



National Audit Office

Report

by the Comptroller
and Auditor General

Department for Work & Pensions

Investigation into errors in Employment and Support Allowance

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Department for Work & Pensions

Investigation into errors in Employment and Support Allowance

Report by the Comptroller and Auditor General

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National Audit Act 1983 for presentation to the House of
Commons in accordance with Section 9 of the Act

Sir Amyas Morse KCB
Comptroller and Auditor General
National Audit Office

15 March 2018

We conducted this investigation because of concerns raised by members of Parliament and in the media in November 2017 about underpayments in Employment and Support Allowance, which is paid to people who have limited capability to work because of their illnesses or disabilities.

Investigations

We conduct investigations to establish the underlying facts in circumstances where concerns have been raised with us, or in response to intelligence that we have gathered through our wider work.

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This report can be found on the National Audit Office website at www.nao.org.uk

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What this investigation is about

1 Employment and Support Allowance (ESA) is a benefit that the Department for Work & Pensions (the Department) pays to people who have limited capability to work because they are disabled or ill. In 2016-17, the Department paid out around £15 billion in ESA to approximately 2.4 million people. There are two main types of ESA:

- contribution-based, which is based on National Insurance contributions; and
- income-related, which is a means-tested benefit. Income-related ESA can be paid on its own or as a top-up to contribution-based ESA.

2 Extra payments, called 'premiums', are available only to qualifying customers who are eligible for income-related benefits. These include the enhanced disability, severe disability, carer, and pensioner premiums.

3 In 2011, the Department began reassessing people who were claiming older-style benefits such as Incapacity Benefit, Severe Disablement Allowance and Income Support. It transferred those who were assessed as eligible to ESA, in a process known as 'conversion'.

4 In November 2017, the media reported that an estimated 75,000 people who had been transferred to ESA had been underpaid premiums. This was because they had been placed on contribution-based ESA only, when they might also have been entitled to income-related ESA. The Department announced on 14 December 2017 that it had already established a special team that had begun to contact the people affected and pay arrears. This team had been convened in August 2017.

5 In 2016-17, the Department made estimated overpayments of £3.6 billion (2% of benefit expenditure) and underpayments of £1.7 billion (1% of expenditure) to claimants across all benefits. The Comptroller and Auditor General has qualified his opinion on the Department's accounts for this reason for the last 29 years. In 2015, the Committee of Public Accounts recommended that the Department should set targets for reducing underpayments, to encourage greater efforts to tackle this neglected issue.

6 The Department initially rejected the Committee's recommendation. Our more recent work has noted that the Department has been taking a more structured approach to tackling fraud and error using analysis of the causes of fraud and error in each benefit to develop its strategy and interventions. In January 2017, the Department agreed to set a target for the 2017-18 financial year that underpayments should be no more than 0.9% of benefit expenditure. In July 2017, we recommended through our audit of the Department's accounts that it should do more to understand the causes of fraud and error and take effective action to reduce underpayments and overpayments.

7 We conducted this investigation because the incorrect payments referred to in this report are a major single source of error that the Department has not addressed over several years. We consider that the events set out in this report emphasise how important it is that the Department continues to improve its approach to identifying and tackling fraud and error. In particular, it should use data and intelligence to investigate the root causes and take prompt action, on both underpayments and overpayments.

8 This investigation:

- explains ESA (Part One);
- assesses the scale of the issue, including: the nature of the error; the amount of underpayment; who is affected; and the Department's plans for paying arrears (Part Two); and
- outlines the Department's management of the issue, including: how and when the issue was discovered; and how information was acted upon (Part Three).

9 We did not assess other aspects of ESA, nor did we examine wider issues relating to fraud and error, or claimants' entitlements to other benefits, as part of this investigation.

Summary

Key findings

The error and how it affects claimants

1 Since 2011, the Department for Work & Pensions (the Department) has underpaid an estimated 70,000 people who transferred to Employment and Support Allowance (ESA) from other benefits. The error related to people who may have been entitled to income-related ESA but were instead only awarded contribution-based ESA, and therefore may have missed out on premium payments. This issue is most likely to affect those with the most limiting illnesses or disabilities, who transferred to ESA from older-style benefits between February 2011 and the end of 2014, by which point the majority of the transfers were complete and the Department had changed the process (paragraphs 2.2 and 2.6 to 2.8).

2 The average underpayment is likely to be around £5,000 by mid 2018-19, with the Department owing an estimated total of £340 million in underpaid benefits. The Department's initial review of a sample of 1,000 cases suggests that 45,000 claimants entitled to the enhanced disability premium only may be due around £2,500 and that around 20,000 claimants who are entitled to the severe disability premium may be owed around £11,500 each on average. One example in the Department's sample indicated that a small number of people could be owed around £20,000 (paragraphs 2.13, 2.14 and Figures 5 and 7).

3 The Department has committed to correcting its error and paying arrears by April 2019. The Department has tasked over 400 staff, mostly experienced ESA processors, with reviewing around 300,000 cases to identify the people affected and pay arrears where these are due. It is recruiting 245 staff to make up the shortfall in other areas of ESA, with the exercise estimated to cost around £14 million (paragraphs 2.16 to 2.19).

4 The Department estimates it will need to pay a total of between £570 million to £830 million more ESA than it previously expected by the end of the 2022-23 financial year. Its central estimate is £680 million more. This is because, in addition to the £340 million in arrears payments, people affected will receive higher amounts of ESA after their claim is corrected (paragraph 2.21 and Figure 7).

5 Eligible claimants will only be paid arrears as far back as 21 October 2014.

On 21 October 2014, the Upper Tribunal (Administrative Appeals Chamber) decided that contribution-based ESA and income-related ESA were a single benefit and that the Department must assess people for both elements when determining their entitlement to ESA. Under social security legislation, the date when a ruling on law is made becomes the date from which the relevant law takes effect. The Department is therefore proceeding on the basis that it can only legally pay arrears as far back as the date of this ruling. The Department estimates that there may be approximately £100 million to £150 million of underpayments accrued before 21 October 2014, which it cannot pay, in addition to the estimated £340 million it will pay for the period from 21 October 2014 (paragraphs 2.10, 2.11 and Figure 3).

How the error happened

6 The Department's process for converting people's benefits to ESA did not reflect its own legislation. Social security legislation from 2010 obliged the Department to check people's entitlement to both income-related ESA and contribution-based ESA, but in practice the Department did not always do this. The Department told us it wanted to avoid delaying the transfer process, reduce administration costs and prevent breaks in payment for claimants. It could not provide evidence that it had carried out any analysis at the time to assess the legal risks involved, or that senior managers had reviewed any such analysis (paragraphs 2.3 to 2.5).

How the error was identified and acted on

7 The Department did not recognise the issue as systemic until 2014.

It issued advice on the correct process to its staff in 2013, indicating that a problem was known to exist, but it does not have a record of how many times the issue was raised. The Department's fraud and error statistics team identified the error as a major cause of ESA underpayments when it was preparing the Department's 2013-14 financial year fraud and error statistics. In April 2014, the Department agreed to classify these cases as official error (paragraphs 3.2 to 3.4).

8 In June 2014, the Department issued new guidance designed to prevent further errors occurring but did not take steps to assess existing cases.

The Department published guidance for decision-makers on its intranet. The Department later updated its formal guidance in February 2015 (paragraph 3.5).

9 The Department's guidance improved the process for people in the ESA 'support group' for those with the most limiting illnesses and disabilities. However, the revised guidance did not cover people in the work-related activity group (who are required to undertake activity such as training or CV skills courses as a condition of their benefit). Although this group is less likely to be eligible for premiums, some will qualify. The Department has now committed to reviewing an additional 6,000 cases in response to our findings about the limits of its guidance (paragraph 3.6).

10 From June 2014 and throughout 2015, the Department did not address existing errors. During this time, two key Upper Tribunal cases helped to clarify the law on ESA claims, including conversion cases. The Department did not recognise at the time that the first of these decisions on 21 October 2014 should have triggered a formal exercise to identify people whose legal entitlements might be affected. Similarly, a further decision in June 2015 prompted discussion but no clear action (paragraphs 3.7 to 3.10 and Figures 3 and 9).

11 From May 2016, the Department's fraud and error team prompted the Department to take action. Following production of the 2015-16 fraud and error statistics in May 2016, the Department's fraud and error strategy and policy team identified an ongoing and significant issue with underpayment of ESA premiums. Their escalation of the issue to the Department's senior management led to an options paper in December 2016. This recommended that the Department should undertake a formal exercise to identify the people affected and provide redress. However, in the first briefing to ministers on this issue in February 2017, the Department recommended undertaking further analysis and seeking further legal advice, while reserving its position on the potential response (paragraphs 3.11 to 3.13).

12 In July 2017, the Department recognised that it had a legal responsibility to identify the people affected and developed a response. The Department first undertook an exercise to review a sample of 1,000 cases and has paid arrears where they were due in those cases. Using the information it gathered through this exercise, it has developed a detailed plan to pay people affected by April 2019 (paragraphs 2.17, 2.18 and 3.14).

Lessons the Department has learned

13 The Department undertook two internal reviews in late 2017 to identify lessons. The first, led by a senior government lawyer and member of the Department's executive team, concluded that a stronger grasp of the Department's legal obligations and risks would have supported better-informed discussions in 2014. It recommended that decisions involving legal risk should be made by sufficiently senior managers. The second review, undertaken by the Department's financial controller, concluded that the Department's finance staff could have been notified about the error more quickly so that they could understand the implications for the Department's financial reporting and its budget once the Department had begun to address the issue in late 2016 and July 2017 (paragraphs 3.15, 3.16 and Figure 9).

Part One

Employment and Support Allowance

1.1 This part of the report introduces the key features of Employment and Support Allowance (ESA) and briefly explains fraud and error in the benefits system.

Introduction of ESA

1.2 ESA is a benefit paid to working-age people if they are ill or disabled and have limited capability to work. As at May 2017, around 2.4 million people in Great Britain received ESA or, in a small number of cases, its predecessor benefits (**Figure 1** overleaf).¹ In 2016-17, the Department for Work & Pensions (the Department) paid out nearly £15 billion in ESA.²

1.3 ESA was first introduced for people making new claims in October 2008. Before that, claimants who had qualifying National Insurance records received Incapacity Benefit. Claimants whose National Insurance contributions record was incomplete, or who had additional needs, and who met a means test, were able to claim Income Support on the grounds of illness or disability.

Reassessing claims for legacy incapacity benefits

1.4 The Department reassessed around 1.5 million existing claimants of legacy incapacity benefits between February 2011 and June 2017 to determine whether these people were entitled to ESA.^{3,4} Most had been reassessed by late 2014 (Figure 1). Meanwhile, the Department continued to pay existing claimants the predecessor benefits.

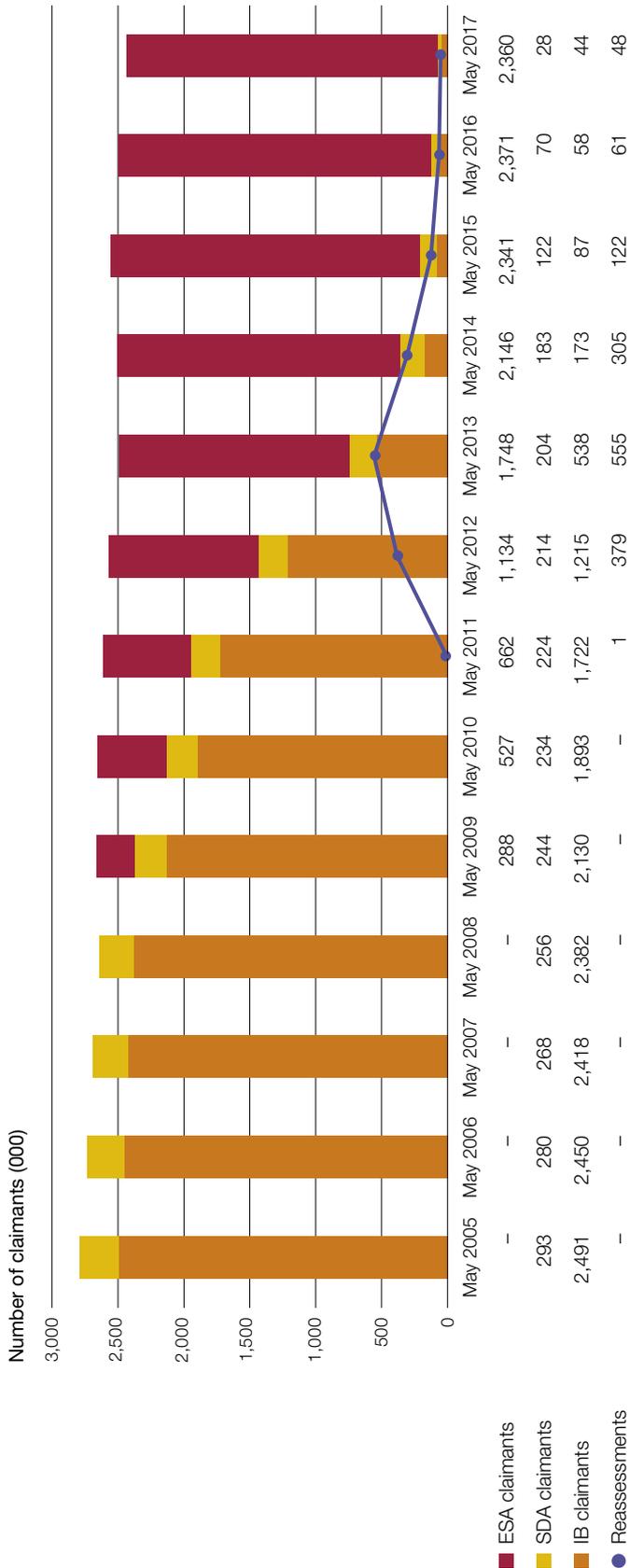
1 Department for Work & Pensions, *DWP benefits statistical summaries 2017, Quarterly benefits summary: November 2017*, November 2017.

2 Department for Work & Pensions, *Benefit expenditure and caseload tables 2017, Outturn and forecast: Autumn Budget 2017*, January 2017.

3 Department for Work & Pensions, *Employment and Support Allowance: outcomes of Work Capability Assessments, Great Britain, quarterly official statistics bulletin*, December 2017.

4 Initial reassessment commenced on 11 October 2010 with a trial of 1,700 claimants in Aberdeen and Burnley. National reassessment began in a phased roll-out from February 2011.

Figure 1
 Number of claimants of incapacity benefits, including Employment and Support Allowance (ESA), May 2005 to May 2017
 ESA started to replace Incapacity Benefit (IB) and Severe Disablement Allowance (SDA) in 2008, and the majority of incapacity benefit reassessments took place between 2011 and 2014



Notes

- 1 Reassessments data is shown for completed reassessments for the year to May. Number of claimants of ESA, SDA and IB is shown as at May each year.
- 2 Data shown is for claimants in Great Britain.
- 3 Reassessments data is for assessments completed and logged between March 2011 and May 2017.

Source: National Audit Office analysis of Department for Work & Pensions data

The two different elements of ESA

1.5 ESA is a single benefit but the basis on which it is claimed can vary:

- If a claimant has made sufficient National Insurance contributions, they may be able to claim **contribution-based ESA** regardless of other family income. Claimants must have paid a minimum level of contributions in one of the two income tax years before the claim. They must also meet a second condition made up of credits and contributions in each of the last two tax years.
- Even if their contribution history is not sufficient, an individual can still claim **income-related ESA** if they have limited family income or savings.⁵ The income-related element of ESA is subject to a means test and includes premiums for additional needs that are not available through the contribution-based element (**Figure 2** overleaf). The income-related element can be paid in addition to the contribution-based element.

1.6 The amount of ESA people are entitled to also varies according to their capability for work-related activity. The Department makes this decision based on a work capability assessment. Following this assessment the claimant will be:

- found to be fit for work and redirected to claim Jobseekers' Allowance; or
- found to be capable of work-related activity, placed in the ESA work-related activity group and required to undertake activity such as training or CV skills courses as a condition of their benefit. Historically, these claimants received an additional work-related activity component, but this is no longer paid for new ESA claims starting on or after 3 April 2017; or
- found not to be capable of work-related activity and placed in the ESA support group. These claimants are not required to undertake work-related activity and receive a higher rate of benefit through an additional support group component of £36.55.

We do not cover the wider ESA assessment process in this report. We reported on the Department's management of the contracted-out work capability assessment in 2016.⁶

⁵ Income-related ESA is now gradually being replaced by Universal Credit. ESA claimed because a person has qualifying National Insurance contributions will not form part of Universal Credit. 'New style' ESA is available to claimants who are entitled to claim Universal Credit and works in the same way as contribution-based ESA.

⁶ Comptroller and Auditor General, *Contracted-out health and disability assessments*, Session 2015-16, HC 609, National Audit Office, January 2016.

Figure 2

Employment and Support Allowance (ESA) amounts and premiums

ESA is payable at different rates depending on factors such as the claimant's age, whether they are in the work-related activity group or the support group, and whether they are entitled to additional premiums

Basic ESA allowance:

- £73.10 for a single claimant/lone parent over 25 (under-25s receive a lower rate);
- £114.85 for couples over 18 (under-18s receive a lower rate);
- £29.05 extra for those placed in the work-related activity group following a work capability assessment; and
- £36.55 extra for those placed in the support group following a work capability assessment.

Those eligible for income-related ESA may also be entitled to additional premiums.

Premium	Amount	Criteria
Severe disability premium	£62.45 for a single claimant or a couple at the lower rate. £124.90 for a couple at the higher rate.	Claimant is entitled to a qualifying benefit, lives alone and no-one receives Carer's Allowance for caring for them. If claimant is in a couple, entitlement varies depending whether these criteria are applicable to either or both members of the couple.
Enhanced disability premium	£15.90 for a single claimant. £22.85 for a couple.	Claimant or their partner is below Pension Credit qualifying age and is in the support group, or is entitled to any of the qualifying benefits.
Carer premium	£34.95 for a single claimant or where carer premium is payable to the claimant only. £69.90 for a couple where carer premium is payable to both the claimant and their partner.	Claimant and/or their partner receives, or has an underlying entitlement to, Carer's Allowance. Underlying entitlement is when a claimant is entitled to Carer's Allowance but does not receive it due to an overlapping benefit.
Pensioner premium	£49.70 for a single claimant in the support group. £99.35 for a couple in the work-related activity group.	Paid if the claimant or their partner has reached Pension Credit qualifying age. The amount of premium payable depends on whether the claimant is single or a member of a couple and whether they are in the work-related activity group or support group.

Notes

- 1 Qualifying benefits are any of: higher rate Disability Living Allowance Care component, enhanced rate Personal Independence Payment Daily Living component, Armed Forces Independence Payment, or Attendance Allowance (SDP only).
- 2 Benefit rates are subject to change each year. Rates shown above are for 2017-18.
- 3 The work-related activity component is no longer paid for new ESA claims starting on or after 3 April 2017.
- 4 Contribution-based ESA is time limited to one year for those in the work-related activity group.

Source: National Audit Office analysis of Department for Work & Pensions data

The right to appeal against a benefit decision

1.7 Since October 2013, if claimants disagree with assessment outcomes they can request a mandatory reconsideration by one of the Department's decision-makers. If they disagree with the mandatory reconsideration outcome, they can appeal to the First-Tier Tribunal. On points of law, further appeal to the Upper Tribunal may be possible. The Department's experimental statistics from December 2017 indicate that between October 2013 and March 2017, 260,000 mandatory reconsiderations were registered in relation to 1,700,000 completed work capability assessments. Some 20% of assessments with a completed mandatory reconsideration also complete an appeal. Of this group (53,000 cases), the latest case decision was upheld 40% of the time. Being found 'fit for work' at assessment is the primary reason for claimants disputing a decision, and also the main reason for appeal hearings.⁷

Fraud and error in ESA

1.8 Sometimes claimants receive the wrong amount of benefit. This can be an underpayment (where claimants are paid too little benefit) or an overpayment (where they are paid too much). The Department groups overpayments and underpayments into three categories:

- **official error:** when a benefit is paid incorrectly due to inaction, delay or a mistaken assessment by the Department, a local authority or HM Revenue & Customs;
- **claimant error:** when claimants make mistakes with no fraudulent intent; and
- **fraud:** when claimants deliberately seek to mislead the Department or local authorities that administer benefits on the Department's behalf to claim money to which they are not entitled.

1.9 The Department's statistics show that in 2016-17, an estimated £3.6 billion of benefits was overpaid (2% of benefit expenditure) and £1.7 billion (1% of expenditure) was underpaid to claimants.⁸ Overpayments and underpayments of ESA were higher than for benefits in general:

- Overpayments of ESA increased between 2015-16 and 2016-17, from 3.1% to 4.0% (£590 million), the highest recorded rate.
- Underpayments of ESA also increased between 2015-16 and 2016-17, from 2.4% to 2.9% (£440 million), also the highest recorded rate.

⁷ See footnote 3.

⁸ Department for Work & Pensions, *Fraud and error in the benefit system: financial year 2016 to 2017 estimates*, November 2017.

1.10 In 2016-17, the Comptroller and Auditor General qualified his opinion on the Department's accounts for the 29th consecutive year, because of the level of fraud and error leading to overpayments and underpayments. In 2015, the Committee of Public Accounts recommended that the Department should set targets for reducing underpayments, in order to encourage greater efforts to tackle this neglected issue.⁹ The Department initially rejected this recommendation but later, in January 2017, it advised the Committee that it had set a target for underpayments to be no more than 0.9% of benefit expenditure in the 2017-18 financial year.¹⁰ Achieving this target would return total underpayments to the level at which it had been in 2014-15.¹¹

1.11 More broadly, in 2015, in response to recommendations we made through our audit work, the Department began to take a more structured approach to tackling fraud and error, using analysis of the causes of fraud and error in each benefit to develop its strategy and interventions.¹² The Department considers that this work led it to apply greater scrutiny to overpayments and underpayments, including detailed analysis of ESA underpayments after May 2016. It was this analysis that, ultimately, led to the Department taking action on the issues we cover in this report. In our most recent financial audit, covering the 2016-17 financial year,¹³ we noted that the Department still has more to do to realise the benefits of its work on fraud and error.

9 HC Committee of Public Accounts, *Fraud and Error Stocktake*, Fourth Report of Session 2015-16, HC 394, October 2015.

10 HM Treasury, Treasury Minutes: *Government responses to the fourth to the eighth reports from the Committee of Public Accounts*: Session 2015-16, Cm 9190, January 2016.

11 Department for Work & Pensions, *Fraud and error in the benefit system: financial year 2014-15 estimates*, November 2015.

12 Comptroller and Auditor General, *Fraud and error stocktake*, Session 2015-16, HC 267, National Audit Office, July 2015.

13 Comptroller and Auditor General, *Department for Work & Pensions 2016-17 Accounts*, Report by the Comptroller and Auditor General: *Fraud and error in benefit expenditure*, July 2017.

Part Two

The error, who is affected and the Department's plans for correcting its mistake

2.1 This part of the report sets out the nature of the error and how it occurred, who it affects, and the Department for Work & Pensions (the Department's) plans for identifying and paying arrears to the people who have been underpaid.

What was the error?

2.2 This investigation covers a single, major cause of underpayment error in Employment and Support Allowance (ESA). This error relates to people whose existing benefit claim was converted to ESA and who were entitled to income-related ESA but were only awarded contribution-based ESA. This caused people to miss out on premium payments.

2.3 The root cause of the error was that the Department's processes did not deliver what was set out in law. Social security legislation from 2010 imposed a duty on the Department to award on conversion what would have been awarded if a new claim for ESA was made. As ESA is made up of two strands (contribution-based and income-related), this would have required an assessment of entitlement to both strands of the benefit. In practice, the Department did not require its decision-making staff to gather the information they needed to make this assessment. The Department described the process in place at the time as set out below:

- Claimants' existing benefits were used as a proxy. The Department told us that it used an automated process to transfer those in receipt of an income-related benefit, such as Income Support, to income-related ESA, and assumed those solely in receipt of a contribution-based benefit, such as Incapacity Benefit, would transfer to contribution-based ESA.
- Claimants who were not already receiving an income-related benefit were to be invited to provide additional income data if they thought they might have an additional entitlement.
- Claimants were contacted by telephone prior to the conversion to explain the process and next steps. Claimants then received a letter at the point of conversion advising them of their payment type and rate.

2.4 If claimants were transferred to contribution-based benefit, the letter set out that income-related benefit was available, and provided some information about the eligibility criteria. The claimant was advised to make contact if they thought that they may be entitled. The letter did not, however, make clear that, if entitled, the claimant might be better off. The Department stated that a further telephone call to the claimant was made at this point, however it cannot confirm how many individuals it spoke to.

2.5 The Department told us that it developed this process because it wanted to avoid delays to the transfer process, reduce administration costs and prevent breaks in payments to claimants. An internal Departmental review, conducted in late 2017, did not find any evidence that officials sought legal advice on the process, nor any record of senior-level sign-off of the process. The Department could not provide any additional evidence to us on this point as part of our investigation. The ‘incapacity benefit reassessment’ process as it was known was controversial. The Department had earlier rejected a recommendation by the Social Security Advisory Committee to pause the process while some of the complexities could be worked out. The Department also noted that reviews conducted at the time did not raise this specific issue.

Who is affected?

2.6 This error is most likely to affect people who transferred to ESA from other benefits between February 2011 and the end of 2014, when the bulk of transfers from older incapacity benefits took place. Specifically, it affects people:

- whose existing contribution-based benefit claim was transferred to contribution-based ESA; and
- who had an underlying entitlement to income-related ESA and would have been better off had they been awarded income-related ESA.

2.7 The error is less likely to affect the minority of people who were transferred to ESA after June 2014, when the Department issued new guidance that brought its process more into line with legislation.

2.8 The Department’s latest estimate is that 70,000 people are affected. Its analysis indicates that most of these people (around 65,000) are in the support group for ESA. This is partly because one of the premiums, enhanced disability premium, is payable automatically to claimants who qualify for income-related ESA and are in the support group. The support group comprises some of the Department’s most vulnerable claimants, who are not required to undertake any work-related activity because of their illnesses or disabilities.

Who is due arrears?

2.9 To qualify for arrears people will have:

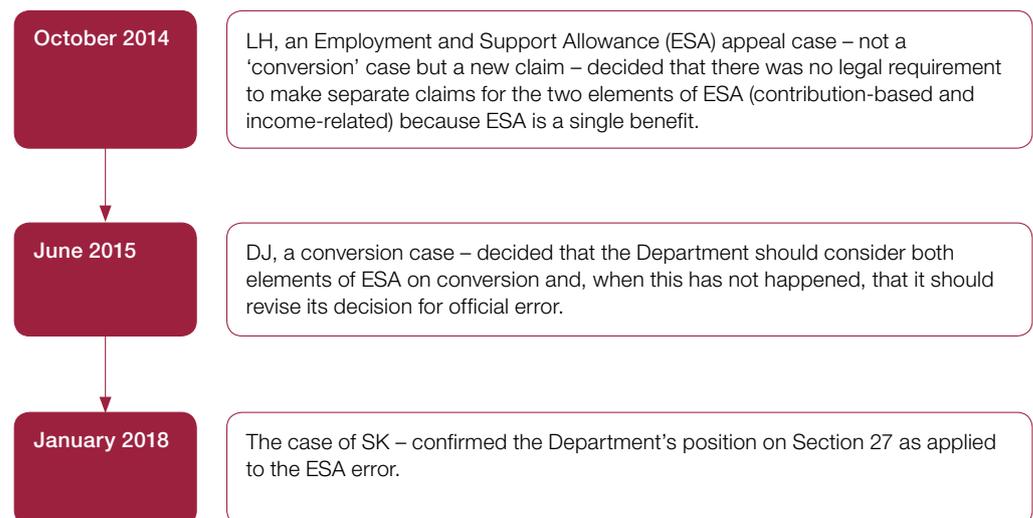
- had their claim converted to ESA from older-style incapacity benefits;
- had a claim that was still live at 21 October 2014; and
- been awarded contribution-based ESA only, but had an underlying entitlement to income-related ESA (and met the eligibility criteria for one or more premiums at the time of conversion).

2.10 Not everyone who has been affected by the error will receive the full amount they have been underpaid. This is because of the effects of Section 27 of the Social Security Act 1998. Under Section 27, when the Upper Tribunal or court considers an appeal under social security legislation and establishes the relevant points of law, the law as established takes effect from the date of the court's decision. On 21 October 2014 the Upper Tribunal (Administrative Appeals Chamber) decided that contribution-based ESA and income-related ESA were a single benefit and that the Department must assess people for both elements when determining their entitlement to ESA. The Department is therefore proceeding on the basis that it can only legally pay arrears as far back as the date of this ruling. **Figure 3** sets out key aspects of the LH case and later relevant decisions.

Figure 3

Key aspects of three Upper Tribunal rulings

There have been three key Upper Tribunal cases which have shaped the Department's response to this error: the case of LH, the case of DJ and the case of SK



Notes

- 1 LH versus SoS for Work and Pensions (ESA) [2014], CE/4181/2013, October 2014.
- 2 DJ versus SoS for Work and Pensions (ESA) [2015], CE/277/2014, June 2015.
- 3 SK versus SoS for Work and Pensions (ESA) [2017], CSE/33/2017, December 2017.

2.11 The Department estimated in November 2017 that there may be approximately £100 million to £150 million of underpayments from before October 2014. These were, however, only indicative estimates. The Department has not updated this analysis more recently because it considered the position on Section 27 clear.

2.12 **Figure 4** illustrates the scope of the Department's review for four hypothetical claimants whose claims begin and end at different points in time, taking into account the Department's guidance and the effect of its application of Section 27.

How much is owed to claimants?

2.13 The Department does not yet know exactly how many people will be owed arrears or what the amounts payable will be. Its latest estimate of 70,000 people is based on an analysis of 1,000 cases that the Department initiated in July 2017. It used this analysis to develop the process to repay claimants, including a process for contacting families and next of kin where claimants have died since October 2014, and to inform estimates of the error rate, the amounts payable and the time it was likely to take to process each case.

2.14 On average, the Department estimates that each claimant could be due around £5,000 by the time the payments are made. The actual amount payable will, however, depend on each individual's specific entitlements and the duration of their claim. Taking the mid point of 2018-19 as the basis of when a payment is made, the Department's initial review of a sample of 1,000 cases suggests that around 45,000 claimants entitled to the enhanced disability premium only may be due around £2,500. Around 20,000 claimants with entitlement to the severe disability premium may be owed around £11,500 each on average. One example in the Department's sample indicated that a small number of people could be owed around £20,000. **Figure 5** on page 20 shows two examples of how individual cases could add up.

2.15 Aside from the direct impact of underpayments, it is possible that claimants may have missed out on other benefits and schemes. For example, people who receive income-related ESA can qualify for free school meals and help with prescriptions. These potential effects are not within the scope of the Department's current exercise.

Figure 4 Illustration of which claimants are included and excluded from the Department's review and which are eligible for payment of arrears

Claimants fall into different cohorts depending on factors such as the date their claim was converted to Employment and Support Allowance (ESA), whether their claim remained live at 21 October 2014 and which assessment group they are in. The cohort a claimant falls into determines whether they are included in the Department's review and how much they may be due in arrears

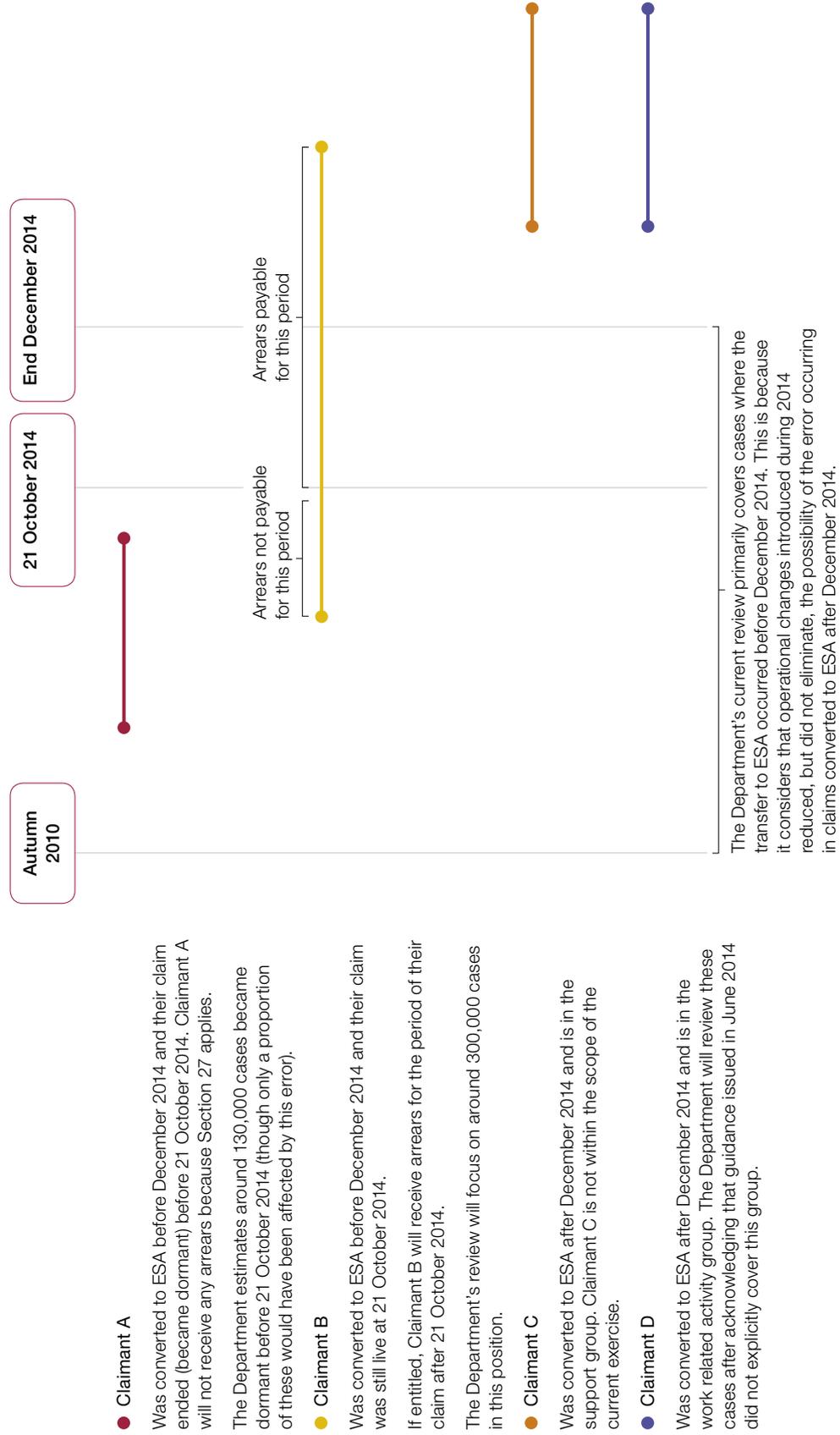


Figure 5

Examples showing how arrears due might differ from case to case

Arrears due will vary depending on premiums the claimant is entitled to and the length of time that these have been underpaid. No arrears will be paid for the period before 21 October 2014 (see paragraph 2.10)

Claimant X	Arrears due
Converted to contribution-based Employment and Support Allowance (ESA) in 2011.	Around £13,000
Their circumstances at the date of conversion meant that if they had been assessed for income-related ESA they would have been entitled to:	
<ul style="list-style-type: none"> • Enhanced Disability Premium (EDP) at around £16 per week; and • Severe Disability Premium (SDP) at around £62 per week. 	
Their circumstances have not changed and their claim to ESA is still active when they are contacted by the Department in 2018.	

Claimant Y	Arrears due
Converted to contribution-based ESA in 2013.	Around £1,000
Their circumstances at the date of conversion meant that if they had been assessed for income-related ESA they would have been entitled to:	
<ul style="list-style-type: none"> • Enhanced Disability Premium (EDP) only at around £16 per week. 	
Their circumstances did not change until they moved off ESA in 2016. Their claim to ESA is dormant when they are contacted by the Department in 2018.	

Notes

- 1 The EDP weekly rate was £15.55 in 2014, rising to £15.90 by 2017. The SDP weekly rate was £61.10 in 2014, rising to £62.45 by 2017. Proposed benefit and pension rates are available for each year at gov.uk.
- 2 Where transitional protection was in payment on conversion to ESA because the previous incapacity benefit award was higher than the new ESA award, this will reduce the amount of underpayment due.
- 3 These are hypothetical examples, assuming the Department made contact at the time of our fieldwork in January 2018.

Source: National Audit Office analysis of Department for Work & Pensions information

The Department's plans to correct the error and the costs involved

2.16 The Department plans to review around 300,000 ESA cases that may be affected. **Figure 6** sets out the process that staff will follow to assess cases and process payments.

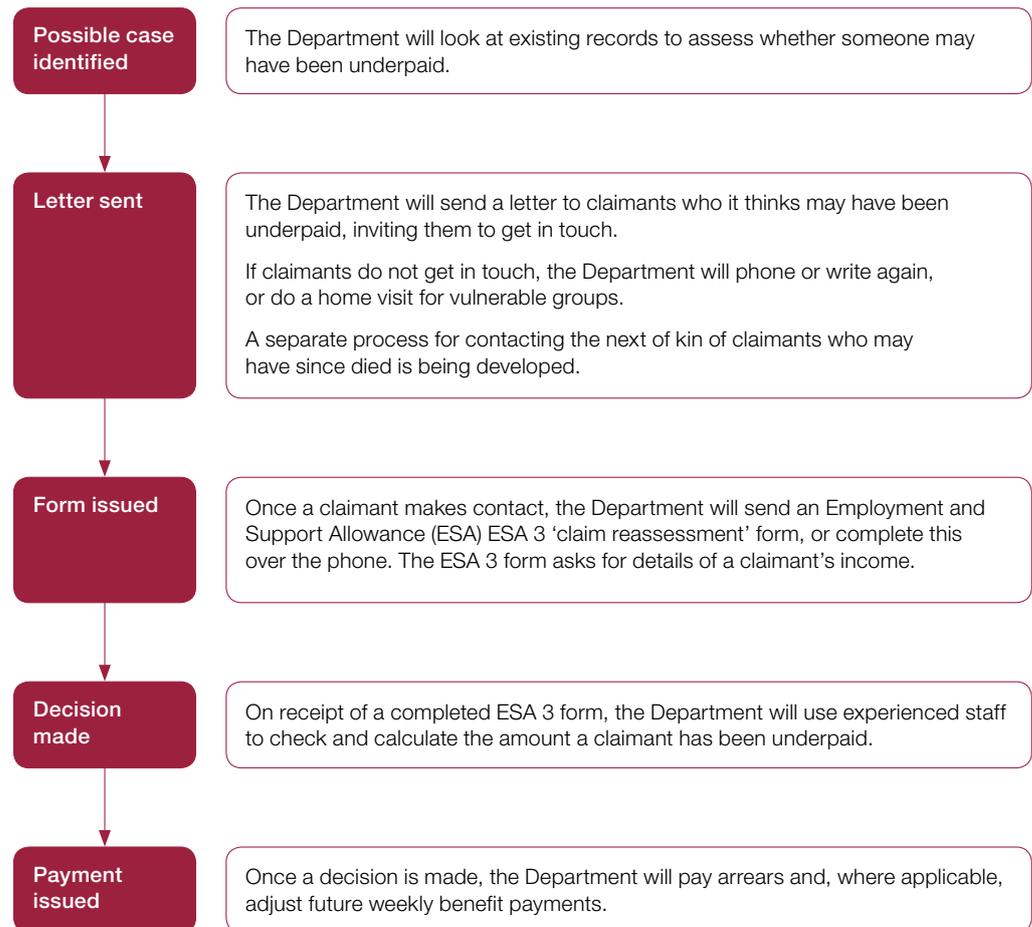
2.17 The Department plans to pay claimants affected and correct their claims by April 2019. It has developed a detailed plan designed to balance meeting this target with maintaining an acceptable service to other ESA claimants. The key elements of the Department's plan involve:

- redeploying around 400 experienced ESA processing staff to undertake the ESA underpayments work such as calculating and paying any arrears due; and
- recruiting 245 administrative staff for one year to 'backfill' roles such as handling telephone enquiries.

Figure 6

The Department's process for correcting claims and paying arrears

The Department will contact people who might be affected to gather the necessary information to assess their claim. Once a claimant is contacted, the Department aims to pay any arrears due within 12 weeks



Source: National Audit Office analysis of Department for Work & Pensions information

2.18 The Department intends to contact all claimants it believes may be affected throughout the course of 2018-19. Once contacted, and subject to the relevant information being obtained, the Department aims to make any payment due within 12 weeks.

2.19 Contacting all the claimants affected, correcting their claims and making repayments will be a major exercise and comes at a time when the Department had expected to be scaling back ESA operations because of the ongoing implementation of Universal Credit. The Department has estimated the total administration cost of this exercise to be around £14 million, taking account of the cost of staff and additional management time required.

2.20 Each case will require staff to carry out a detailed assessment of the individual's benefit entitlement and calculate the amounts payable. During our fieldwork in February 2018, we observed staff undertaking manual calculations to assess people's entitlements. At this time, the Department was still developing its quality assurance processes and was also working on ways to automate some of the calculations required.

2.21 Correcting these errors means the Department will have to pay out more ESA than it had expected. Based on its review of a sample of 1,000 cases, it estimates it will pay out a total of £680 million more between now and the end of the 2022-23 financial year. This is because, in addition to the £340 million arrears payments, people affected will receive higher amounts of ESA after their claim is corrected. The actual amount could be higher or lower. **Figure 7** shows the Department's estimate of the amount of extra benefit that will be payable in each year.

Figure 7

The Department's estimates of the total extra amount of Employment and Support Allowance (ESA) payable

The Department estimates it will need to pay £340 million in historic underpayments, and between £70 and £80 million per year in increased forward payments. Total extra ESA payable is estimated at £680 million

	2018-19 (£m)	2019-20 (£m)	2020-21 (£m)	2021-22 (£m)	2022-23 (£m)	Total (£m)
Upper case	480	100	90	80	80	830
Central case	390	80	80	70	70	680
Lower case	320	70	60	60	60	570

Notes

- 1 The £390 million central case estimate in 2018-19 comprises £340 million in 'one-off' arrears payments, plus £50 million in increased forward payments because the claimant is being paid, correctly, a higher amount.
- 2 Forecasts of higher awards to be paid on corrected claims have been adjusted for inflation. Historic arrears accounted for are the benefit rates applicable to each year of underpayment.
- 3 The central case is the Department's best estimate. The upper and lower cases illustrate the Department's estimate of the likely minimum and maximum amounts. The actual amount will depend on the number of people affected and the amount of arrears owed in each case.
- 4 These figures are estimates based on a sample of 1,000 cases that the Department analysed during 2017.
- 5 Totals may not sum due to rounding.

Part Three

How the Department identified and acted on the error

3.1 This part of the report covers the Department for Work & Pensions (the Department's) actions to identify and act on the error. **Figure 8** overleaf summarises the key events.

The period February 2011 to May 2014

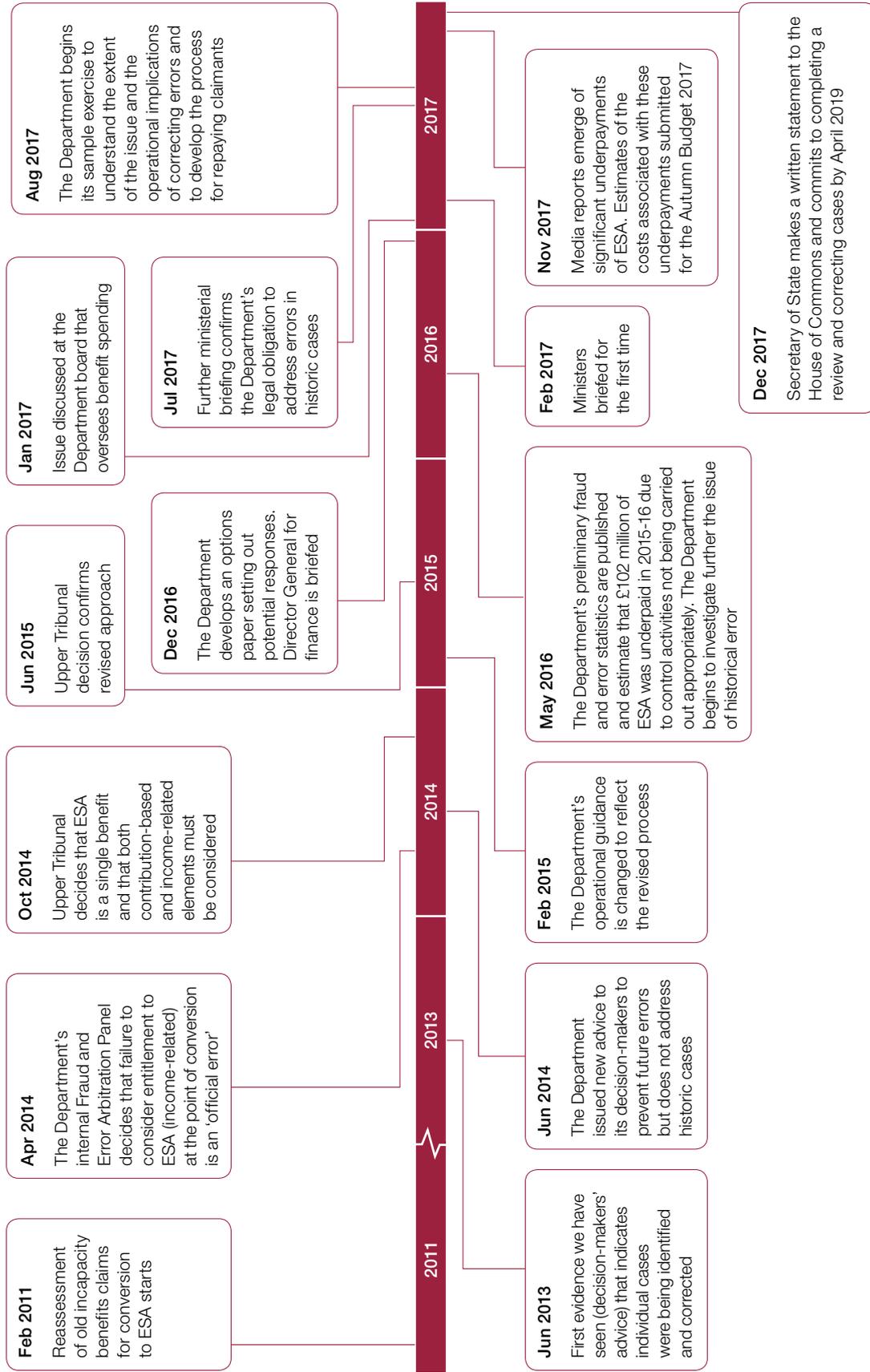
3.2 The Department did not initially recognise individual cases as part of a wider problem. Some Departmental discussions from 2017 refer to ministerial correspondence from 2013. The Department has not, however, been able to find specific instances of correspondence because its records only go back to 2014. We have also seen advice for decision-makers from June 2013, which shows that the issue was raised by front-line staff before this date.

3.3 The Department first identified the error as a systemic issue in 2014, while preparing its regular statistics on fraud and error in the benefits system. To prepare these statistics, the Department's analysts check a representative sample of benefits payments made across the year. From these results, they estimate the total level of overpayments and underpayments. The Department first carried out this type of analysis for Employment and Support Allowance (ESA) for the 2013-14 financial year statistics, and identified cases where entitlement had been assessed incorrectly on conversion.

3.4 Initially, there was disagreement within the Department as to whether this was 'official' error (error on its part) or 'customer' error (error on claimants' part). Following internal arbitration in April 2014, however, the Department agreed to classify these cases as official error. The final 2013-14 statistics, published in November 2014, reported that, of the £190 million ESA underpayments that year, over a third were because of official errors on premiums that occurred when people were transferred from Income Support or Incapacity Benefit to ESA and their case was not dealt with correctly.

3.5 In June 2014, the Department issued new advice to its decision-makers. It then updated its formal guidance in February 2015. The changes to the guidance were designed to ensure that new cases of this error did not occur and that cases were put right if they came to light. Specifically, the Department told staff to issue an 'ESA 3' form to gather information from claimants who were placed in the ESA support group. It did not, however, tell staff to actively review existing cases where someone's claim had already been converted to ESA.

Figure 8 Key events in managing the Employment and Support Allowance (ESA) underpayment error between February 2011 and December 2017



Source: National Audit Office analysis

3.6 We found that the Department's revised guidance did not set out a process for gathering information from claimants in the work-related activity group, some of whom might still be entitled to premiums. This created a risk that some people might miss out on premium payments, because the Department's exercise to identify people who had been underpaid included people who were in the work-related activity group before December 2014 but not after. The Department has committed to reviewing a further 6,000 cases in response to our findings about the limits of its guidance.

The Department's response to key legal decisions in 2014 and 2015

3.7 Meanwhile, and separately to work on the fraud and error estimates, the Department's policy, operations and legal staff were preparing for the first of two key Upper Tribunal cases. These cases had a significant bearing on the Department's eventual response to the error, but their importance was not fully recognised at the time.

3.8 On 21 October 2014, the Upper Tribunal decided the first of two key ESA cases (see Figure 3). The Department's teams working on this case did not identify its importance for conversion cases, nor did they recognise its effect in setting the statutory bar for payment of arrears. The Department now acknowledges that this case should have triggered a formal exercise in line with Legal Entitlements and Administrative Practices (LEAP) principles (**Figure 9**).

Figure 9

Legal Entitlements and Administrative Practices (LEAP)

LEAP is a report by civil service officials in 1979 which provides a framework for considering how to deal with cases where there has been a failure by a government department to meet legal entitlements:

- The Department uses LEAP exercises to make key decisions in situations where a mistake has been made that affects a large volume of cases.
- The exercise weighs the individual impact on each claimant against the overall impact on the Department, and tries to establish a proportionate response.
- The exercise does not have any legal standing, but can be used in future litigation to show that the Department has taken a rational approach to the decision.

Note

1 Legal entitlements and administrative practices: A report by officials, 1979.

Source: National Audit Office review of Department for Work & Pensions information

3.9 Over the next two months, operational, strategy and legal officials continued to work on the second key Upper Tribunal case (the case of DJ - see Figure 3). Discussions between the Department's officials at this point mentioned the potential for Section 27 to be triggered by the tribunal's decision in the DJ case, and also the potential operational impact should the Department be obliged to revisit historical cases. The need for a ministerial submission was discussed but we have not seen any evidence that a submission was made.

3.10 During September 2015, officials involved in the earlier tribunal cases continued to express doubt about the Department's conversion process. These discussions referred to possible further analysis involving the Department's operational excellence team, but there is no evidence that the Department carried this out. No further clear action was taken on this issue in the second half of 2015.

The Department's response from 2016

3.11 The Department's preparations for its 2015-16 publication of interim statistics on fraud and error in the benefits system again highlighted historical underpayment of premiums as a major source of ESA underpayments. Following publication of the interim fraud and error statistics in May 2016, the Department's fraud and error strategy and policy team commissioned further analysis. This confirmed that there was an ongoing issue and highlighted that errors in historical cases had not been addressed.

3.12 From August 2016, the Department's fraud and error strategy and policy team played an active role in escalating this issue to senior managers. In November 2016, the head of the team raised the error with senior officials in the Department's ESA policy and finance teams, and recommended an urgent response. In December 2016, the fraud and error strategy and policy team was commissioned to develop options for a response.

3.13 The resulting options paper, completed in December 2016, recommended that the Department undertake a 'LEAP' exercise to identify the people affected and provide redress (see Figure 9). However, the first briefing to ministers on this issue in February 2017 recommended undertaking further analysis and seeking further legal advice, reserving the Department's position and deferring any decision to launch a formal exercise.

3.14 In July 2017, following the general election, the Department further advised the then ministers that it had a legal responsibility to identify the people affected and develop a response. At this time, it also confirmed its view that the 21 October 2014 Upper Tribunal decision had the effect of barring payment of arrears before that date. In August 2017, the Department began an exercise to review and begin paying 1,000 of the cases, to inform its approach to the full exercise. The approach to complete a full review was agreed by ministers in November 2017 and was announced via a written ministerial statement in December 2017.

Lessons the Department has learned

3.15 The Department undertook two internal reviews in late 2017 to identify lessons. The first, led by a senior government lawyer and member of the Department's executive team, concluded that a stronger grasp of the legal obligations and risks described in the LEAP report would have been a better backdrop to the discussions in 2014. It recommended that decisions involving legal risk should be made by managers of appropriate seniority.

3.16 The second review, undertaken by the Department's head of financial control, focused on the period after March 2016. It concluded that finance staff could have been notified more quickly as part of the escalation of the issue in late 2016 and 2017. The review also agreed with our past recommendations that the Department should review annual fraud and error estimates after publication to assess the root causes of fraud and error and explain what action is being taken to tackle them.

Appendix One

Our investigative approach

Scope

1 We conducted an investigation into underpayment errors in Employment and Support Allowance (ESA) affecting people whose benefits were converted to ESA from older style incapacity benefits. In November 2017, the media reported that an estimated 75,000 people who had been transferred to ESA had been underpaid premiums on their ESA. This was because they had been placed on contribution-based ESA incorrectly, when they might have been entitled to income-related ESA. We examined:

- the scale of the issue, including: the nature of the error; the amount of underpayment; who is affected; and the Department's plans for paying arrears; and
- the Department's management of the issue, including: how and when the issue was discovered; and how information was acted upon.

Methods

2 In examining these issues, we drew on a variety of evidence sources:

- We interviewed Department for Work & Pensions (the Department) officials to establish the nature of the error, who is affected, the impact on claimants, how the Department identified the error and its plans to correct the error.
- We visited front-line staff in one of the benefits centres that are contacting the people affected and correcting individual cases.

3 We reviewed:

- a range of the Department's documents, including: official guidance; operational plans; internal review documents; quantitative analysis; and correspondence between Departmental officials;
- online discussion forums covering individual cases affected by this error and Freedom of Information requests; and
- decisions of the Upper Tribunal (Administrative Appeals Chamber).

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