

Report by the Comptroller and Auditor General to the House of Commons

Part One: Key Features of the Client Funds Account

Following the abolition of the Child Maintenance and Enforcement Commission on 31 July 2012, operational responsibility for the statutory child maintenance schemes in Great Britain has passed to the Department for Work and Pensions (DWP). The Client Funds Account records the receipts of child maintenance from non-resident parents; payments to parents with care and the Secretary of State; and a statement of cash balances held at the year end, this being the value of maintenance received which has not yet been paid out. I have issued an unqualified audit opinion on whether these receipts and payments are properly presented, and a qualified audit opinion on regularity. Further details of my reasons for the qualification are set out below.

The Account also includes an arrears balance (Note 6), which is the amount of child maintenance outstanding and owed by the non-resident parent to either the parent with care or to the Secretary of State. Note 6 also includes an analysis of the collectability of the outstanding arrears. I have concluded that this note does not give a true and fair view of the arrears outstanding, or its collectability, as at 31 March 2013 for the reasons set out in my report below.

These modifications to my audit opinions are longstanding and reflect significant and ongoing problems in the accurate calculation of maintenance and with the underlying IT systems since statutory child maintenance schemes were first introduced. I have reported on these issues previously.

Part Two: Irregular Receipts and Payments

Audit Opinion

As the independent external auditor, I am required to give an opinion on whether, in all material respects, the Client Funds Account properly presents the receipts and payments for the year ended 31 March 2013 and whether these transactions have been applied to the purposes intended by Parliament and conform to the authorities which govern them (the 'regularity' opinion).

The Department is required to adhere to specific legislative requirements when determining maintenance assessments and has no authority to exercise latitude. When an assessment is made that is not in accordance with these legislative requirements, the receipt and associated payment are incorrect and not in accordance with legislation. Whilst the account properly presents the amounts of child maintenance received and paid in the year, I have qualified my regularity audit opinion on the grounds of material errors in the calculations of maintenance assessments; these assessments are not in accordance with the legislation and therefore are not in line with the purposes intended by

Parliament.

In 2012-13, the Department received £827.3 million in respect of child maintenance from non-resident parents. As a result of errors in the calculations of maintenance assessments, I have estimated that, within this amount, a proportion of non-resident parents have made overpayments of child maintenance amounting to £7.6 million, while others have made underpayments totalling £6.1 million. The cases affected by overpayments are unconnected to the cases affected by underpayments; consequently I must report the gross figures. I have therefore qualified my regularity audit opinion on the basis of the gross value of irregular receipts and payments.

My estimate for the level of over and underpayments remains unadjusted within the reported receipts and payments figures in the Account. An adjustment cannot be made to the figures because the value of over and underpayments is an accumulation of a significant number of individual incorrect maintenance assessments. To correct these errors, every decision on each of the affected cases would need to be reassessed from the inception of the case to the present day. Since each case can have a large number of reassessments over its lifetime to account for changes in circumstance, this would represent a significant piece of work.

How do incorrect maintenance assessments occur?

There are currently three statutory maintenance schemes in operation, and the basis for the maintenance assessments under each scheme is set out in the relevant legislation introduced in 1993, 2003 and 2012. The legislation determines the value of the maintenance assessment and the date from which the assessment is effective.

The original 1993 legislation required up to 148 different pieces of information to calculate a maintenance assessment. An error in any element of the assessment will impact the regularity of the child maintenance ultimately received from the non-resident parent. Ordinarily there are multiple assessments throughout the lifetime of a case to reflect changes in circumstance. Where such reassessments occur, the likelihood of error increases.

The 2003 legislation sought to simplify the assessment process and significantly reduce the amount of information required to make an assessment. Despite this simplification, the Department has determined the error rate for cases assessed under these rules to be higher than those operated under the 1993 legislation. This suggests that caseworker error and system problems, rather than complexity of legislation, are the primary causes of incorrect maintenance assessments.

On 10 December 2012, the Department introduced a third maintenance scheme (the 2012 scheme). It was initially launched for new cases involving four or more qualifying children, but from 29 July 2013 the scheme has been extended to new applicants with two or more qualifying children. The Department intends that from 25 November 2013 all new applicants will pass through the 2012

scheme, and that it will transfer all remaining cases on the 1993 and 2003 schemes to the 2012 scheme by 2018, thereby allowing for the closure of the older schemes. At 31 March 2013 there were 581 live cases on the 2012 scheme, of which 187 had amounts charged, with £11,000 received in year. The latest scheme is managed through new processes and a new IT system, which uses gross income information directly drawn from Her Majesty's Revenue and Customs (HMRC) records and systems to automatically calculate assessments. The Department intends that this will reduce much of the administrative complexity and reliance on manual processes that has previously attended the calculation of assessments.

Action taken to address incorrect maintenance assessments

The Department's Client and Process Assurance Team (C&PA) carries out extensive checking of maintenance assessments each year. These checks cover both new applications for child maintenance and cases where there has been a recalculation owing to a change in circumstance. C&PA reported that the Department achieved a cash value accuracy¹ of 98.3 per cent in 2012-13 (98.3 per cent in 2011-12), of which 95 per cent was accurate to the penny (93.4 per cent in 2011-12). The Department's target for 2012-13 was to achieve a cash value accuracy of 97 per cent, which it achieved.

Table 1 shows the percentage of maintenance assessments that C&PA found to be accurate to the penny has improved significantly in recent years. The improvement reflects a more sophisticated analysis by C&PA of the root cause of the errors it found. This has, in turn, allowed both a more targeted process of training for caseworkers and the development of clearer business procedures for undertaking assessments.

Cash value accuracy has remained relatively stable over the same period. In the Department's view, this reflects the embedding of measures introduced to improve the accuracy of assessments.

The table also includes my estimate of the percentage of irregular receipts and payments each year (gross of both under and overpayments). Although the cash value accuracy percentage is used within the calculation of irregular receipts and payments, the two are not directly linked due to the complex calculation methodology.

Table 1: Accuracy of maintenance assessments

	2009-10	2010-11	2011-12	2012-13
<i>Assessments accurate to within a penny</i>	85%	90%	93%	95%

¹ Cash value accuracy is a measure of the value of correct assessment against the value of incorrect assessment. This means that, for an incorrect maintenance assessment calculated at £90 per week which should have been calculated at £100 per week, cash value accuracy would be reported as 90 per cent.

<i>Cash Value Accuracy¹</i>	97%	97%	98%	98%
<i>Estimated irregular receipts and payments (gross)</i>	3.1%	3.1%	2.7%	1.7%

Part Three: Outstanding Maintenance Arrears

Audit Opinion

Where a non-resident parent does not make payments in accordance with their child maintenance assessment, the Department records any shortfall in the outstanding maintenance arrears balance and reports it in Note 6 of the Client Funds Account. The balance of £3.853 billion is the cumulative total of outstanding arrears since the Child Support Agency was established in 1993. This balance represents the total amount owed by non-resident parents to either the parent with care or, in some instances, the Secretary of State. Current legislation allows the Department to write off arrears only in very limited circumstances.

I am required to give an opinion on whether the outstanding maintenance arrears balance as at 31 March 2013 is true and fair. In my opinion there is material error in the value of arrears recorded in Note 6 to the account and as a result I have concluded that Note 6 does not give a true and fair view of the maintenance arrears outstanding at 31 March 2013. The misstatement is primarily a result of:

- a) Incorrect maintenance assessments (as outlined in Part Two); and
- b) Incorrect adjustments to arrears.

a) Incorrect maintenance assessments

Where the Department has made incorrect maintenance assessments, for the reasons set out in Part Two of this report, any arrears accruing will be doing so at an incorrect rate and consequently the value of the accrued outstanding maintenance arrears will be misstated. The Department is unable to estimate the value of this misstatement, but our audit work indicates that the cumulative impact of incorrect maintenance assessments on the value of arrears as at 31 March 2013 is significant.

Action taken to address incorrect maintenance assessments

Part Two of this report outlines the action taken by the Department to address the issue of incorrect maintenance assessments. These actions are taken with a view to improving the accuracy of assessments performed. No action is taken to rectify the errors which remain within arrears, which have built up over a number of years.

b) Incorrect adjustments to arrears

Caseworkers administering child maintenance cases are able to adjust the value of arrears on individual cases. This is to allow the Department to take retrospective action when circumstances change which alter the value of maintenance charged. Errors can arise in the calculation of the required adjustment, which can then result in a misstatement in the value of arrears.

Note 6 in the Client Funds Account reports the arrears balance net of any caseworkers' adjustments, which means that any errors made in these adjustments affect the arrears balance reported. I estimate that arrears are overstated by around £15.2 million and understated by around £105.2 million as a result of such errors.

As with the level of irregular receipts and payments, the Department is unable to make a revision to the arrears note in order to correct for these errors, because they are an estimated aggregation of the accumulated over- and under-adjustments made to individual cases since the inception of the statutory schemes.

Action taken to address incorrect adjustments to arrears

The actions taken by the Department to tackle incorrect adjustments to arrears are similar to the actions taken to address incorrect maintenance assessments. A separate part of the Department's C&PA Team measures the accuracy of adjustments to arrears and undertakes a similar root cause analysis to allow focussed training and improvements to processing procedures.

Table 2 shows that the Department has reached a steady state in the accuracy of adjustments made to arrears. However, as the errors that have accumulated over the years remain uncorrected in the arrears balance, we consider a material level of error remains.

Table 2: Accuracy of adjustments to arrears 2009-10 to 2012-13

	2009-10	2010-11	2011-12	2012-13
<i>Percentage of cases with accurate adjustments to arrears</i>	84%	86%	91%	86%

The clerical case database

The two issues described above are the primary cause of the high value of errors in the arrears balance. Further errors arise from weaknesses in the management of clerical cases, but it is not possible to accurately estimate the financial impact.

Where system failures prevent on-line case management, the Department has to manage the

affected cases manually on a separate clerical case database. This database was originally set up to manage around 10,000 cases, but there are currently over 106,000 cases managed in this way. There are two specific issues with the clerical case database, which are set out below. The Department is planning to take corrective action on the clerical case database balances from 2014-15 onwards, in readiness for the transition of these cases to the 2012 scheme.

Incorrect charging status of cases

The clerical case database requires the manual input of customer maintenance schedules. A maintenance schedule which is not correctly maintained can result in cases incorrectly reporting that no maintenance is due, which will understate the arrears balance at the year end. There is no adequate information available from which I can provide a reliable estimate of error, but the available evidence indicates that arrears are understated as a result.

Opening balances on the clerical case database

Of the cases that the Department has transferred onto the database, there are a number which it transferred without arrears balances. The Department had adjusted for this in the Account by increasing the arrears balance by the value of the arrears reported on the on-line systems for the affected cases before they transferred. The Department's two key assumptions underlying this adjustment are that the majority of nil opening balances on the clerical case database are errors and that the closing balance on the 2003 system is the correct opening balance for cases managed on the clerical case database. My testing has confirmed that this is not the case in all instances. While it is clear that the arrears balance is overstated, there is not, however, sufficient information available to make a reliable estimate for the value of this error.

Collectability analysis

In line with the Accounts Direction, Note 6 also provides an analysis of the Department's assessment of the collectability of the outstanding maintenance balances. The Department has estimated the value of arrears 'likely to be collected' and 'potentially collectable', based on the history of payment from, and payment agreements with, non-resident parents, as well as an estimate of additional recoveries it could secure using existing enforcement powers.

Management's assumptions are subject to an inherent degree of uncertainty, since a number of external factors (including the economic climate and the resources available to the Department to pursue the enforcement of arrears) influence whether any individual non-resident parent will satisfy their arrears balance. Furthermore, the collectability assessment is applied to information on arrears which is known to contain errors as described above. As a result the value of arrears existing as at 31 March 2013 which will actually be collected in the future may be significantly different to that reported as 'likely to be collected' within Note 6.

Part Four: Financial Reporting and IT Systems

Since the inception of the statutory child maintenance schemes there have been significant problems with the main IT systems supporting the schemes. Amongst other problems, the IT systems do not have the functionality to fully report arrears for inclusion in the Account. In order to address this, the Department has developed a separate process to scan the underlying systems and produce a suite of reports. The Department used these reports, in addition to the general ledgers, as the basis for preparing Note 6 to the Account.

The Department first used this revised methodology in 2008-09, and the reports generated have increased the visibility of a number of historic problems which were not previously identifiable. In response to this, the Department has made a number of refinements to the reports since 2008-09 to take account of the issues identified in the underlying data.

The efforts of the Department have resulted in the reporting of a more robust arrears position to that reported in the past. However, due to the scale and age of the issues which have accumulated against some of these arrears balances, there remain significant and unresolved inaccuracies, which materially misstate the arrears balance reported in the Account.

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