practice, Appendix 3.)
- 6.39 Hardship payments are part of tax credit entitlement rather than ex-gratia payments, they inevitably create further overpayments. The scheme is akin to taking out further loans, or extending a loan period, though at least no interest is payable. The need for additional payments where claimants could show hardship caused by overpayment recovery has continued to feature in the tax credits system. An estimated 65,000 giro

²⁵ Section 28(5) Tax Credits Act 2002

payments to the value of £170 million to top-up awards to prevent hardship were made during 2003/04.²⁶

- 6.40 Such a system is far from ideal. The availability of additional payments to lessen hardship is not made widely known. Claimants must either read the codes of practice and apply for payments, or receive accurate advice from the Helpline or from a CAB. In any case, there will be an inevitable delay before any payment is received.
- 6.41 The Revenue has decided that it will continue to issue top-up payments, now to be called 'additional' tax credit payments in 2004/05. It has set much more clearly defined criteria for who will and who will not be 'entitled' to them.²⁷

The importance of secure, stable incomes

- 6.42 The current operation and structure of tax credits risks running counter to the government's guiding principles for tax benefit reform and integration, which include promoting incentives to work and tackling poverty – "minimum levels of income should be guaranteed for the most vulnerable in society – the elderly, families and those who cannot work because of illness or disability."²⁸
- 6.43 People on low incomes (and arguably most households) live on daily, weekly or monthly budgets and do not budget across a whole year. Yet the tax credit system is structured annually - like the tax system. This means that if someone is paid at a rate above their entitlement for a few weeks or months their payments will be reduced below their entitlement for the next few months. This may be manageable for a medium income family entitled to £10, which is paid £15 and later has it cut to £5, but it is not manageable for a family for whom tax credits provides a minimum weekly income. For these families, reducing tax credits immediately puts them below poverty level. Taking it away can reduce their incomes by over 50%.
- 6.44 Professor Jane Millar has commented that "*no money management strategy can be sustained if income is too low to make ends meet.*" There is abundant evidence to show that people on lower incomes have developed considerable skill in managing their finances, juggling small amounts of weekly or monthly income, struggling to maintain repayment of debts.²⁹ People on low incomes may 'choose' to pay more for goods and services in order to manage a budget – using pre-payment meters with higher tariffs, or paying more for food by using local convenience stores, because doing so gives them control over their finances.

²⁶ *Report of the Comptroller and Auditor General 2003-04*, October 2004

²⁷ *Code of Practice 26, What happens if we have paid you too much tax credit?* Inland Revenue, August 2004

²⁸ *Tax credits: reforming financial support for families*, Paper 11 March 2005

²⁹ e.g. *How people on low incomes manage their finances* ESRC 2002

- 6.45 There is also research that shows how living on restricted incomes, such as the amounts afforded by income support, is characterised by “constant worry, juggling and fighting to stay afloat financially”.³⁰
- 6.46 It is widely understood that low income households are most seriously affected by debt. More than half of all households with serious debt have incomes of less than £7,500 a year.³¹ They are unlikely to have savings to cushion them through a loss of income or unexpected expenses.³²
- 6.47 It is also widely understood that the UK faces a challenge in that 12.2 million people are not saving enough in a private pension for their retirement at present³³. This represents 43% of the total working population and compares to 36% in 2003.
- 6.48 Households with low incomes tend to have little savings. The 1998–99 Family Resources Survey found that among households with less than £200 a week gross income, more than 40 per cent do not have any liquid financial savings, while 70 per cent of single parent families have none.³⁴
- 6.49 Currently, 7.4 million people are not saving at all and 4.8 million are saving only small amounts. Those on the lowest incomes (less than £15k per annum) account for 3 million of those who are not saving at all.³⁵
- 6.50 Research by the Department for Work and Pensions using the British Household Panel Survey for 1991 – 2000 found that savings behaviour is strongly related to people’s economic activity.³⁶ Changes to peoples’ work status had among the largest effects on saving and pension-building identified in the report. This means that for people leaving benefits to take up work, supported by tax credits, that change has the potential to increase both their propensity and ability to save, with consequent long term financial benefits for their household, and the economy as a whole.
- 6.51 However, the DWP also found that whilst increases in earnings, when in work, had a lesser impact on savings and pensions than changes in economic activity, a fall in earnings of as little as ten per cent had a large impact on savings behaviour. For example a ten per cent reduction in income caused 40 per cent of those saving to cease saving, and overall the proportion of people saving fell by 9% if income reduced by 10%. There was also a large reduction in the proportion that were members of occupational pensions following at least ten per cent fall in earnings.

³⁰ *ibid*

³¹ *Overindebtedness in Britain, a report to the DTI*, Kempson, 2002

³² *Action on Debt*, Social Exclusion Unit, ODPM, 2004

³³ *The State of the Nation’s Savings* Association of British Insurers, November 2004

³⁴ *Pre Budget Report 2000: The Modernisation of Britain’s Tax and Benefit System* Number 7

³⁵ Association of British Insurers, *op cit*.

³⁶ *Savings and Life events*, McKay and Kempson, DWP Research report 194, (2003)

- 6.52 The Government's own research points not only to the fact that lower income households are under financial pressure from debt and are less likely to have savings to draw on to deal with changes in their income or expenditure but also shows that changes in income of as little as 10% can result in many people ceasing to save.
- 6.53 This must surely make a powerful case for the Revenue to get the delivery of tax credits right, including policy and practice on recovery of overpayments. By failing to deliver stability in incomes for some people through tax credits, the Revenue is frustrating individuals and causing hardship in the short term. It is also frustrating wider Government objectives to create the conditions in which individuals save, and save more for their retirement over the long term.
- 6.54 The Revenue's powers to define and recover overpayments are not set out in either the Tax Credits Act 2002 or in secondary legislation. The Government resisted amendments which would have set down rules in legislation, and instead decided to cover these matters by way of a Code of Practice.
- 6.55 We believe the Code of Practice on adjustments, overpayments, and recovery needs to be revised in order to ensure that the tax credit system does not produce unintended consequences for claimants. A new Code of Practice on recovery of overpayments is issued for formal consultation. **We recommend all adjustments to payments should be limited to ensure that claimants cannot be left with weekly incomes below minimum levels.** Households on maximum child tax credit should not have their payments by more than 10% of weekly entitlement. Households with an entitlement above the family element should not have weekly payments reduced to below 75% of their entitlement. Additional payments do not represent a long-term solution because of the requirement to know about them, claim them, and because of inevitable delays in receiving them.
- 6.56 We believe it is wrong to allow payments for children through child tax credit to be reduced or stopped in order to recover overpaid working tax credit for adults, as it can throw families into poverty as they lose minimum payments for children and are left with adult income support rates, child benefit, and no or much less child tax credit. **We would like to see consideration given to limiting adjustments or recovery of overpaid working tax credit to claimants who have entitlement to working tax credit.** The intention would be to ensure that recovery only took place from families where someone was in work.
- 6.57 **Where there is an overpayment from both a previous year and a current year, recovery must not be compounded so that the maximum reductions in payments, as outlined above, apply.**
- 6.58 The substantial additional amounts for childcare are extremely welcome, but the effect when payments stop is dramatic, and we have seen cases where people have had to stop work. **We believe the childcare**

element of working tax credit should always be paid in full, in order to enable families to remain in employment. When reducing payments to recover overpayments, the childcare element should be removed from the calculation to ensure that the claimant can pay their childcare costs and their employment is not put at risk.

Appendix 1: Tax credit awards and values

Tax credit awards - family type and amounts April 2005				
Family type	No.s (millions)	Tax credit award	2005/06 annual rates (£)	2005/06 weekly rates (£)
No adult in work	0.6	Maximum CTC	1690 per child 545 per family	32.50 10.48
No adult in work	0.8	Equivalent to max. CTC through IS/JSA	As above.	
With children, at least one adult in work	1.53	Maximum CTC & some WTC	1690 per child 545 per family 1620 maximum basic element 1620 couple or lone parent rate 660 when working 30 hours 2165 Disabled worker element 920 Severe disability element 1100 50+ returning to 16-29 hrs work 1660 50+ returning to 30 hrs work	32.50 10.48 31.15 31.15 12.69 41.63 17.69 21.15 31.92
Family with children and at least one adult in work	0.71	CTC below maximum but above family element		
Family with at least one adult in work	2.0	Family element of CTC	545 per family	
Families in work	0.12	Less than the family element of CTC	Less than 545	
Working families with no children	0.3	WTC only		

Appendix 2: Award notice received November 2004 – payments page

Child Tax Credit

The full amount for the period is £547.50

Amount you owe us that will be collected from future years **£791.97**

Less amount we have already paid you for this period
 Less amount you owe us from previous years **£453.33**

Our records show that you have received too much tax credit for the year(s) to **reducing your tax credit payments** until the amount overpaid has been paid back to us.

Payments in 2005-2006

If your circumstances are unchanged, **your payments will continue** as shown below.

20/01/2006 £9.95

Your payments will then change to every 4 weeks until further notice. £42.11

Working Tax Credit

Taking your income into account, the amount of Working Tax Credit due is reduced to nil.

Unclear overpayment and recovery figures demonstrates need for new 'crib sheet' (TC602PE)

Relevant years are not detailed

'Reducing your tax credit payments' for this client means 'stopping all payments'.

CAB commented that 'your payments will continue' for this client actually means 'payments will restart in 15 months time'

Appendix 3: Extract from HMRC Code of Practice 26 – What happens if we pay you too much tax credit?

Adjusting awards during the year

During the tax year, we may find that we need to adjust your payments to avoid paying you too much tax credit over the year. This might be because there was a delay before we knew about a change in your circumstances that reduced your award, or you tell us that you expect your income for 2004-05 to be higher than the income on which we have based your award, or your award was not based on the right information or you have been paid the wrong amount for your circumstances and income.

If we find out during the year that we have been paying you too much tax credit, we will normally reduce the amount we are paying you from then on, so that we pay you the right amount of tax credit for the year, or stop paying you tax credit for the rest of the year, if we have already paid you as much as, or more than, you are entitled to. If we have already paid you more than you are entitled to, we will normally also ask you to pay back the extra after the end of the year, once all the relevant information about your income and circumstances is available.

Finalising awards at the end of the year

After the end of the year, once all the information about your income and circumstances is available, we will compare your tax credit entitlement with what we have paid you.

We will write to you about your claim and ask you to confirm that we have a correct and complete picture of your circumstances during the year and to tell us your income (or an estimate of your income) for the year.

Once we have that information, we will send you a notice about your final tax credit entitlement for the year just ended. If we have paid you too much tax credit, we will usually expect you to pay it back. In the notice finalising your award for the year, we will tell you the amount you have been overpaid. We will also tell you how we expect you to pay it back. If we have paid you too little tax credit, we will pay out the extra as a single payment.

There are several reasons why we might find at the end of the year that you have been paid too much tax credit. For example if we did not know about a change of circumstances that reduced your entitlement if your income rose by more than £2,500 in tax year 2004-05, compared with your 2003-04 income, and we did not know about it, or if you told us about a change in your income during the year but your actual income is different from what you expected.

If we identify an overpayment when we finalise your tax credit award, we can ask you to pay it back by one of the following methods reducing your tax credit award for the current year. This is our preferred approach wherever possible making a payment to us direct, due within 30 days. But for overpayments arising in 2003-04 and 2004-05, you will be able to pay in 12 monthly instalments if you wish.

Where we can, we will ask you to pay back overpaid tax credit from the previous year by taking the money from a tax credit award you are entitled to for the current year. Depending on the size of your award, we will not take more than a certain percentage of your tax credits for the next year to pay off what you owe us. Families whose incomes are too high for them to receive payments of tax credit will be asked to pay back any amounts overpaid direct.

The maximum amounts by which we would reduce your payments to recover overpaid tax credit from the previous year are

10% for claimants receiving the maximum award

100% for claimants receiving only the family element of Child Tax Credit,

and 25% for all other claimants.

These limits are applied after your payments for the current year have been calculated.

Appendix 4: Bureaux that submitted evidence

EAST REGION

Abbots Langley
 Basildon
 Beccles
 Bedford & District
 Biggleswade
 Billericay
 Bishop's Stortford
 & District
 Braintree & District
 Brandon & Mildenhall
 Broxbourne
 (Cheshunt &
 Hoddesden)
 Buntingford
 Bury St Edmunds
 Bushey (Hertsmere)
 Cambridge & District
 Castle Point
 Chelmsford
 Clacton-on-Sea
 (Tendring)
 Colchester
 Dacorum & District
 Dereham
 Diss & District
 Dunstable & District
 Elstree &
 Borehamwood
 Ely
 Epping
 Fakenham & District
 Felixstowe & District
 Fenland
 Great Yarmouth
 Hatfield
 Haverhill
 Hertford
 Hitchin
 Holt
 Huntingdon
 Ipswich & District
 Kings Lynn & District
 Leighton Linlade
 Leiston &
 Saxmundham
 Loughton
 Lowestoft

Luton
 Maldon & District
 Marham
 Mid-Bedfordshire
 (Ampthill)
 North Hertfordshire &
 District
 North Walsham &
 District
 Norwich & District
 Oxhey & District
 Peterborough
 Potters Bar
 Rayleigh
 Rickmansworth
 Rochford & Rayleigh
 Royston
 Southend-on-Sea
 St Albans
 St Neots
 Stevenage
 Sudbury
 Thetford & District
 Thurrock
 Uttlesford
 Waltham Abbey
 Ware & District
 Watford
 Welwyn Garden City
 Welwyn Hatfield
 Wickford
 Wisbech
 Witham
 Wymondham &
 District

LONDON REGION

Addington
 Barking & Dagenham
 Battersea Legal
 Service
 Beckenham & Penge
 Bermondsey
 Bexleyheath &
 Welling
 Bow (East End)
 Brent
 Brentford & Chiswick

Bromley &
 Chislehurst
 Camden HIV
 Housebound Project
 Catford
 Chessington & Hook
 City of London
 Dagenham
 Enfield Town
 Erith
 Feltham
 Finchley
 Fulham
 Grahame Park
 Greenwich Money
 Advice
 Hackney (Mare
 Street)
 Haringey District
 Harrow
 Havering
 Hendon
 Hillingdon
 (Ealing/Action)
 Hillingdon (Hayes)
 Hillingdon (Ruislip)
 Hillingdon (Uxbridge)
 Hillingdon (Yiewsley)
 Holborn
 Hornchurch
 Hounslow
 Islington
 Kensington
 Kentish Town
 Kilburn
 Kingston & Surbiton
 Leytonstone
 Malden & Coombe
 Merton & Lambeth
 CAB Ltd
 Mitcham
 Morden
 New Barnet
 Newham (East End)
 North Paddington
 Orpington
 Palmers Green
 Peckham

Strabane
Suffolk /
Andersonstown
Upper Springfield

NORTH REGION

Alnwick & District
Barnsley
Berwick
Blyth Valley
Boothferry District
Bradford
Brighouse
Castle Morpeth
Calderdale
Chapelton
Chester-le-Street
Cowgate
Craven
Darlington
Derwentside
Dewsbury
Doncaster
Durham
Easington & District
East Yorkshire
Gateshead
Grimsby
Hambleton
Harrogate
Hartlepool
Hull City Centre
Keighley
Killingworth & Benton
Leeds
Mexborough
Middlesbrough
Newcastle City
North Kirklees
(Batley)
North Tyneside
District
Otley
Pitsmoor
Pontefract
Redcar & Cleveland
Richmondshire
Ripon
Rotherham
Ryedale

Scarborough &
District
Scunthorpe
Sedgefield & District
AIS
Selby District
Sharrow
Sheffield Debt
Support Unit
Sheffield Mental
Health Unit
Shipley
South East Sheffield
South Elmsall
South Kirklees
South Tyneside
Spenn Valley
Stockton & District
Information & Advice
Centre
Teesdale District
Todmorden
Tynedale
Wakefield District
Wallsend
Wansbeck
Washington
Wear Valley
Whitley Bay
York

**NORTH WEST
REGION**

Altrincham
Atherton
Barnoldswick
Barrow-in-Furness
Birchwood
Birkenhead
Blackburn
Blackley
Blackpool
Bolton & District
Bootle
Bradford
Bury
Carlisle
Cheadle & Gatley
Chester
Chorley & District

Cleveleys
Combined Hospitals
Congleton
Crewe & Nantwich
Crosby
Cumbria Rural
Eccles
Eden
Ellesmere Port
Gorton
Halewood
Halton District
Harpurhey
Heswall
Heywood
High Peak
Hindley
Hulme
Hyndburn
Irlam & Cadishead
Kendal
Kirkham & Rural
Fylde
Knowsley & District
Knowsley District
Lancaster
Leigh & District
Liverpool City Centre
Liverpool County
Court Service
Longsight
Lymm
Macclesfield,
Wilmslow & District
Manchester Central
Manchester District
Marple
Middleton
Millom & District
Morcambe &
Heysham
Netherley
North Liverpool
Northwich
Old Trafford
Oldham District
Paveways
Pendle District
Preston & District
Prestwich

Radcliff	Bracknell	Herne Bay
Ribble Valley	Brighton & Hove	High Wycombe
Rochdale	Broadstairs	Horsham
Rossendale District	Buckingham,	Jersey
Royton	Winslow & District	Kent Probation
Sale	Burgess Hill	Service
Salford District	Camberley	Lancing & Sompting
South Lakeland	Canterbury	Leatherhead
South Ribble	Caterham &	Leigh Park
Southport	Warlingham	Lewes
Speke	Chiltern CAB Ltd	Littlehampton
St Helen's	(Amersham &	Lymington
Stockport	Chesham)	Maidenhead
Stretford	Chichester & District	Maidstone
Tameside District	Cosham	Malling
Toxteth	Cranbrook & District	Margate
Ulverston & North	Cranleigh & District	Medway District
Lonsdale	Crawley	Milton Keynes
Vale Royal	Crowborough	District
Walkden	Deal	New Milton & District
Wallasey	Didcot & District	Newport Isle of Wight
Walton	Diss, Thetford and	Newbury
Warrington District	District Citizen's	Oxford
West Kirby	Advice Bureau	Oxted
West Lancashire	Dorking	Paddock Wood
Whitehaven	East Grinstead	Petersfield
Wigan	Eastbourne	Portsmouth
Windermere	Eastleigh	Reading
Winsford	Edenbridge &	Reading Community
Withington	Westerham	WRU
Workington	Epsom & Ewell	Redhill, Reigate and
Worsley	Esher & District	Banstead
Wyre District	Fareham	Ringwood &
Wythenshawe	Farnborough	Fordingbridge
	Farnham	Romsey & District
SOUTH EAST	Faversham & District	Runnymede
REGION	Fleet & District	Seaford
Abingdon	Folkestone	Sevenoaks
Aldershot	(Shepway)	Shoreham &
Alton	Godalming	Southwick
Andover	Gosport	Sittingbourne & Isle
Ash	Gravesham	of Sheppey
Ashford	Guildford	Slough
Banbury & District	Hailsham	Southampton
Banstead	Haslemere	Staines
Basingstoke	Hastings & Rother	Sunbury &
Bexhill & Rother	Havant & District	Shepperton
Bicester	Haywards Heath	Spelthorne
Bishop's Waltham	Heathlands	Surrey Welfare
Bognor Regis	Henley & District	Rights Unit

Swanley and District	Monmouth	Frome & District
Tadley & District	Montgomeryshire	Gloucester & District
Thame	Neath	Gloucester MAS
Thanet	Newport	Ilfracombe
Tonbridge	New Town Advice	Kennet
Totton & District	Centre	Kerrier District
Tunbridge Wells	North Denbighshire	Liskeard
Uckfield	Pembroke Dock	Lydney
Walton, Weybridge &	Penarth	Marlborough
Hersham	Pontypridd	Mid Devon District
Waterlooville	Port Talbot	Mid Somerset
West Berkshire	Powys	Newquay
Whitehill & Bordon	Prestatyn	Newton Abbott
Winchester	Pwllheli	North Cornwall
West Oxfordshire	Risca	North Dorset
(Witney)	South Denbighshire	North East Somerset
Woking	Swansea	North Somerset
Wokingham	Torfaen	North Wiltshire
Worthing & District	Vale of Glamorgan	Okehampton
Yateley & District	Wrexham	Paignton
	Ynys Mon	Penwith
	Ystradgynlais	Plymouth City Centre
		Poole
WALES	SOUTH WEST	Purbeck
Abergavenny	REGION	Restormel
Aberystwyth	Barnstaple	Salisbury & District
Ammanford	Bath & District	Saltash
Bangor	Bideford	Sedgemoor
Bargoed & District	Bodmin	Sherborne
Blaenau Gwent	Bournemouth	South Gloucester
Bridgend	Bridport & District	South Hams
Caerphilly	Bristol	South Somerset
Caldicot	Brixham	St Austell
Cardiff	Bude, Holsworthy &	Stroud
Cardigan	District	Swindon & District
Carmarthen	Carrick District	Taunton & District
Chepstow	Camborne	Tavistock
Colwyn Bay	Caradon	Teignmouth
Conwy District	Cheltenham &	(Teignbridge)
Cowbridge	District	Tidworth
Cynon Valley	Christchurch	Torbay
Denbigh	Cirencester	Trowbridge
Flintshire	Dawlish	Truro
Gwynedd & De Ynys	Dorchester & District	West Wiltshire
Mon	East Dorset	Weymouth &
Haverfordwest	East Devon	Portland
Llandudno	Exeter	
Llanelli	Exmouth	
Llantwit Major	Falmouth	
Machynlleth	Forest of Dean	
Maesteg		
Merthyr Tydfil		

SCOTLAND

Aberdeen
Airdrie
Angus (Arbroath)
Angus (Forfar)
Angus (Montrose)
Bellshill
Caithness
Central Borders
CARF (Contact
Centre)
CARF
(Cowdenbeath)
CARF (Cupar)
CARF (Dunfermline)
CARF (Kirkcaldy)
CARF (Levenmouth)
Clackmannanshire
Clydebank
Clydesdale
Coatbridge
Cumbernauld
DAGCAS (Annan)
DAGCAS (Castle
Douglas)
DAGCAS (Dumfries)
DAGCAS (Stranraer)
Dalkeith
Denny & Dunipace
Dumbarton
Dundee
East Ayrshire
East Dunbartonshire
East Kilbride
East Renfrewshire
Edinburgh (Central)
Edinburgh
(Gorgie/Dalry)
Edinburgh (Leith)
Edinburgh
(Portobello)
Falkirk
Glasgow (Castlemilk)
Glasgow
(Drumchapel)
Glasgow (Greater
Pollok)
Glasgow (Maryhill)
Grangemouth and
Bo'ness

Haddington
Hamilton
Inverness
Lochaber
Moray
Motherwell and
Wishaw
NACAS (Arran)
Orkney
Peebles
Penicuik
Perth
Renfrewshire
Ross and Cromarty
Roxburgh
Rutherglen and
Cambuslang
Skye and Lochalsh
Western Isles (Barra)
West Lothian