



HM REVENUE AND CUSTOMS

KAI: Benefits & Credits

Child and Working Tax Credits

Error and Fraud Statistics

2011-12

Estimates of error and fraud in Tax Credits 2011-12

Introduction

1. Child Tax Credit (CTC) and Working Tax Credit (WTC) were introduced in April 2003. They are a flexible system of financial support designed to deliver support as and when a family needs it, tailored to their specific circumstances. They are part of wider government policy to provide support to parents returning to work, reduce child poverty and increase financial support for all families. The flexibility of the design of the system means that as families' circumstances change, so (daily) entitlement to tax credits changes. This means tax credits can respond quickly to families' changing circumstances, providing support to those that need it most. Tax credits are based on household circumstances and can be claimed jointly by members of a couple, or by singles. Entitlement is based on the following factors: age, income, hours worked, number and age of children, childcare costs and disabilities. For further information on who can claim tax credits please refer to the HM Revenue & Customs (HMRC) website.
2. This report presents results from the tax credits Error & Fraud Analytical Programme (EFAP), which is designed to measure error and fraud across the tax credits population. This publication will be of particular interest to the National Audit Office (as part of their overall review of HMRC's accounts), academics and think-tanks and operationally within HMRC.
3. For 2011-12 this exercise took a stratified random sample of cases which were selected to be representative of the tax credit population. Around 3,780 cases were then taken up for examination by claimant compliance officers who worked the cases as they would for any other enquiry. The figures in this publication are based on around 3,420 of these enquiries that had been completed by the time this publication was produced. As such all estimates in this report may be subject to change as more enquiries are completed. The results from these sample cases have been scaled up to population numbers to estimate the overall level of error and fraud in the tax credit system. We will re-publish the estimates if the central estimate rate of error and fraud favouring the claimant changes by +/- 0.2 percentage points as agreed with the National Audit Office as part of a review of the processes for measuring error and fraud.
4. Because of the size and diversity of the claimant population, and the possible variation in compliance risk, the sample has been stratified. This is so that we can measure the level of compliance for various claimant groups, as well as for claimants as a whole. More details about the sampling methodology used can be found in Annex A.
5. The EFAP helps to provide an understanding of the overall level of error within the Tax Credit system. The level of error and fraud by monetary value was 10-14%

under Working Families Tax Credit, 9.2% for Income Support and 13.2% for Job Seekers Allowance in 1997-98 when data was first collected on a systematic basis. In 2011-12, the latest year for which statistics are available, the level of error and fraud was around 7.3% of finalised tax credit entitlement. Headline results from previous exercises are shown in Annex A.

Section 1: Likely levels of error and fraud

6. The details presented in the following tables are based on a sample of cases and hence there are margins of error associated with these estimates. Therefore, Tables 1 to 4 also illustrate the 95% confidence intervals associated with these central estimates – and note that the estimates presented in the rest of the tables are the central estimates.

Table 1: total error and fraud as a proportion of finalised entitlement, 2011-12

| | Error and fraud as a percentage of finalised entitlement | | |
|---|--|-------------------------|-------------|
| | Lower bound | Central estimate | Upper bound |
| <i>Estimated error & fraud favouring the claimant</i> | 6.6 | 7.3 | 7.9 |
| <i>Estimated error favouring HMRC</i> | 0.6 | 0.9 | 1.2 |

7. Table 1 shows for 2011-12 the proportion of finalised tax credit entitlement that was accounted for by error and fraud.
8. Error and fraud favouring the claimant refers to cases where the claimant has been found to be non-compliant in a way that has led HMRC to pay them more tax credits than they were entitled to for the year – i.e. there was a monetary gain for the claimant and hence a monetary loss for HMRC. Error and fraud favouring HMRC refers to cases where the claimant has been found to be non-compliant in a way that has led HMRC to pay them less tax credits than they were entitled to for the year – i.e. there was a monetary gain for HMRC and hence a monetary loss for the claimant.

Table 2: overall level of error and fraud, 2011-12

| | Number ('000) | | | Amount (£m) | | |
|--|---------------|------------------|-------------|-------------|------------------|-------------|
| | Lower bound | Central estimate | Upper bound | Lower bound | Central estimate | Upper bound |
| Estimated error and fraud favouring the claimant | 1,270 | 1,360 | 1,460 | 1,910 | 2,090 | 2,270 |
| Estimated error favouring HMRC | 430 | 490 | 550 | 170 | 260 | 360 |

9. Table 2 shows central estimates and their associated 95% confidence intervals for the overall levels of error and fraud for 2011-12.

Table 3: error and fraud favouring the claimant as a proportion of finalised entitlement, 2011-12

| | Error and fraud as a percentage of finalised entitlement | | |
|---|--|-------------------------|-------------|
| | Lower bound | Central estimate | Upper bound |
| <i>Estimated error favouring the claimant</i> | 3.8 | 4.2 | 4.6 |
| <i>Estimated fraud favouring the claimant</i> | 2.6 | 3.0 | 3.5 |

10. Table 3 shows for 2011-12 the proportion of finalised tax credit entitlement that was accounted for by error in the claimant's favour and the proportion that was accounted for by fraud in the claimant's favour. Due to the small number of sample cases in the Error and Fraud Analytical Programme classified as 'fraud' separate breakdowns of the components split by error and fraud are not available. The categorisation between error and fraud is not comparable with years prior to 2008-09. A new penalty regime and associated guidance was introduced in compliance on 6 April 2008. The result of this was that the way fraud was categorised changed, however, in 2007-08 only part of the impact of this was captured in the published figures. The classification of fraud used here was fully aligned with the new penalty regime from 2008-09 onwards and this has resulted in a larger proportion of error and fraud being classified as fraud.

Table 4: level of error and fraud favouring the claimant, 2011-12

| | Number ('000) | | | Amount (£m) | | |
|--|---------------|------------------|-------------|-------------|------------------|-------------|
| | Lower bound | Central estimate | Upper bound | Lower bound | Central estimate | Upper bound |
| Estimated error favouring the claimant | 1,000 | 1,090 | 1,170 | 1,100 | 1,220 | 1,330 |
| Estimated fraud favouring the claimant | 230 | 280 | 320 | 740 | 870 | 1010 |

11. Table 4 shows the central estimates and their associated 95% confidence intervals split by the levels of error and fraud in the claimant's favour.

12. For the central estimate, the level of error can be further broken down between customer error and HMRC error. This is set out in table 5 below.

Table 5 – overall level of error split between claimant error and HMRC error - central estimates, 2011-12

| | Claimant error | | HMRC error | |
|---|-----------------------|--------------|-------------------|--------------|
| | Numbers ('000) | Amounts (£m) | Numbers ('000) | Amounts (£m) |
| <i>Estimated error favouring the claimant</i> | 1,070 | 1,210 | 20 | 10 |
| <i>Estimated error favouring HMRC</i> | 460 | 240 | 30 | 20 |

Table 6 - breakdown of error and fraud by type of tax credit award - central estimates, 2011-12¹

| Estimated error and fraud favouring the claimant | Numbers ('000) | Amounts (£m) |
|---|----------------|--------------|
| Nil award | - | - |
| Out of work | 160 | 300 |
| In work, children, more than family element | 790 | 1,430 |
| In work, children, family element or less | 190 | 70 |
| WTC only | 210 | 280 |
| Total | 1,360 | 2,090 |
| Estimated error favouring HMRC | | |
| Nil award | 20 | 10 |
| Out of work | 20 | 10 |
| In work, children, more than family element | 350 | 160 |
| In work, children, family element or less | 50 | 60 |
| WTC only | 50 | 20 |
| Total | 490 | 260 |

¹ To compare these figures to those presented in Table 3 of the 2003-04 publication and Table 4 of the 2004-05 publication then 'In work, children, family element or less' is equivalent to 'Flat rate' and the summation of 'Out of work', 'In work, children, more than family element' and 'WTC only' is equivalent to 'Others'.

Table 7 - distribution of error and fraud by its value - central estimates, 2011-12

| Value of error and fraud | Estimated error and fraud favouring the claimant | | Estimated error favouring HMRC | |
|--------------------------|--|-------------|--------------------------------|-------------|
| | Number ('000) | Amount (£m) | Number ('000) | Amount (£m) |
| Less than £100 | 180 | 10 | 190 | 10 |
| £100 to £499 | 310 | 95 | 160 | 45 |
| £500 to £999 | 300 | 225 | 80 | 60 |
| £1,000 or more | 570 | 1,760 | 60 | 150 |
| Total | 1,360 | 2,090 | 490 | 260 |

Table 8 - distribution of error and fraud by value of finalised award - central estimates, 2011-12

| Value of award | Estimated error and fraud favouring the claimant | | Estimated error favouring HMRC | |
|------------------|--|-------------|--------------------------------|-------------|
| | Number ('000) | Amount (£m) | Number ('000) | Amount (£m) |
| £0 | - | - | - | - |
| Under £1,000 | 260 | 100 | 105 | 90 |
| £1,000 to £1,999 | 160 | 145 | 60 | 25 |
| £2,000 to £2,999 | 155 | 235 | 60 | 15 |
| £3,000 to £3,999 | 130 | 200 | 40 | 20 |
| £4,000 to £4,999 | 95 | 200 | 25 | 5 |
| £5,000 to £5,999 | 105 | 165 | 30 | 20 |
| £6,000 to £6,999 | 90 | 205 | 35 | 20 |
| £7,000 and over | 360 | 835 | 140 | 65 |
| Total | 1,360 | 2,090 | 490 | 260 |

13. Note that the value of the award shown in Table 8 is the value of the finalised award when the EFAP sample was drawn.

Table 9 - reasons for error and fraud - central estimates, 2011-12

| Reason | Estimated error and fraud favouring the claimant | | Estimated error favouring HMRC | |
|--------------------|--|-------------|--------------------------------|-------------|
| | Number ('000) | Amount (£m) | Number ('000) | Amount (£m) |
| Income | 600 | 395 | 435 | 220 |
| Undeclared Partner | 240 | 710 | - | - |
| Childcare costs | 190 | 185 | * | * |
| Children | 240 | 325 | * | * |
| Work and hours | 285 | 410 | 65 | 25 |
| Disability | 45 | 60 | 5 | 5 |
| Total | 1,600 | 2,090 | 530 | 260 |

* These figures have not been published as a result of small sample sizes.

14. Note that in Table 9 some claimants will have more than one reason for adjustment so the numbers will not sum to the total number of awards presented in the other tables.

Annex A

The 2011-12 Tax Credits Error and Fraud Analytical Programme (EFAP): Methodological and Technical Details

Introduction

1. The tax credits system is designed to respond to changes in income and circumstances as they happen. In 2011-12, a family's award was initially based on their circumstances (e.g. number of children, any disabilities, etc.) and income as held by HMRC on their 2010-11 award at April 2011.² Once their 2010-11 award had been finalised then their 2011-12 award would be based on their finalised 2010-11 income; although, at any time they could provide an estimate for their current year income. At the end of 2011-12 a number of claimants are auto renewed. These claimants are only required to contact HMRC if they have had a change in income and are required to tell HMRC what their final income was for the year by 31 July 2012. However, some recipients who had only been able to provide an estimate by this date were given until 31 January 2013 to provide their final 2011-12 incomes.
2. The 2011-12 exercise could not start until recipients had provided HMRC with details of their final 2011-12 incomes, which meant that compliance officers were unable to start work on some cases until after 31 January 2013 (as an enquiry can only be opened once the award is finalised).

Error and Fraud

3. When Claimant Compliance Officers identified non-compliance, they were required to indicate whether they believed it was due to genuine error or fraud. To be classified as fraud, a caseworker needs to have found evidence that the claimant deliberately set out to misrepresent their circumstances to get money to which they are not entitled (e.g. claiming for a child that does not exist). Error covers instances where there is no evidence of the claimant deliberately trying to deceive HMRC. It covers a range of situations, including cases where a claimant inadvertently over-claims because they simply provided HMRC with the wrong information. It could also cover a situation where the correct information has been provided but this information has been incorrectly processed by HMRC.
4. The split between error and fraud in this publication has changed due to the new penalty regime and associated guidance introduced in compliance on 6 April 2008. This is the fourth year that the results fully reflect the way that the new penalty regime distinguishes between error and fraud and therefore they are not comparable

² Unless 2011-12 is their first year of tax credit receipt in which case it will be based on their circumstances at the time of application and their 2010-11 income.

to years prior to 2008/09. This has increased the amount of error and fraud classified as fraud.

5. Estimates of official error were published for the first time in 2006-07. As part of the working of each case compliance officers were asked not only to classify whether or not a case that was found to be incorrect was due to either error or fraud, but also whether or not the error was due to HMRC. HMRC error figures were not included in the 2007-08, 2008-09, 2010-11 and 2011-12 publications due to the small number of cases in those samples found to be affected.
6. For cases where error or fraud have been identified the Claimant Compliance Officer also has to identify the causes of the error or fraud - and the monetary consequence of this - the adjustment categories are shown in Table 9. These categorise whether or not the income reported at finalisation is under or over-stated, likewise with childcare costs. Similarly, whether or not there is a partner in the household whose income has not been declared, whether or not a child claimed for is still in full time education and being cared for by the claimant, whether or not the adults in the claim are working and if so the number of hours that they are working and whether or not the adults and children in the claim are disabled or severely disabled³.
7. Due to the nature of organised fraud and HMRC compliance procedures the vast majority of organised fraud claims are stopped quickly and awards in payment are terminated. This means that organised fraud is more likely to be detected as overpayments rather than in the EFAP. Any overpayments that are not remitted during the year will be included in the annual National Statistics publication on under and overpayments.

Sampling

8. The sample for the 2011-12 EFAP is constructed from 4 strata of claimants; these strata, together with the sample sizes, are shown below:

Table A1: Sample Strata and Sample Sizes

| Stratum | Sample size |
|----------------|--------------------|
| Nil awards | 75 |
| Flat rate | 250 |
| WTC only | 400 |
| Others | 3,275 |
| Overall | 4,000 |

³ This last category also covers the small number of cases where the claimant or their partner were incorrectly reporting that they were in receipt of IS/JSA (passporting them to maximum CTC with no tapering) or the 50+ return to work element.

9. The sample was stratified in this way to ensure that an appropriate number of both Nil, Other and WTC only awards were included in the sample. If a purely random sample had been used this would have consisted of a high number of Nil and Flat rate awards which show relatively low rates of non compliance, thus reducing the accuracy of the results of the EFAP. The use of a stratified sample allows for the levels of error and fraud in each stratum to be estimated more accurately by ensuring the number of cases in each strata is representative of the likelihood of fraud and error occurring in that strata of the population.
10. An individual award can fall into a number of different strata during the year depending on the circumstances of the household at a given point in time, for example a couple could initially be receiving WTC only and then half way through the year have their first child thus moving them to our other strata. In fact there are ten possible categories (which we aggregate into our four strata) that a household in award could find themselves in at a given point during the year depending on their circumstances and income. When an award moves between these categories we say that a new entitlement sub-period has been created. It is not possible to aggregate these sub-periods into one category that would give the household an overall status for the year, therefore we allocate them based on the entitlement sub-period that they have spent the most time in during that year.
11. It is important to note that our sample base is awards and not families – these two differ as a family can have a number of awards during a year. Take the following example, initially a lone parent family is in award then a new household is formed when a partner moves in and later in the year the partner moves out (the household breaks down) and they become a lone parent again, so in total they have had three separate awards during the year. We follow awards as this is the unit that the tax credit system is based around and hence is most suitable for constructing a representative sample from.
12. The sample base contains all 2011-12 awards present on the HMRC tax credit system at the end of the first week of August 2012. An award may last for a period of anywhere between one day and the whole year.
13. The samples for each stratum were selected at random and were picked using a set of randomly generated numbers.

Sampling errors around the estimates

14. Estimates in the tables are rounded to the nearest £10m/10,000 in tables 2 and 4 to 6 and for all the overall totals in the other tables whilst the breakdowns in the other tables are rounded to the nearest £5m/5,000. The estimates presented are the central estimates derived from the sample taking account of the methodological approach set out below. Since these estimates are based on a sample they are

subject to sampling errors. These margins of error have been expressed by calculating a 95% confidence interval around the estimates. These have been calculated and are shown in Tables 1 to 4.

Methodology

15. This next section sets out a number of different methodological issues - such as how we process the data, how cases in the sample have been scaled up to represent population estimates, how certain cases have been treated, etc.

Processing

16. The underlying data is recorded by the compliance officers who carried out the enquiries; it then undergoes a number of steps where it is checked and processed before it is used to calculate the figures in this publication.

17. The final data used is created by cross checking the information held in our compliance management information system against that held in the main tax credit computer system and against information recorded about the case by the compliance officer who worked it. Where a lone parent is found to have an undisclosed partner we offset the entitlement that they would have had under their (notional) joint award against the amount that was paid out incorrectly in the single-person award and the remainder is what we classify as error/fraud in this publication.

18. Each award has a number of entitlement sub-periods⁴ and it is clear that some of these sub-periods cannot be associated with certain types of error/fraud that are recorded, for example if 25% of an award's time is spent in a WTC only sub-period and 75% of its time in sub-periods relating to CTC then a claimant favour error/fraud relating to a child could only have occurred in the latter 75% of the award. We therefore allocate the error to the sub-periods that it could be associated with, so in the earlier example the child error would be allocated to the 75% of the award spent in sub-periods relating to CTC. HMRC favour error has been reallocated between sub-periods based on the proportion of that award spent in that sub-period.

Projections

19. Although the figures in this publication are based on the 3,416 cases which had been settled, there were still 367 cases which had been opened but not completed in time to be included. A projection has been made to cover the estimated additional amount of extra error/fraud these cases will provide.

20. It is assumed in this analysis that these incomplete cases exhibit the same characteristics, on average, to those that had been settled most recently and

⁴ See paragraph 10 for an explanation of entitlement sub-periods.

assumed that the cases left to work to the end will on average exhibit this average level of settlements and level of non-compliance. Where there is only a small number of sample cases for recently settled cases the average level over a longer time period is used. We will re-visit this projection once more cases have been completed and re-publish the estimates if the headline rate of error and fraud favouring the claimant changes by more than +/- 0.2 percentage points.

Grossing

21. The sample results of the cases that have been worked to completion plus the projected results from the cases still being worked have been grossed to reflect population estimates. Differential grossing factors have been applied depending on the value of the finalised award and the characteristics of the claimant during the year. The process by which the grossing was carried out differs from that used in 2003-04 and 2004-05 as a new improved methodology was introduced from 2005-06 onwards. Although the changes set out below introduce a discontinuity into any time series comparisons this is offset by the increased accuracy that the method provides for this and future years. For reference published figures for prior years are contained in the table over the page.

Table A2: Published Error and Fraud rates for Prior Years

| Estimate | Year of EFAP | Error and Fraud as a Percentage of Finalised Entitlement | | |
|--|--------------|--|-------------------------|-------------|
| | | Lower bound | Central estimate | Upper bound |
| Estimated error and fraud favouring the claimant | 2003-04 | 8.8 | 9.7 | 10.6 |
| | 2004-05 | 7.3 | 8.2 | 9.1 |
| | 2005-06 | 8.5 | 9.6 | 10.6 |
| | 2006-07 | 7.2 | 7.8 | 8.4 |
| | 2007-08 | 8.3 | 9.0 | 9.7 |
| | 2008-09 | 8.3 | 8.9 | 9.6 |
| | 2009-10 | 7.0 | 7.8 | 8.6 |
| | 2010-11 | 7.5 | 8.1 | 8.8 |
| Estimated error and fraud favouring HMRC | 2003-04 | 1.6 | 1.9 | 2.3 |
| | 2004-05 | 1.4 | 1.9 | 2.4 |
| | 2005-06 | 1.4 | 1.9 | 2.4 |
| | 2006-07 | 1.3 | 1.7 | 2.1 |
| | 2007-08 | 1.0 | 1.3 | 1.6 |
| | 2008-09 | 0.8 | 1.1 | 1.3 |
| | 2009-10 | 0.9 | 1.4 | 2.0 |
| | 2010-11 | 0.6 | 0.8 | 1.0 |

22. The sample frame used from 2005-06 onwards provided more information than that used in previous years – giving us information on all the entitlement sub-periods⁵ that an award had had during the year compared to previously having just the last of the year. Therefore since 2005-06 we gross our sample results to the total of entitlement sub-periods for the population over the whole year rather than to the single entitlement sub-period present at the end of the year.

23. We also now gross up to the position of the award on each tax credit profile rather than to each strata that the award falls into (the four strata are an amalgamation of the 10 different profile positions) which gives us increased accuracy over groups with potentially differing rates of error and fraud.

24. The final change was a move from grossing to the total number of awards as the control population to instead using the total amount of entitlement.

Exclusions

25. The figures underlying this report are based on 3,416 cases examined by claimant compliance officers supplemented by the projections for the 367 cases that were opened but have not yet been closed. In the analysis presented in this report account has been taken of:

cases that are not taken up for enquiry - in some cases, for example if the claimant or their children have died, an enquiry is not taken up, these cases have been excluded from the results - implicitly assuming that if they had been worked they would have the same result, on average, to the cases that have been successfully completed.

Contact point

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⁵ See paragraph 10 for an explanation of entitlement sub-periods.