



## **HM REVENUE & CUSTOMS**

---

Reducing error and fraud in Tax Credits

---

© Crown Copyright 2008

## Foreword by the Commissioner and Director General, Benefits and Credits

Child and Working Tax Credits were introduced in April 2003 as part of the Government's reforms of the tax and benefits system aimed at relieving child poverty and making work pay. They provide additional financial support to families with children and working people on low incomes. Tax credits provide support to around 6 million families and 10 million children.

Tax credits are designed to be flexible, with the level of financial support reflecting individual circumstances. The system is responsive to the changing needs of customers and their specific circumstances, for example, the birth of a new child or starting a new job.

When we published the first set of fraud and error statistics for tax credits in July 2006, covering the tax year 2003-04, we also published a document explaining what we were doing to tackle the issue. The figures show that HMRC has reduced the level of error favouring the customer from 9.2 per cent of all tax credit entitlement in 2003-04 to 7.6 per cent in 2006-07, and the levels of fraud from 0.6 per cent in 2003-04 to 0.2 per cent in 2006-07.

The Government has now set us a challenging target to reduce the level of error and fraud in the tax credits system to no more than 5% by March 2011. We have therefore strengthened our strategy to reduce further the level of customer and official error and tackle fraud.

**Michael Hanson**

**Commissioner and Director General, Benefits and Credits**

## Introduction

The Government is committed to reducing child poverty and providing incentives for work. Child Tax Credit (CTC) and Working Tax Credit (WTC) were introduced in April 2003 and replaced Working Families' Tax Credit, Disabled Person's Tax Credit and Children's Tax Credit, as well as some other forms of financial support for families with children. For the first time, WTC also extended in-work financial support to families without children or a disability.

Tax credits improve support for the family, tackle child poverty and help make work pay. They provide support to 20 million people including around 6 million families and 10 million children, targeting resources to provide:

- on-going support for families with children
- help with the payment of childcare expenses
- additional financial support for those on lower incomes
- support for those with disabilities who may be disadvantaged in gaining employment

Take up of tax credits is a significant success. Tax credits have played a key role in tackling child poverty. Since 1998-99, 600,000 children have been lifted out of relative poverty, compared to a doubling of child poverty in the previous 20 years. Tax credits also play a major role in moving people into work and helping people move up the employment ladder, ensuring that work pays over welfare.

The most up to date figures show that in 2006-07 the level of error (favouring the customer) was 7.6% and fraud was 0.2% of finalised entitlement.

These figures compare favourably with the levels found under Working Families Tax Credit (10-14%) and are also comparable with figures relating to social security benefits when the Government first collected data on a systematic basis. For example, in 1997-98 error and fraud was 9.2% for working age recipients of Income Support, and 13.2% for Job Seeker's Allowance.

The Government has set us a target of reducing the overall level of error and fraud in finalised awards to no more than 5% by March 2011. This is comparable with the latest measure of error and fraud in Income Support and Job Seeker's Allowance and will be equivalent to the reduction achieved by DWP, who reduced the level of error and fraud in the benefits system by 50% over an eight year period.

We have further strengthened our strategy for reducing error and fraud, which is based around four key elements:

1. Supporting customers so they get it right
2. Improving use of information to target compliance activity
3. Preventing fraud
4. Improving professionalism

This document sets out the size of the challenge, the progress made to date and explains our strengthened strategy.

## The size of the challenge

We measure the levels of error and fraud in the tax credit system each year by means of a stand-alone programme of work through which we randomly select and work through a proportion of cases at the end of the year to test the levels of error and fraud occurring. This is in addition to the cases we select for compliance action each year.

### Results for 2005-06 and 2006-07

	Central estimate of number (% of awards)		Central estimate of amount (% of entitlement)	
	2005-06	2006-07	2005-06	2006-07
Estimated error favouring the claimant	19.8	12.0	9.3	7.6
Estimated fraud favouring the claimant	0.4	0.2	0.3	0.2
Estimated error favouring HMRC	7.5	4.8	1.9	1.7

These figures include

- customer error
- HMRC error undetected at the end of the year
- fraud

They do not include organised fraud, which is likely to be detected before the end of the year. Estimates of organised fraud are calculated separately.

In 2006-07, we estimated the overall loss to HMRC as a result of error was 7.6% of finalised entitlement and fraud was 0.2%.

The statistics show that the vast majority of losses related to mistakes by the customer, either simple error arising from misunderstanding or failure to take reasonable care when making a claim. Our priority is therefore to reduce this.

## Progress made to date

This section describes our progress to date in tackling organised fraud, reducing official error and reducing customer error.

### **Reducing fraud**

Organised fraud typically involves external fraudsters using stolen identities to make claims, in some cases “hijacking” existing claims. We have put restrictions on the availability of claim forms and withdrawn the facility to claim over the internet in order to tighten up the security of on-line claims. Similarly, we have tightened the security questions we use to verify the identity of telephone callers in the light of specific risks associated with criminals hijacking live claims and diverting payments. We actively disrupt such frauds by preventing payments and monitor the accounts of previously stolen identities for further suspicious activity.

We are able to impose monetary penalties and, where appropriate, investigate with a view to prosecution.

We have worked with the Police, the Serious Organised Crime Agency, Local Authorities and other agencies to tackle organised crime. Working with financial institutions, we have also used anti-money laundering provisions to ensure that accounts suspected of receiving fraudulently claimed tax credits have been reported, frozen and the funds returned to us. In 2006-07, around £20 million was recovered in this way.

In 2006-07 we identified attempts to defraud the Tax Credits system of around £252 million. Of this, the vast majority – some £212 million, was detected before any money was paid out. Although we are stopping most organised fraud attempts before payment is made, we continue to be vigilant and look for new approaches and tools that can be used to combat these attacks.

### **Reducing levels of official error**

The level of official error as part of finalised entitlement was systematically measured for the first time as part of the 2005-06 random enquiry programme. We estimated that, for the population as a whole in 2006-07, £30m was in the customer’s favour. This is a comparatively small figure and does not accurately reflect the overall level of official error because it is likely that a large proportion of official error will have been corrected before awards are finalised. Overall, we are confident that levels of HMRC error are falling. We are working to reduce the errors we generate and are committed to continuously improving our effectiveness and accuracy.

- We have improved the accuracy of our processing of tax credits awards. In 2003-04 our accuracy level was 78.6%. In 2006-07 it was 96.85%.
- We have also put a great deal of effort into reducing the number of “system” errors in our IT systems. We are reviewing the current system problems which have the greatest impact on customers as part of an ongoing initiative to drive down errors in the computer system.
- Taking account of feedback from voluntary organisations, customers and staff we continue to improve guidance used by staff to make it both more accurate and easy to use.

## Reducing customer error

Over the past two years we have taken a number of positive steps to improve the quality of service we provide and deliver to our customers, and we believe these steps have already helped to reduce the number of mistakes people have been making. These have included:

- Understanding our customers

We have continued to develop a better understanding of our customers – in particular, the things they do and the areas where they have difficulties. We are using this understanding to tailor both our customer support and our compliance interventions to make them more effective.

We have introduced new services to ensure our customers have the help they need. For example, in 2007 we set up a process to help people who have separated from their partner re-claim tax credits over the telephone at the time they notify the separation (where appropriate). This service is helping around 150,000 customers who report a household breakdown each year, and taking claims over the phone, should help to reduce errors.

- Working with intermediaries

We have worked with intermediaries in the voluntary and community sectors to help to improve awareness and understanding of tax credits.

- Advertising campaigns

We have focused our advertising campaigns on influencing the behaviour of existing customers, recognising that the tax credit system supports around 6 million households. So, for example, we have directed our campaigns towards encouraging our customers to report changes in their circumstances and renew their awards promptly.

- Improving our guidance

We have made our forms and guidance easier to understand, for example, giving customers a clearer summary of what they will be paid and how this amount has been calculated. This helps to improve customer understanding of how tax credits works and the importance of ensuring their details are correct and up to date. An increasing number of our customers tell us that they find the award notice easy to understand.

- Risk assessment

We have improved and enhanced our assessment of risk, making better use of information held by us, other Government Departments and third parties to target our compliance activity. This has helped us to support honest customers better, and ensured that the checks we carry out to identify and tackle non-compliant behaviour have been well focused.

- Checking new claims

We have been making extensive checks on new claims at the point of receipt to ensure that we are targeting the highest risk claims before an award is even made. Our activities have ranged from simple interventions that focus on helping the customer to correct minor errors that could lead to an overpayment, through to a full examination of their claim.

## Strengthening our strategy

We have made good progress over the last two years tackling official error and organised fraud. We are making the service we provide more responsive to customer's needs as their circumstances change. We are improving our customer understanding and helping customers to make fewer errors whilst encouraging them to claim their entitlement.

However, there is more to do if we are to achieve our target of reducing error and fraud to no more than 5% of entitlement by March 2011.

We have strengthened our strategy to meet this target, concentrating on four key themes.

- Continued development of the **support** we give to customers, tailored to their individual needs, including helping to reduce the number of mistakes they make.
- Improve **use of information to target compliance activity** so that we can better handle and process information about risks of non-compliance and tailor our responses accordingly.
- Continued **prevention of fraud** so that we can stop losses before they happen and ensure the tax credits system is robust against criminal attacks.
- Improved levels of **professionalism** so that our work is structured to make the best use of our resources and our staff are deployed in stretching, well-designed jobs with the necessary skills, tools and management support.

### Supporting our customers to get it right first time

Supporting our customers to get it right is fundamental to delivering a reduction in error and fraud. The Tax Credit Transformation Programme started in November 2006 with a key aim of enabling HMRC to tailor its services and interventions to customer needs – providing more help and support for customers who are at most risk of getting it wrong. Understanding our customers will enable us to identify, for example, those who are more likely to have lower literacy and numeracy levels and lower financial capability. This group of customers also tends to see more variation in their level of income and domestic circumstances. Based on this understanding we can offer these customers more assistance when they need it.

Some examples of the areas being looked at in the Programme are set out below.

#### a) Assistance for customers at the point of claim

We know that different customers need different types of help when claiming. Through the Programme, different types of support will be offered to our customers depending on their needs and circumstances. This will range from simple advice when a customer requests a claim form to intensive help over the phone or face to face. Examples of the types of assistance we are implementing include:

- When a customer contacts us for a claim form, we will make them aware of common errors made by people when they complete the form. This will help customers avoid making mistakes from the beginning.
- For customers with complex personal circumstances who might need more support through the claims process, we will offer to go through key parts of the claim form with them over the telephone, particularly around income and childcare.

#### b) Ensuring that changes of circumstances are reported on time

Tax credits are flexible, providing support to people as their circumstances change. However, customers are often not aware that they need to inform us of changes and that, by not doing so, they may not receive the correct payments.

Some customers contact us to report one change in their circumstances but may not report other changes because they don't think they need to. Following two successful pilots in 2007, we will implement a service from September 2008 to ask extra questions when people call us, to seek information from customers in key areas of their claim (income, childcare and children) in order to keep their award up to date. By taking this proactive approach, we will help customers to report all relevant changes so that they receive the correct amount and understand what they need to do in future.

Some customers do not contact us at all. In these cases, we will proactively contact them and offer a 'health check' of their award to make sure it is up to date – this will, again, minimise any overpayments and reduce the risk of error.

Where we have given extra help to a customer at the time of their claim we will continue to offer support. After a period of time we will contact them again to make sure that they understand what they need to do and to provide advice on any problems that they have encountered.

All these new services will help ensure that we have up to date information about the customer's circumstances and help them cope with some of the more complex aspects of tax credits. For instance, we can help them recalculate childcare costs when a child moves into full time education or ask them whether the hours they work have changed when they report a fall in income.

#### c) Supporting customers through the renewals process

The final element of the tax credits cycle is the annual process of finalising the previous year's award and renewing for the current year. Failure to renew on time often results in overpayments. Each year a significant number of customers do not renew on time. The Programme is introducing a number of initiatives to help our more vulnerable customers to renew on time:

- during the renewals window, proactively contacting customers most at risk of being overpaid if they do not renew promptly, to:
  - remind them to renew;
  - explain the consequences of not renewing early; and
  - renew them if they have the material on hand to renew.

- after the renewals deadline we will phone customers who have failed to renew in time and are still eligible to receive tax credits to help them to get back into payment quicker.

#### d) Services provided throughout the tax credits cycle

We will make better use of the information we already hold by ensuring that customers who receive tax credits and Child Benefit only have to report certain key information (such as a child leaving school or the birth of a new child) to HMRC once. In addition we are looking at whether we can use tax data that a customer has started a new job to help customers keep their awards up to date.

We are also testing new ways of keeping in contact with tax credit customers. We are piloting different ways of delivering advice and services through Children's Centres. These provide a one-stop shop for families with children under five, bringing together childcare, early education, healthcare, family support and Jobcentre Plus services and represent an opportunity to keep in touch with a key group of tax credit customers.

We will also pilot new services to engage with tax credit customers and offer them the opportunity to take advantage of a series of services designed to help them avoid end-year adjustments leading to overpayments. Work is underway to identify those individuals, including both new and existing tax credit customers, who will benefit most from these services, and how best to engage with them.

#### e) Improving our communications

Through the Transformation Programme we are developing clearer and better targeted communications products and marketing campaigns to help customers understand what they have to do, when they have to do it and what services we can offer to help them. These products will again focus on the three key stages of, making a claim, reporting a change of circumstances and renewing awards each year.

Examples of some of the communication products include:

- We have launched 'Do you qualify?' - an on-line tool to enable potential customers to see in a few simple steps whether they are likely to be eligible for tax credits at all;
- We are developing shorter, more focused guidance to help customers to complete the claim form correctly; highlighting common mistakes and telling them where to get further assistance;
- We plan to issue targeted reminders at specific points in the year to prompt customers to report specific events which may result in change of circumstances.

The improvements being developed through the Transformation Programme will make a key contribution towards helping to support the customer and reduce the numbers of mistakes they make by providing tailored services based on customer understanding.

## **Use of information to target compliance activity**

Alongside more tailored support to our customers being introduced through the Transformation Programme we are also embedding this principle into mainstream compliance. Compliance resources will be deployed on the basis of a deeper understanding of likely areas of error and fraud across the customer base.. This will enable compliance activity to influence a wider range of customers, aimed at ensuring that the resulting behavioural changes are sustained over time.

### Improving our risk processes

Improving our management of risk is at the heart of our compliance strategy. Automated risk assessment tools identify cases for review by our compliance specialists are built into our processes already. We already undertake extensive checks on new claims and concentrate on areas of work where we know there are risks that errors are being made. We have a range of interventions tailored to suit the specific risks identified. We continue to strengthen our approach to the assessment of potential risk and to adjust our responses accordingly.

We have developed our understanding of the nature and extent of the risks we are dealing with. We will be using this improved understanding to focus and direct our front line activity to ensure the best result for customers and the most efficient use of our resources.

We also plan to extend the current process of checking certain high risk claims before they are put onto the system to be assessed by introducing further up front risk assessment and risk assessment immediately after the first payment and then conduct in-year checks, rather than waiting until a claim is finalised. This will not only correct the immediate error, but also provide education and advice which will then help avoid errors in the future. These interventions will also help with the earlier identification of potential fraud.

We can better manage risk of error and fraud through greater understanding of our customers. We know there are some customers who find some areas of the claim difficult to understand, such as disability, definition of working hours and calculating childcare. We are planning to take a more educative approach to help these customers. Where we have investigated a claim in one year, we are currently considering whether to follow up during the following year to help support the customer.

### Working with other agencies

We currently work with Jobcentre Plus to 'Fast Track' awards for customers on benefits that either move into work or have a baby. Working together we have introduced a number of measures to improve the Fast Track Process. For example:

- changes of circumstances for existing benefit/tax credits customers are now processed more quickly through the Department of Work and Pensions priority helpline;
- providing Jobcentre Plus with 'top tips' to enable them to reduce the risk of incomplete information or errors that delay payment; and
- communicating joint objectives to staff by a series of memos.

This work has enabled us to improve the timeliness of payment to customers. In addition to this, Jobcentre Plus can quickly tell us about changes of circumstances while the customer is on their premises, reducing error. We have seen an increase in the number of changes of circumstances processed automatically from 40% to around 90%. We are also working more effectively with and through intermediaries and other Government departments and agencies, sharing intelligence on organised fraud.

### Working with intermediaries

We are seeking to develop national and regional networks of intermediaries, focusing on customer groups and geographic areas where our risk analysis suggests there is a high risk of error. At the national level this could include working with national employers, and locally we will identify where customers are turning for help and advice and build appropriate local networks. We will also look to participate in local initiatives or events that reach our customer groups.

### **Prevention of fraud**

We continue to devote substantial resources to tackle fraud. By putting in place an effective range of sanctions we will raise the awareness amongst those inclined towards fraud that they are likely to get caught.

We undertake selective criminal investigations to detect and deter fraudsters and maintain the integrity of the tax credits system. Other cases will be subject to face to face interventions and possible penalties. For less serious cases of non-compliance we will continue to develop a range of educative approaches to change the behaviour of those who are confused about their obligations.

### Identifying new types of fraud

The ability to identify new types of fraud is crucial if we are to have a sustained effect on criminal attacks. We will build on our current successes in combating organised criminal attacks - further improving our risk analysis, designing out opportunities for fraud, policing entry to the system, sharing intelligence effectively with others and tackling criminal finances.

For example, we are examining the potential for using new, risk-based technology in our Contact Centres and compliance work to identify fraudsters. We are exploring opportunities for improving our document verification processes – using industry standards software to help identify forged or stolen documents.

### Identity Authentication Service

We will soon improve our ability to tackle the risk of organised fraud involving the theft of customers' identities through the introduction of a robust regime for verifying identity. This is the Identity Authentication Service (IDAS) and it will help us verify the identity of our customers when they contact us via telephone.

Once we are satisfied that IDAS provides the security we expect it to, we will then also be in a position to re-open the Online Service. This will enable customers to securely register, enrol and transact with us via the Internet.

Meanwhile, we have already developed more robust defences in our Contact Centres, particularly against those who attempt to hijack a genuine customer's identity. We have compliance staff based in all our Contact Centres which means that we are able to react quickly to new attempts at fraud.

#### Cross-departmental working

We already work across the whole department and Government to identify criminal attacks on the system. In particular, we work with the Department for Work and Pensions to investigate organised tax credit fraud and form a Joint Instant Response Team within 48 hours to efficiently act upon intelligence in respect of serious fraud.

#### Raising fraud awareness

We now have compliance specialists based in all our Contact Centres and they help to raise fraud awareness more widely among our staff, and to provide specialist support. Building on this we are now developing a fraud awareness programme to enhance further the skills and knowledge of all contact centre staff.

### **Professionalism**

#### Structural changes

In response to the Capability Review (an independent assessment of HMRC's ability to meet both the challenges it faces today and those it will face in the future), HMRC have improved accountabilities and have now appointed a single Director General with specific accountability for delivering our Departmental Strategic Objectives in relation to Tax Credits and Child Benefit. This is a first step towards clarifying accountability throughout HMRC by simplifying the organisation's structure, making it clearer who is responsible for what and shortening the lines of responsibility.

#### Investing in Leadership

We are investing in operational leadership and engaging our front-line staff more closely with our overall improvement work and problem resolution. In the Tax Credit Office, this has focused on delivering the sort of performance management and continuous improvement skills that managers need.

#### Developing our people

Our compliance staff already have highly developed skills, and work is underway to raise awareness of compliance issues among staff in processing offices and Contact Centres. However, we have identified a need to enhance and better focus the training given to compliance staff and ensure continued professional development. The introduction of new, centralised units combined with smaller, geographically dispersed teams will enable effective and efficient delivery of our compliance strategy with increased flexibility.

## Conclusion

Error and fraud has reduced since we first measured this for tax credits in July 2006. We now have 4 years of data from the random enquiry programme that has allowed us to perform a thorough analysis of risk. This, along with the understanding of customers we have gained from our work on the Tax Credit Transformation Programme, has enabled us to plan and adapt our strategy for reducing error and fraud. The Government has set us a target to reduce this to no more than 5% by March 2011 as measured by the 2010-11 random enquiry programme, and we are committed to achieving that.

We have therefore strengthened our strategy to tackle error and fraud. We will ensure that customers receive the help they require so that their tax credit claim is correct, by introducing new services which are designed to meet the needs of customers tailored to their circumstances. We will continue our robust approach to those who seek to abuse the system. This coupled with compliance interventions, will enable us to tackle fraud, correct incorrect claims and educate and support our customers to prevent errors in the future.

We are committed to reducing error and fraud and delivering the target of reducing error and fraud to 5% by 2011.