Challenging tax credit overpayments

A practical guide for Advisers
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Challenging tax credit overpayments – A guide for advisers

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SECTION 1 – AN OVERVIEW OF THE TAX CREDIT SYSTEM

This guide has been written primarily for those who have some knowledge of the tax credit system and who need more information about the methods of challenging tax credit overpayments. We have also written, in association with Advicenow, a guide for claimants which provides basic information about appealing, disputing and dealing with tax credit debt. More information about tax credits can be found on our website. We have also created a website, in partnership with Rightsnet, for advisers which contains information, resources and updates on all parts of the tax credits system – www.revenuebenefits.org.uk

1.1 Introduction

Of the many differences between traditional social security benefits and tax credits, one of the most fundamental is that, in tax credits, overpayments are an integral and often unavoidable part of the system.

While a benefit claimant’s entitlement is generally ascertainable at the time of payment, entitlement to tax credits for a tax year cannot be established until after the year-end. Payment during the year is based on income of a previous year, or an estimate of income for the current year; but it is not until after the year-end that the actual current year income can be ascertained and final entitlement assessed. If it then transpires that the claimant’s entitlement exceeds what they have been paid, there is an underpayment; if it is less, an overpayment arises.

First let us look in greater detail at how the tax credit system is structured, as it is necessary to understand that in order to grasp how tax credit overpayments arise.

1.2 Annual nature of the tax credit system

The cycle of award and entitlement

The reason why overpayments are endemic in the tax credit system is that the system works on the basis of pay now, establish entitlement later. Unlike any other welfare benefits, entitlement to tax credits is based on the tax year, 6 April to the following 5 April, but it is not until after the end of the tax year in which payment is made that entitlement is finally ascertained. This ‘cycle’ of award followed by entitlement works like this.

An initial award is made at the start of the year, or when a claim is received, based on the claimants’ current circumstances, and their income for the previous tax year. ¹

As the year progresses the claimant has the opportunity to notify changes in circumstances and income so as to keep their award updated, and is obliged to report certain changes such as alterations in the composition of the adult members of the household, in the children or young persons for whom a claimant is responsible, and in normal weekly working hours. The first of those groups includes single claimants entering a relationship, couples splitting up, or one member of a couple dying or going abroad for a prolonged period.

¹ For 2003-2004 the ‘previous tax year’ was deemed to be 2001-2002 (not 2002-2003) to enable claims to be made in advance.
The second might include children leaving the household and going into care, young people aged 16 or over dropping out of further education or training, or a child dying. The third group involves reporting to HMRC if ‘normal’ weekly working hours drop from 16 or more hours a week to below 16, or from 30 or more hours a week to less than 30. A full list of changes that must be notified can be found on the HMRC website.

Assessing entitlement for the ‘current year’

After the year end, HMRC send a stack of renewal papers, the purpose of which is to ascertain the claimants’ actual entitlement for the year just gone, and if appropriate act as a claim for the year ahead. Changes in entitlement will arise from changes in personal circumstances and changes in income. For income the final entitlement is based on the following formula:

For income rises – income disregard £5,000

(a) If current year income (CYI) is greater than previous year income (PYI) by no more than a certain amount (known as an income disregard, the final award is based on PYI;

(b) If CYI is greater than PYI by more than the specified income disregard, the final award is based on CYI less the income disregard, and an overpayment may arise.

For falls in income – income disregard £2,500

(c) If PYI exceeds CYI by no more than a certain amount (known as an income disregard) the final award is based on PYI;

(d) If PYI exceeds CYI by more than the specified income disregard, the final award is based on CYI plus that specified income disregard.

All other cases

Where none of the above apply, the claim is based on CYI.

Establishing initial award for the following year

The same information is also used to establish the claimants’ initial award for the following tax year although in that case the full CY income is used. The income disregard for the current year, CY, can only be used to compare CY income with preceding year income; it cannot be carried forward to the following tax year.

1.3 The income disregard and its implications

The income disregard in each year from 2003-04 to 2005-06 inclusive was £2,500. Its purpose was to provide a ‘buffer zone’ in which a family’s income could increase during the course of a year without affecting their tax credit entitlement. Though considered generous at the time it was introduced, in the event the £2,500 buffer zone proved insufficient to prevent hardship to families whose income increased above that amount. Therefore in 2006-07, in a bid to reduce the volume of overpayments arising from increases in income, the income disregard was increased quite dramatically to £25,000.
That was probably the most significant of the changes announced in the pre-Budget Report on 5 December 2005 (‘PBR 2005’), and the overpayment figures relating to the 2006-2007 tax year showed a significant fall in both the number and amount of overpayments. HMRC have attributed this largely to the increased disregard.

The effect of the increase has been to bring greater certainty for claimants in a system where a major problem had been the sheer unpredictability of what families could expect to receive. Yet, the tax credit system retains some flexibility for those whose income goes down in a year to claim a higher entitlement, subject to one important new restriction discussed at point 3 below. The June 2010 emergency Budget announced changes to the disregard both by introducing a disregard for falls in income but also by reducing the disregard for rises in income from £25,000 to £10,000 from April 2011 and then down to £5,000 from April 2013.

As a result of these changes, it is likely that overpayment figures will rise again as the disregard gets nearer to the original choice of £2,500. In addition, the introduction of an income disregard for falls in income means that the flexibility which the system had will be partially restricted when income falls as such families will no longer be immediately able to secure a higher entitlement to match their new income level. See our Revenuebenefits website for more information about Budget changes.

We have written a detailed guide called ‘understanding the disregards’ aimed at advisers who need more knowledge of how the disregards work. The guide covers the history of the income disregards, how changes to the disregards are applied, how each of the disregards works, the position when income decreases and then increases in year and HMRC’s power to estimate current year income. The guide can be found at http://www.revenuebenefits.org.uk/tax-credits/guidance/how-do-tax-credits-work/understanding-the-disregard/
SECTION 2 – AN INTRODUCTION TO OVERPAYMENTS

2.1 How do overpayments arise

Apart from income rises (as explained in section 1), there are several other ways in which overpayments can occur. These include:

1. **Claimant error**

   The tax credit system is extremely complex and claimants have many responsibilities that they must adhere to in order to keep their tax credits up to date. As if having complex rules was not difficult enough, HMRC’s explanation of those rules is not always good enough for most claimants to understand their obligations. This often leads to claimants misunderstanding the rules.

2. **Official (HMRC) error**

   Official error by HMRC can refer to many things from wrong advice by the tax credit helpline and computer errors to misleading advertising materials. As complex as the system is for claimants, it is equally so for the HMRC staff who have to administer it, which means that helpline advice can be wrong or misleading and even HMRC publications have given incorrect information about the system.

3. **Claimant delay in notifying changes of circumstances or income**

   There are certain changes of circumstances that must be notified to HMRC within one month of them happening (or from when the claimant became aware of them occurring). Even if a claimant reports a change within one month, an overpayment may still build up because an overpayment generally starts to accrue the day after the change. For example, if someone drops their working hours from 35 to 25 (thereby losing the 30-hour element) on 1 May and tells HMRC on 25 May, they will avoid a penalty for failure to report a change of circumstances, but will most likely have an overpayment of the 30-hour element from 2 May to 25 May.

4. **HMRC delay in processing changes of circumstances or income**

   Changes of circumstances can be reported via the tax credit helpline or in writing to the Tax Credit Office. Generally, changes done via the helpline are implemented immediately. On occasion, HMRC take a considerable period of time to action the changes and in some cases don’t action them at all. As explained later in the guide, HMRC allow themselves 30 days to action a change, and any overpayment building up in that period is fully recoverable.

5. **Adjustment of a claim following in-year examination or end-of-year enquiry**

   HMRC have various compliance powers to check claims during the year (examinations) and also following the end of the tax year (enquiries). If they find anything that they believe is wrong, an amendment to the claim will be made and often these go back at least one tax year, generally creating an overpayment.
For example, an enquiry into a 2011-2012 claim concludes that the claimant was not a single person and should have claimed as a couple. The whole 2011-2012 claim will become overpaid as there was no entitlement as a single person. (Note that notional offsetting may apply here as explained in section 4.5)

6. Failure to complete renewal forms

Following the end of each tax year, HMRC send claimants renewal papers which seek to gather information about circumstances and income in order to finalise the year just ended and act as a claim for the new tax year. Each tax credit award is at most a tax year long. In order to ensure there is no stop in payments, HMRC continue paying ‘provisional payments’ at the start of the new tax year based on the information they held in the tax year just ended until they get up-to-date information during the renewals process.

If the renewals process is not completed (either by returning the forms to HMRC or completing the declaration over the phone) by 31 July following the end of the tax year (or another date if shown on the renewal forms), HMRC will end the provisional payments. The tax year just ended will be finalised on information held. However, as the renewals process was not completed, there is no claim for the new tax year and so all of the provisional payments made become an overpayment. Note, however, that some claimants who are are ‘auto-renewal’ cases and are not required to reply unless their income or circumstances are different from those shown on their renewal notice.

Provided the claimant contacts HMRC within 30 days of the statement of account (issued when their payments are stopped), the renewal should be completed and claim put in place back to 6 April. For renewals relating to 2009-2010, 2010-2011 and 2011-2012, the 30 days was extended to 60. After this 30-day (or 60-day) period, the claim can only be put in place from 6 April if there is good cause for missing the deadline. If that doesn’t apply, the only alternative is to make a new claim which can be backdated three months and dispute any overpayment.

7. Payments via employer (PVE)

Until February 2006, working tax credit (WTC) was often paid via employers through the payroll. An employer was allowed up to 42 days to process a change to payment of WTC. An overpayment would often accrue during the waiting period before any change was made. No new overpayments can arise in this way, but many outstanding overpayments are caused by PVE. In addition, we have seen cases where HMRC have sought recovery of an overpayment where they claim payments were made via a claimant’s employer but upon a check of payslips we have discovered the payments were never made, even though the HMRC system believes they were. It is always useful to confirm that the payments were in fact made, rather than relying on confirmation from HMRC.

2.2 Understanding overpayments

From an adviser’s perspective, one of the most difficult aspects of dealing with tax credit overpayments is identifying the cause of the overpayment.
We have set out the main causes of overpayments in section 1 and 2.1 above; however, in most cases there is more than one cause and indeed in some cases several of these causes may be present.

Most claimants have gone through the dispute process at least once before they seek advice, which can be helpful as they will generally have received a response from HMRC which gives some indication of why HMRC think there is an overpayment. In these cases the starting point is to analyse the awards for the period in question (and often earlier periods) in order to verify whether HMRC’s explanation is correct. We often find that HMRC issue explanations that are either completely wrong, do not explain the whole overpayment or identify the cause correctly but ignore evidence as to why it happened.

One of the most difficult aspects about working an overpayment case is that it is not possible to look at each tax year in isolation. So, for example, if HMRC are seeking recovery of an overpayment for 2009-2010, it could be affected by something that happened in 2007-2008 and it is therefore necessary to establish what has happened each year in order to make sense of the current overpayment.

The following points may be useful when dealing with an overpayment:

1. If HMRC have already issued a dispute response or explanation, a good starting point is to analyse that response to verify whether it is correct.
2. If there is no HMRC response or explanation, start with the year which first shows the overpayment and analyse each award notice from that year to identify any changes that may have caused the overpayment. The award notices need to be checked against the claimant’s actual circumstances. This should allow identification of any official error (e.g. computer or processing errors) as well as any claimant error.
3. If an award notice shows recovery of an earlier overpayment, it may be necessary to go back and look at earlier tax years to get a full view of whether that recovery is correct.
4. Use the intermediaries helpline (0845 300 3946). They can answer questions about awards, tell you how many awards were issued in a particular year and what information HMRC used to calculate them. This is particularly useful if the claimant has lost their paperwork. You can register as an intermediary by completing the form on the Revenuebenefits website.

2.3 Recovery of overpayments – law vs. policy

Section 28(1) Tax Credit Act 2002 sets out the law on recovery:

‘Where the amount of a tax credit paid for a tax year to a person or persons exceeds the amount of the tax credit to which he is entitled, or they are jointly entitled, for the tax year . . . the Board may decide that the excess, or any part of it, is to be repaid to the Board.’ (italics supplied).

Note that unlike the position on social security benefits, HMRC have the discretion to recovery any overpayment no matter how it was caused. To deal with this discretion, HMRC have a policy for overpayment recovery which is set out in Code of Practice 26 (COP 26).
Section 28(1) should be read in conjunction with Section 28(5), which gives HMRC power to adjust an award in-year if they detect that an overpayment is likely to arise at the end of it:

‘Where it appears to the Board that there is likely to be an overpayment of a tax credit for a tax year under an award made to a person or persons, the Board may, with a view to reducing or eliminating the overpayment, amend the award or any other award of any tax credit made to the person or persons . . .’

Under TCA 2002, Section 29(3) to (5), HMRC may recover overpayments in one of three ways:

- by deduction from any tax credit award made to the claimants (referred to as ‘ongoing’ recovery)
- by direct recovery; or
- through PAYE coding.

COP26, HMRC’s policy statement on recovery of overpayments, has been modified many times since its introduction in 2003. The current version dates April 2013. We outline the three main recovery methods below. More discussion about current recovery practice can be found in section 4.

Recovery by deduction from ongoing award

This is HMRC’s preferred method of recovery. Under the current version of COP26, there are certain limits on the amount by which payments of tax credits can be reduced in order to recover an overpayment which arose in the previous year (cross-year overpayment). Those limits, which depend upon a claimant’s income, are as follows:

- 10% of the award payment for claimants on maximum tax credits;
- 100% for claimants receiving only the family element of child tax credit; and
- 25% for all other claimants.

Sometimes HMRC will adjust an award during the award period in order to try to prevent an overpayment from accruing. In such cases the limits set out above apply to restrict recovery.

HMRC will reduce, or even stop, payment of tax credits where the claimant reports a change in circumstances or income that results in a lower entitlement, or entitlement ceasing altogether.

Potential overpayments that are identified during the award period in this way are loosely termed in-year overpayments.

In certain circumstances, HMRC will agree to reduce the recovery percentages further, or collect an overpayment over a longer period, or write off an overpayment altogether if the claimant is experiencing particular hardship (see section 4.4).
Former recovery practices

Recovery practices were not always so simple. Historically, the above limits applied only to cross-year overpayments. In-year overpayments were recovered differently. HMRC’s computer would automatically adjust the award to ensure that tax credit was paid at ‘the right amount’ for the whole year. If this caused hardship, claimants could ask for additional payments, which might prevent them from falling into poverty but prolonged the recovery of the overpayment debt into later years. Also, the initial hardship caused by the automatic 100% in-year recovery was only alleviated if the claimant asked, and knew that it was possible to ask, for additional payments.

The additional payments, where made, brought payments back up to a certain percentage of what they were before the recovery began, that percentage depending on the circumstances of the claimant. Up to and including March 2006 those percentages were:

- 10% for those on income support or jobseeker’s allowance whose child tax credit payments had fallen below 90% of what they would have received if they had not been overpaid;
- 25% for those on maximum working tax credit or child tax credit, or in receipt of a disability element in either tax credit;
- 50% for other claimants whose payments had dropped below that percentage of what they would have received if they had not been overpaid.

Additional payments were not made to those receiving only the family element of child tax credit, or to those whose award was reduced because HMRC found that ‘something was wrong’ with their claim. In addition, where an overpayment had arisen from an increase in income of more than £2,500, no additional payments were made. That latter restriction was removed with effect from 13 February 2006.

After March 2006 the percentage rates of in-year recovery were brought into line with the more generous rates applied to cross-year overpayment recovery – ie the 10%, 100% and 25% rates set out above. This was announced in a statement made by the Paymaster General to the House of Commons Treasury Sub-Committee dated 1 February 2006.

In an earlier statement made at the same time as the pre-Budget Report on 5 December 2005, the Paymaster General announced that from November 2006 in-year overpayment recovery would be subject to automatic limits set at those 10%, 25% and 100% rates. In other words, in-year overpayments would no longer be subject to 100% automatic recovery, and there would no longer be any difference between the rates of recovery of in-year and cross-year overpayments.

Both these announcements were in response to specific lobbying by LITRG and other tax and welfare rights bodies.

Then, in a further statement on 6 December 2006, the Paymaster General announced that it had not been possible for the technology to achieve the automatic limits on recovery promised for in-year overpayments from November 2006. Instead, the automatic limits would apply from April 2007; the limits would be applied manually in appropriate cases, without the claimants having to ask, from January 2007; and meanwhile HMRC remained open to requests for top-up payments from those eligible.
The fully automated limits were finally implemented during a system upgrade over the weekend of 30 June/1 July 2007.

For 2004-05 and 2005-06, where a cross-year overpayment was being collected at the 10%, 25% or 100% rate (see above), it was recovered at the same percentage from any additional payments made. Thus, if additional payments were being made at the 90% rate, and a cross-year overpayment was still being collected at 10%, the effective rate of additional payment was 81%, i.e. 90% less 10% of 90%. It is understood that this double recovery has not applied since April 2006.

The Appendix shows a table that traces the developments in the history of HMRC’s tax credit overpayment recovery since just before and after the 2005 pre-Budget report.

Direct recovery

HMRC generally recover tax credit overpayments directly like any other tax debt in two situations:

- where there is no continuing award; or
- where the claim in which the overpayment occurred has ended. For example, where there has been a change of household which has ended the previous household’s claim, and the overpayment being collected arose under the claim made by that previous household.

Direct recovery cases are dealt with by the Debt Management and Banking (DMB) arm of HMRC which is separate from the Tax Credit Office (TCO), which deals with ongoing recovery. TCO issue the initial notice to pay the overpayment and recovery is then passed to DMB to pursue. Strictly the payments are due in 30 days, but claimants can ask to repay over anything up to 10 years if their circumstances require it. DMB recently introduced a much clearer and fairer policy on recovery of direct recovery overpayments, the detail of which is set out in HMRC’s guide for intermediaries ‘How HM Revenue & Customs handle tax credits overpayments’.

More information about how HMRC pursue direct recovery cases in practice can be found in Section 4.

Recovery through PAYE coding

While provision is made in the Tax Credit Act 2002, Section 29(5) for tax credit overpayments to be collected through the PAYE system, HMRC did not use the provision until 2011 after a successful pilot. Recovery through PAYE may impact on means-tested benefits and so careful thought needs to be given if this is offered as an option by HMRC. More information about PAYE recovery can be found in Section 4.2.
SECTION 3 – CHALLENGING OVERPAYMENTS

3.1 Options for challenging overpayments

There are six options that must be considered when challenging an overpayment. The options are not mutually exclusive, therefore it may be appropriate to pursue one, two, three or all of them, depending on the circumstances of each case. The options are:

1. Appeal
2. Dispute
3. Official error
4. Complaint
5. Repayment/hardship
6. Judicial Review

We give further information about each course of action in the remainder of this section.

3.2 Appeals

The appeals process

A tax credit appeal is a formal process that allows a claimant to challenge a tax credit overpayment. Appeals are dealt with by an independent tribunal which is completely separate from HMRC. This is the First-tier Tribunal (Social Entitlement Chamber) to which most welfare benefit appeals go in the first instance. It is administered by the Tribunals Service which is an agency of the Ministry of Justice. The Tribunals Service is legally independent of HMRC and there is a specific set of rules governing the First-Tier Tribunal’s procedures.

If you are dissatisfied with the decision of the First-tier Tribunal, you can appeal further, but only on a point of law and with permission, to the Upper Tribunal (Administrative Appeals Chamber), which replaced the former Social Security and Child Support Commissioners on 11 November 2008. On matters of fact, as opposed to law, the decision of the First-tier Tribunal is nearly always final.

From the Upper Tribunal, a right of further appeal lies, again with permission and on a point of law, to the Court of Appeal, Court of Session in Scotland, or Court of Appeal in Northern Ireland.

Appealable decisions

Not all decisions by HMRC are appealable. Only those decisions set out in Section 38 Tax Credit Act 2002 carry a right of appeal:

- An initial decision on a claim for tax credit (Section 14(1));
- A revised decision on reporting a change of circumstances (Section 15(1));
- Any other revised in-year decision altering or terminating an award (Section 16(1));
- An end-of-year decision leading to a final award (Section 18(1) for reply-required cases or (6) for auto-renewal cases);
- A decision following an enquiry (Section 19(3));
- The continuation of an enquiry (appellant may ask for a direction that HMRC must give a closure notice – Section 19(9), (10);
• A decision on a discovery (s 20(1) – revision of income tax liability, or Section 20(4) – fraud or neglect of claimant or representative);
• A decision correcting an official error under regulations made under Section 21. Note there is no right of appeal against a refusal by HMRC to correct an official error;
• The determination of a penalty by HMRC (Sch 2, para 1); and
• A decision to charge interest on an overpayment (Section 37(1)).

Appeals must be made in writing to HMRC within 30 days of the date on the decision notice. It is possible to file a late appeal within 13 months of the date on the decision notice in certain circumstances. When an appeal is filed, recovery action should be suspended.

Appeals are submitted on form WTC/AP or by way of letter to the Appeals team, Tax Credit Office, Preston, PR1 4AT. When an appeal is lodged, HMRC policy is to suspend recovery of the overpayment under appeal. If the decision was made as a result of a compliance investigation the claimant should have received a letter from the compliance officer at the start of the investigation that contains a direct dial phone number. It is often useful to contact the compliance officer directly to confirm that an appeal will be forthcoming and see if further evidence can be submitted directly to them to avoid an appeal. Whilst this can sometimes be useful, care must be taken not to miss the appeal time limit.

**Decision to recover an overpayment**

One noticeable absence from the list above is a right of appeal against a decision by HMRC to recover an overpayment. Using the appeal rights above, a claimant can challenge a decision by HMRC that led to an overpayment and, if successful, that decision can be reversed establishing that there is in fact no overpayment (or it is less than the original amount).

However, if there is in fact an overpayment (the claimant has received more than their entitlement), there is no right of appeal against HMRC’s decision to recover this overpayment.

**Mandatory reconsideration before appeal**

On 3 July 2012, HMRC published a consultation document called ‘Tax Credits: mandatory revision before appeal’. HMRC sought views on the impacts of changing the tax credits appeals process to mirror the Department for Work and Pensions planned changes to their appeals process which was announced in the Welfare Reform Act 2012 and subject to a consultation between February and May 2012.

The aim of the consultation was to look at simplifying the tax credits appeals process by introducing a mandatory consideration of revision before appeal. HMRC anticipated that this would significantly reduce the number of appeals to be heard by the Courts and Tribunal Service and ensure continued alignment and consistency of treatment with the revised DWP appeals legislation and processes which DWP will be introducing.

The consultation closed in October 2012. HMRC confirmed at the November 2012 Benefits and Credits Consultation Group meeting that although the proposals in the consultation document would go ahead to mirror DWP changes, given the current delays in the tax credits appeals system they will
not be implemented from April 2013 as originally planned. Instead it will be implemented from April 2014.

*Settling an appeal with HMRC*

Once the appeal has been processed, someone at the TCO will contact you (if there is an authority in place, otherwise they will contact the claimant), usually by phone, to discuss the appeal. HMRC may agree a settlement of an appeal with you or the claimant, and that is what they generally aim to do in the first instance. Although the proposals should be considered, you do not have to settle and can choose to have the case listed with the First-tier Tribunal.

If agreement is reached, the TCO will confirm it in writing, and amend the award there and then. It is advisable to ask for the direct dial number of the appeal officer should there be any further queries and ensure that they agree to send confirmation of the outcome in writing in addition to a new award notice (on occasion TCO have been known to send only the new award notice).

If settlement is not reached, a date will be set for a hearing before the First-tier Tribunal. The claimant has the right to back out of any agreement made with the TCO under this procedure, provided TCO are told within 30 days.

More information about settlements can be found in the [HMRC technical manual](https://www.gov.uk/government/collections/tax-credit-manual).

*Appeal delays*

Due to the rapid rise in the number of compliance interventions being carried out by HMRC in trying to tackle error and fraud in the system, the number of appeals has also risen dramatically. This has caused a concerning backlog of appeals in the Tax Credit Office. It is not uncommon for compliance appeals to take several months before any contact is made with the claimant and even longer for the case to progress to the Tribunal.

HMRC do try and triage cases to ensure that people who are completely out of payment (such as those subject to undisclosed partner decisions) have their appeals dealt with quickly (within three months is the timescale). However, evidence suggests this doesn’t always happen.

In theory it is possible to ask the First-tier Tribunal directly to list the case where HMRC are acting unreasonably and delaying the appeal and there is hardship. Child Poverty Action Group have written some [guidance on dealing with delays](https://www.gov.uk/government/collections/tax-credit-manual) that covers writing to the Tribunal directly. They note that such applications are unlikely to be entertained unless there are special reasons why the case should be dealt with urgently, or there has been a significant delay.

### 3.3 The dispute process

Most challenges against overpayments will be done using the dispute process. This process is used where there is in fact an overpayment but the claimant believes that they should not pay it back because of an error by HMRC.
The dispute process is not governed by statute. Under statute, HMRC may recover all overpayments howsoever caused. HMRC set out their policy on how they exercise this discretion in Code of Practice 26. The process in COP26 is referred to as the ‘dispute process’.

The dispute process is internal to HMRC. Disputes are decided by the Customer Service and Support Group (CSSG), part of the Tax Credit Office in Preston.

In September 2009, a specialist team was set up within CSSG to deal with disputes and complaints from certain intermediaries (primarily those who provide free help to claimants). As well as creating a dedicated team, a new process was implemented which means advisers should receive an acknowledgement letter with the contact details of the named caseworker dealing with the dispute or complaint. More information on how to write to the team can be found here.

Disputes can be lodged using form TC846 or by letter (generally preferred by advisers as it allows a full argument to be put forward). Prior to 6 April 2013 there was no time limit for disputing an overpayment. From 6 April 2013, HMRC have introduced a 3 month time limit for disputes. See Section 3.7 for more detail about how the time limit works in practice.

For disputes received by HMRC prior to 15 July 2013, as soon as a claimant disputed an overpayment, whether on form TC846 or in some other written format, HMRC suspended recovery of the overpayment whilst they investigated the matter. Recovery did not recommence unless and until the dispute was resolved against the claimant and in HMRC’s favour. Thereafter, HMRC’s policy was that suspension could only be reactivated if the claimant submitted a new dispute with new evidence to HMRC which required further investigation.

HMRC changed their policy in relation to recovery suspension for disputes received from 15 July 2013. This represents a major change in policy. For disputes received after that date, there will no longer be any suspension of recovery when a dispute is lodged.

If the overpayment is being recovered from an ongoing tax credits award, that will continue whilst the dispute is considered. If the overpayment is being recovered directly via debt management and banking (DMB), they will continue recovery action whilst TCO consider the dispute.

We are not aware of any changes to the policy that if a dispute is successful, any payments made will be refunded to the claimant.

The new policy means it is crucial that claimants and their advisers engage with DMB if the debt is in direct recovery so that further action (ultimately distraint or county court) is avoided. Information about time to pay arrangements can be found in Section 4.

It is still worth speaking to DMB for direct recovery debts to request a suspension of recovery by DMB (rather than TCO). This can be requested under their official guidance where the claimant is in financial hardship or in receipt of certain means tested (see Section 4 for further details). Even if the claimant doesn’t fit this criteria it is still worth asking DMB for suspension if a dispute has been filed as even though it is not official DMB policy some officers are prepared to suspend when cases are in dispute or go to the Adjudicator.
3.4 Appeals vs. disputes

The distinction between appeals and disputes is one that even HMRC staff have difficulty with. The box below gives an example of when an appeal and dispute may be appropriate.

<table>
<thead>
<tr>
<th>APPEAL</th>
<th>DISPUTE</th>
</tr>
</thead>
<tbody>
<tr>
<td>HMRC have worked out your tax credit award incorrectly or decided that you are not entitled to tax credits or some part of tax credits and you do not agree with this.</td>
<td>HMRC have the right information about your income and situation, but for some reason you were paid more than you were entitled to have.</td>
</tr>
<tr>
<td><strong>Examples of when an “appeal” is the right thing to do:</strong></td>
<td><strong>Example of when a “dispute” is the right thing to do:</strong></td>
</tr>
<tr>
<td>Daisha claims tax credits for her three children. Her eldest child finishes her GCSEs but decides to stay on at school to do her A levels. Daisha tells HMRC and continues to receive tax credits for three children. When HMRC work out Daisha’s final tax credits for the year, they only include two children. Because Daisha received money for three children, HMRC think that they have overpaid her. Daisha can appeal the decision and ask HMRC to change her award as she should have received tax credits for three children. If this is successful, the overpayment will disappear.</td>
<td>Eric and his wife were paid tax credits for three children when they only have two. When Eric received his award notice, he phoned HMRC to tell them they had the number of children wrong. HMRC did not correct the mistake and kept on paying Eric too much tax credit. After the end of the year, Eric had received more tax credit than he should have and so has an overpayment. Eric can use the dispute process because he accepts that he has been paid too much, but doesn’t think he should have to pay it back because he told HMRC of the mistake as soon as he saw his award notice.</td>
</tr>
</tbody>
</table>

There are some important differences between the two processes:

- Appeals are a statutory process. Disputes are governed by COP26 published by HMRC that sets out how their statutory discretion is exercised.

- Appeals are dealt with initially by HMRC but proceed to an independent Tribunal outside of HMRC. Onward appeals go through the court system. This is in contrast to disputes that are decided within HMRC and further challenge is limited through the Adjudicator and Parliamentary Ombudsman.

- Appeals have a strict time limit and should be made within 30 days of the date on the decision notice. In certain circumstances you can lodge a late appeal within 13 months of the date on the decision notice. From 6 April 2013, disputes have a 3 month time limit (prior to that date there was no time limit). The time limit is explained in full in section 3.7.

- Appeals are dealt with by the appeals team in the Tax Credit Office. Disputes are handled by the Customer Service and Support Group in the Tax Credit Office.
• Appeals are filed either by letter or using form WTC/AP. Disputes can be sent either by letter or using form TC846.

• In view of the new time limit for disputes (introduced from 6 April 2013), advisers should consider Official Error if the appeal and dispute time limits have expired. See section 3.11.

• When an appeal is received by HMRC recovery of the overpayment will be suspended. From 15 July 2013 there will be no suspension of recovery for disputes.

If a claimant sends an ‘appeal’ to HMRC that should be a dispute, it will generally be re-directed. Unfortunately when the opposite happens, a claimant sends a ‘dispute’ when in fact they want to appeal, the letter tends to be treated as a dispute. In such cases we recommend that advisers argue that HMRC should treat the original letter as an appeal. There is no requirement that appeals must state that they are an ‘appeal’ so long as they meet the other appeal requirements.

3.5 The previous ‘reasonableness’ test

Prior to 31 January 2008, claimants faced the much criticised ‘reasonableness test’. This test had long been criticised by representative bodies, and following a succession of reports in 2007 by the Adjudicator, The Parliamentary Ombudsman and Citizens Advice, HMRC decided to revise the test.

The following paragraphs contain information about the operation of the reasonableness test. Whilst the test is not applicable to new cases, HMRC have stated that the test will still be used where a claimant asks HMRC to review a previous dispute decision that was made under the old test. In practice, our experience is that all current disputes are being dealt with under the new test which is generally more generous to claimants. Officially, any disputes outstanding as of 31st January 2008 should have been dealt with under the new test.

COP26 (April 2007 version) stated:

‘For us to write off an overpayment you must be able to show that the overpayment happened because:

- we made a mistake, and
- it was reasonable for you to think your payments were right.’

Both tests had to be satisfied before HMRC would write off an overpayment.

Of the two tests described above – that HMRC must have made a mistake, and that it must be reasonable for the claimant to have thought their award was right – it was the second of the two, commonly known as ‘the reasonableness test’, that provoked the most controversy.

The April 2007 version of COP26 put the section ‘Disagreeing with recovery of an overpayment’ very near the front of the document. It tended to adopt a ‘tick box’ approach to satisfying the reasonableness test, the general thrust being that if the claimant had done all they could be expected to do, and HMRC had not, then it was likely that HMRC would agree to write off the overpayment.
What was the claimant expected to do? Specifically, the claimant was required to check their award notice promptly on receiving it. As a minimum, the claimant was expected to check the following details.

- Whether the award was for an individual or for a couple. If the award was made out to a single claimant, and the claimant was a couple and in receipt of a joint award, any resulting overpayment was unlikely to be written off if the claimant did not spot and report the error.

- The hours the claimant worked. The award notice should have shown that information, and if it recorded it incorrectly, the claimant should have spotted and reported it. Simple enough in straightforward situations, though where working hours fluctuated because the claimant worked for an agency, for instance, or did shift work, this test could be more difficult to satisfy. The difficulty could be exacerbated by the absence of any clear guidance from HMRC as to how an agency or shift worker should compute their ‘normal’ working hours.

- Whether the claimant received income support or income-based jobseeker’s allowance. If they did, then they should also have received maximum tax credits. Again, this should have been an easy check to make in most situations, though where people were unfamiliar with the benefits system they may have been unsure of the difference between the income-based and contribution-based variants of jobseeker’s allowance (JSA). To add to their confusion, DWP notices did not always make it clear which variant the claimant was being paid. It was not uncommon for tax credit overpayments to arise because claimants in receipt of contribution-based JSA had been paid maximum tax credits appropriate to income-based JSA, and because of their unfamiliarity with the systems they had not spotted or reported the error. Unfamiliarity with systems (in the case of a migrant claimant) has been held to satisfy the equivalent reasonableness test in housing benefit (see CH/858/2006).

- Whether the claimant, or anyone in the claimant’s household, had a disability element. Again, confusion often arose when people were paid severe disability element (SDE) when they were only entitled to the standard disability element. It was rare for an overpayment so generated to be written off, and we have even seen a case where (initially at least) the TCO refused to write off an overpayment where a local tax office had themselves wrongly advised the claimant that she was entitled to SDE.

- The number and age of any children in the claimant’s household.

- Childcare costs. The difficulties in correctly calculating the average where there are fluctuating childcare costs need hardly be elaborated here. The important thing was to check that the figure reported to the TCO was the one that was shown on the award notice.

- Total household income for the period shown on the award notice. Again, this should reflect what the claimant reported to the TCO.

- In addition, the claimant was required to check that the amounts going into their bank account matched what was shown on the award notice. This was easier said than done in cases where the payments matched in total, but individual bank account entries did not tally with the individual payments listed on the award notice.
HMRC expected the claimant to report any incorrect information on their award notice on the day that the notice was issued. If there was a change in their circumstances or income, they were obliged again to report that to HMRC.

Given the legendary complexity and opacity of the tax credit award notice, there was surprisingly little sympathy for people who misunderstood it. They were simply expected to ask for advice, or get someone to do so on their behalf. This betrayed a complete lack of understanding of the predicament of people with a disability that made deciphering, or understanding, such material problematic, and was arguably in breach of HMRC’s own disability equality scheme.

A claimant could have been excused for failing to make these checks in exceptional circumstances – bereavement of a close relative or a serious illness were given as examples. For both claimants and advisers, the test was extremely difficult to satisfy, not helped by the seemingly inconsistent approach taken by HMRC staff in administering the test. Cases that were very similar in nature often received different outcomes and HMRC staff were notoriously bad at explaining why any decision had been made, other than to say that ‘it was not reasonable for the claimant to think their award was correct’.

3.6 The responsibilities test

The old versions of COP26 were most noticeably silent on what claimants could expect from HMRC. Whilst HMRC internal guidance gave some indication of what claimants could expect, the reasonableness test centred around the claimant and put the emphasis on them to check HMRC’s work. There seemed little responsibility for HMRC and this led to large overpayments being recovered in situations where the claimant did not spot an error which HMRC had made.

In designing the new test, HMRC attempted to move away from the one-sided list of responsibilities, replacing a test which imposed all of the responsibility on the claimant to one which set out responsibilities for both parties.

HMRC’s responsibilities

COP26 sets out the following HMRC responsibilities:

- When you contact us for information we should give you the correct advice based on the information you give us. We’ll offer you support, for example, if you want us to explain your award notice to you, we’ll talk you through it in detail.

- When you make or renew your claim we should accurately record and use the information you give us to work out your tax credits and pay you the correct amount.

- When we send you an award notice we should include information you’ve given us about your family and your income. If you tell us that there is a mistake or something missing on your award notice, we’ll put it right and send you a correct award notice.

- When you contact us to tell us about a change of circumstance we should accurately record what you’ve told us and send you a new award notice within 30 days. The 30 days doesn’t start until we get all of the information we need from you to make the change. It is therefore important that you give us all of the information when you tell us about a change.
Claimant responsibilities

HMRC have set out the following responsibilities for claimants:

- When you make or renew your claim you should give us accurate, complete and up-to-date information.

- You should tell us about any change of circumstance throughout the year so we have accurate and up-to-date information. The law says you must tell us about certain changes within one month of them happening – you should use the checklist we sent with your award notice to check what the changes are, a copy of the checklist is included with this leaflet.

  To reduce the chance of getting an overpayment, we recommend that you tell us about any changes in income as soon as possible.

- Each time you get an award notice you should use the checklist we sent with it, a copy of the checklist is included with this leaflet. You should check all the items listed and tell us if anything is wrong, missing or incomplete.

- You must tell us about some changes within one month of them happening – these are listed on the back of the checklist.

  The main details we expect you to check are:
  – whether the award is for you as an individual or as part of a couple
  – the hours you work
  – whether you get Income Support or income-based Jobseeker’s Allowance or Pension Credit
  – whether you, or anyone in your household, has a disability element
  – the number and age of any children in your household
  – childcare costs
  – your total household income for the period shown on the award notice.

  We’ll send you a corrected award notice when you tell us if anything is wrong, missing or incomplete. If you don’t get an award notice within one month of telling us about a change in circumstance please phone our Helpline as soon as possible.

- After you get any award notice you should check that the payments you get from us every week or every four weeks match the amount we said you should get on the award notice. We expect you to tell us if you got any payments that didn’t match what was shown on the award notices during the period an overpayment arose.

- If you spot a mistake on your award notice you should tell us within one month of getting your award notice. Please make a note of when you got your award notice and when you told us about the mistake. We may ask you for this information to show that you acted within one month.
There are four possible outcomes to a dispute:

<table>
<thead>
<tr>
<th>Outcome</th>
<th>Overpayment written off?</th>
<th>Explanation</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Both HMRC and the claimant have met their responsibilities.</td>
<td>NO</td>
<td>If both sides have met their responsibilities, the overpayment is likely to be a naturally occurring overpayment which is built into the system, or is caused because HMRC have 30 days to action a change.</td>
</tr>
<tr>
<td>2. HMRC have met their responsibilities but the claimant has failed to meet theirs.</td>
<td>NO</td>
<td>The overpayment is not written off because of the failure of the claimant to meet their responsibilities. This may be overridden if there are exceptional circumstances.</td>
</tr>
<tr>
<td>3. HMRC have failed to meet their responsibilities but the claimant has met theirs.</td>
<td>YES</td>
<td>The overpayment is written off in full because HMRC failed to meet their responsibilities.</td>
</tr>
<tr>
<td>4. Both HMRC and the claimant have failed to meet their responsibilities</td>
<td>PARTIALLY</td>
<td>The part of the overpayment attributable to HMRC’s failure will be written off, the part attributable to claimant error will remain recoverable unless exceptional circumstances are present.</td>
</tr>
</tbody>
</table>

There is a useful action guide which sets out the process staff follow when looking at a dispute in the tax credits manual.

Under point 4 in the summary table above, where both parties have failed in their responsibilities there will be a partial write off calculated by apportioning the part of the overpayment that is attributable to HMRC’s failure.

The guidance directs dispute staff to go on and consider four additional questions in this situation:

*Did the claimant, for overpayments in 2008-2009 onwards, report any error on their award notice within one month of receiving it?*

*Did the claimant, for overpayments prior to 2008-2009, report any award notice error promptly?*
**Did HMRC delay in processing a change of circumstances for more than 30 days?**

**Did HMRC incorrectly process a change of circumstances?**

In the first two cases, if the claimant informed HMRC within one month (or promptly for overpayments arising earlier than 2008-2009) the overpayment relating to the error on the award notice should be written off. If notification is made outside of these time limits, it would seem that the overpayment will only be written off from the date that HMRC were actually informed of the error.

In the last two cases, the part of the overpayment relating to HMRC’s error in not processing a change of circumstances within 30 days or processing a change incorrectly should be written off.

Any remaining overpayment would appear to be recoverable.

One other way of having an overpayment written off is to examine whether ‘notional offsetting’ applies if the case involves separating couples, couples coming together or one member of a couple dying or going abroad for longer than 8 or 12 weeks (depending on the circumstances). More information can be found in section 4.5.

**3.7 Time limit for disputes**

**Background**

Since the tax credits system began, most challenges of overpayments have been made through the dispute process (outlined in Section 3.3 above). Prior to 6 April 2013, there was no time limit for disputing an overpayment.

Due to the design of the award notices, it isn’t always easy to tell whether there is an overpayment and, even if there is an overpayment, to tell how much is owed. This is especially true for overpayments that occurred in the early years of the system and are still being recovered. It often isn’t until the claimant’s award ends and they receive a demand from DMB (debt management and banking - part of HMRC) that they realise that they have an overpayment, or appreciate its true extent.

Because historically there has been no limit on the time allowed to dispute an overpayment, people could still dispute an overpayment even after their award had ended, and could still be successful in getting it written off if the relevant evidence was available.

However, in order to manage the number of disputes, and get tax credits system ready for the move to Universal Credit, HMRC decided to introduce a three month time limit for disputes from 6 April 2013.

Although this is a fairly simple change in theory, the operation of the time limit is very complex. As a result, although the time limit appeared on award notices from April 2013, it was only fully implemented from October 2013.
When does the time limit run from?

As set out in COP 26, the three month time limit for disputing an overpayment runs from the date of the final award notice relating to the tax year in which the overpayment arose (but see below for overpayments from earlier years).

For people whose claims are auto-renewed the time limit runs from the date the renewal notice states a final decision will be made. For most people this will be 31 July following the end of the tax year to which the claim relates. Note that it is not the date of the renewal notice itself, but the date that it says a decision will be made.

Example 1

Dean and Sharon receive a Section 17 auto-renewal notice which is dated 14 May 2013 as they were in receipt of income based Jobseeker’s allowance for the entire 2012-2013 tax year. The notice states that if HMRC do not hear from the couple, they will confirm the amount due for 2012/13 and make a decision on entitlement for 2013/14 on 31 July 2013. Dean and Sharon have 3 months from 31 July 2013 to dispute any overpayment listed for 2012/13.

Following representations by LITRG, where an appeal is unsuccessful (or only partially successful) and any remaining overpayment then needs to be disputed, the three month time limit for the dispute will run from the date of letter telling the claimant the outcome of their appeal.

Finally, in some cases, such as where a claim is investigated by HMRC under their compliance powers, a new final award notice may be issued at the end of the investigation. If that happens, the three month time limit is activated again from the new final award notice.

Overpayments from earlier years

The time limit was introduced from 6 April 2013 and therefore it affected the finalised notices for the 2012-13 tax year. As explained above, the time limit runs from the date of the final notice relating to the tax year in which the overpayment arose. However as this is the first year of operation of the time limit, consideration needs to be given for overpayments from earlier years and how the limit will work.

For 2012-13 final award notices only, the time limit will apply to overpayments relating to the 2012-13 tax year and historic overpayments for earlier years.

In other words, claimants should dispute within three months of the 2012-13 final notice in order to challenge any 2012-13 overpayments and any overpayments from earlier years that have not already been disputed. If they do not, the chance may be lost (subject to the relaxation for some disputes between April and October 2013 described below under the heading ‘Interim arrangements from April 2013’).

Example 2

Ronnie has been overpaid during 2012-13 because HMRC did not initially process a change of circumstances that she reported. The overpayment of £1000 is shown on the final award notice dated 21 August 2013. Ronnie will have until 21 November 2013 to dispute that overpayment.
Example 3

Daniel and Hazel have been overpaid in 2012-13 by £850. They also have two overpayments from earlier years. One is from 2005-06 with £2,800 outstanding and the other from 2009-10 with £1,400 outstanding.

Their final award notice for 2012-13 is dated 3 August 2013 and shows all three overpayments.

They have until 3 November 2013 to dispute all three overpayments. Once that date has passed, HMRC’s intention is that they will lose the ability to dispute these overpayments (but see below for a relaxation of this rule in certain situations during 2013-14).

Final award notices for 2013-14 and subsequent years will only carry dispute rights against any overpayment that occurred in the year being finalised. For example, the final notice for 2013-14 will give three months to dispute any overpayment that occurred during 2013-14 but not any overpayment from 2012-13 or earlier years. The time limit for disputing those overpayments will have passed.

Example 4

Ronnie has been overpaid again during 2013-14 as HMRC did not initially process a change of circumstances that she reported. The overpayment of £2500 is shown on the final award notice dated 17 August 2014. Ronnie will have until 17 November 2014 to dispute that overpayment. She cannot dispute the overpayment that will show on the notice for the earlier year of 2012-13 (See example 2 above) as the time limit for that overpayment has expired.

Interim arrangements April to October 2013

As noted above, the time limit runs (in most cases) from the date of the final award notice for the relevant tax year. Those who are familiar with award notices will know that this is not as straightforward as it sounds.

There are two major problems with the time limit:

1. Claimants can receive several notices throughout a tax year. There will be a notice on each of them giving the claimant three months to dispute. But in reality tax credit overpayments do not crystallise until the end of the tax year, so they will still have three months from the final notice to dispute overpayments occurring in that same tax year.

Example 5

Peter and Angela have a joint tax credits claim. They receive an initial 2013-14 award notice and then two further notices after reporting changes to HMRC about their childcare costs. The couple separate in November 2013 and a potential overpayment is showing for 2013-14. The notice will say that the couple have three months to dispute that overpayment from the date of the notice, but as the claim is not yet finalised they will get another three months from their 2013-2014 final award notice to dispute the overpayment.
2. Often claimants have more than one overpayment and the overpayments can be from different years. As explained above, HMRC’s intention is to give claimants three months from the date of the 2012-13 final notice to dispute any overpayments for earlier years. The problem is that some claimants will continue to receive notices during 2013-2014 that show those earlier overpayments which will still indicate they have a further three months to dispute.

To address this second issue, interim measures were put in place between April and October 2013. If a claimant has incurred an overpayment for the 2012-13 tax year, this will be confirmed after they renew their claim. It will be shown on their 2012-13 finalised award notice which will be issued in the summer of 2013. If that is the only overpayment showing on the notice, the claimant will have three months to dispute the overpayment from the date on the final award notice.

As explained above, for 2012-13 final notices, the three month time limit will apply to overpayments that occurred in 2012-13 as well as overpayments from earlier years. For finalised award notices for 2013-14 and later years the intention is that the time limit will apply only to those overpayments occurring in the year being finalised.

Continuing the example of Daniel and Hazel (Example 3 above), the problem with this approach is that at the same time as receiving their final 2012-13 notice, Daniel and Hazel will also receive their initial 2013-14 award. If they then report any changes during the 2013-14 tax year, or if their award is recalculated for any reason, they will receive a new notice. This notice will still show the three historic overpayments (2012-13 now being a previous year overpayment along with 2005-06 and 2009-10) with a notice that says they have three months to dispute those overpayments. These notices do not reflect HMRC’s policy intention and are misleading for claimants.

As a result of representations by LITRG, HMRC have agreed that between April and October 2013, they will accept disputes from people on earlier year overpayments where they have been issued with new award notices that restate the time limit.

**Example 6**

Suppose Daniel and Hazel have another child in September 2013 and report the birth to HMRC on 5 September. A new award notice will be issued which will show their three historic overpayments and tell them they have three months to dispute from 5 September. In strict terms, the time limit for disputing those overpayments expires on 3 November 2013 (three months from their final award notice for 2012-13).

However, under a relaxation of the rules, HMRC will accept a dispute within three months of the new award notice for 2013-14, which is three months from 5 September 2013 so gives a dispute deadline of 5 December 2013.

**Example 7**

Suppose Daniel and Hazel did not report any changes to HMRC before October 2013 and so did not receive any further notices for 2013-14. In that case the three month time limit of 3 November 2013 on their 2012-13 notice would stand and they could not dispute their three historic overpayments.
LITRG believe it is essential that claimants fully understand when the time limit runs for both current and historic overpayments. Until HMRC can communicate this clearly and fully, we believe they should continue to accept disputes in cases where people have had notices that state they have three months to dispute.

Claimants with old overpayment debts

Many tax credits claimants do not realise that they have an overpayment until their claim has ended and they receive a demand from Debt Management and Banking. The volume of overpayment debt has meant that HMRC have been slow to chase claimants for old debt. In some cases, claimants have heard nothing from HMRC for a number of years. It is worth checking whether the Limitation Act 1980 might apply in particularly old cases.

Up until October 2013, where claimants received a new demand from HMRC after years of no contact, if they chose to do so they could have sent in a dispute against the overpayment.

From October 2013, HMRC have made it clear that claimants can no longer dispute old overpayments where they have not disputed within 3 months of their final award notice.

What if HMRC refuse to admit a dispute?

As explained above, the time limit is extremely complicated due to the inflexibility of the award notices and HMRC’s policy intention not matching what is actually stated on the award notices people receive.

It is crucial that advisers check award notices carefully to see whether they are interim or final notices, and to which tax year they relate.

We envisage that there may be situations where claimants have contacted the helpline to dispute an overpayment but have received incorrect advice. Or the issue may have been referred to a back office team and no dispute form been given to the claimant. In such cases, advisers should write to HMRC stating that the dispute should be admitted.

If HMRC still refuse to accept the dispute, then advisers should lodge a formal complaint (remembering that there is generally no suspension of recovery during the complaints process unless agreement can be obtained on a case by case basis from DMB).

Alternative ways to challenge the overpayment

The introduction of the three month time limit for disputes means that the statutory official error provisions become more important.

Under these provisions, an HMRC decision can be revised in favour of the claimant if it is incorrect by reason of official error – defined as an error by HMRC or DWP to which the claimant or adviser did not materially contribute. In most cases these provisions provide an avenue where the appeal time limit has passed, although in certain circumstances they can apply as an alternative to disputes.

Although these official error provisions have always existed, they are rarely used by claimants and advisers. Instead the issues often get dealt with as ‘disputes’ particularly where the time limit for an appeal has expired. For the claimant, the result of a successful challenge under the official error
provisions is that the overpayment does not have to be repaid. The two routes are different because a successful official error argument means that the award is amended so the overpayment disappears, whereas with a dispute the overpayment remains but is simply written off so the claimant does not have to repay it.

As there has been no time limit for disputes up to 5 April 2013, there was no need for claimants to specify which heading they were challenging the overpayment under.

However, now the dispute time limit has been implemented, it is important to consider whether the statutory official error provisions apply because the time limit for official error is much longer (five years) than the three months allowed for disputes and the time limit allowed for appeals. The rules relating to official error are explained in Section 3.11.

If HMRC refuse to admit a dispute because it is outside of the time limit and the appeal time limit has passed, but the case is one that fits the official error provisions, advisers should make a request under the Official Error Regulations and highlight the time limit. The complaints process can be used if HMRC continue to refuse to accept this or in serious cases Judicial Review might need to be considered.

3.8 Exceptional circumstances

The seventh step of the process for TCO advisers requires consideration of whether any ‘exceptional circumstances’ were present which prevented the claimant from meeting their responsibilities (see 2 and 4 in the summary table above).

According to the guidance exceptional circumstances do not need to be rare, and the words can simply mean ‘strong reasons’. Examples given of exceptional circumstances are the death of a close relative, serious illness, and flooding of the claimant’s home.

If exceptional circumstances are found then the overpayment that resulted from the claimants’ failure to meet their responsibilities due to exceptional circumstances should be written off.

It is not possible to list circumstances which HMRC will accept as ‘exceptional’. HMRC take a different approach in each and every case depending on the circumstances. It should be noted that the exceptional circumstances with which HMRC are concerned in this part of the test are those existing at the time when the claimant was expected to meet their responsibilities. Exceptional circumstances may also exist which mean it is more difficult for the claimant to repay an overpayment. This is discussed in section 4.7.

3.9 Evidence

One of the biggest difficulties with disputes is evidence. HMRC will often refuse to accept that a claimant has met their responsibilities if they cannot locate correspondence or telephone calls in support.

It is for this reason that we recommend that claimants keep a file with copies of all tax credit correspondence. Claimants should keep copies of all letters sent to HMRC as well as detailed notes about any telephone calls including date, time, operator name and a brief description of the conversation.
**Subject access requests (SAR)**

Sometimes called data protection requests, this is useful to obtain copies of data from HMRC including print outs of household notes (the notes that helpline operators make during telephone calls), other award information and telephone calls.

Requests should be made in writing to:

TCO SAR Team  
Group 7  
Area F  
Floor 1 St Marks House  
ST Marys Street  
Preston  
Lancs  
PR1 4AT

Prior to December 2010, advisers could write to the TCO SAR Team attaching a copy of a TC689 consent form and ask for their client’s data. Since that date, the SAR Team have sent letters to advisers stating that this is no longer possible and written permission for SAR data to be sent to an adviser must be obtained, otherwise the data will be sent directly to the claimant.

**Records of telephone calls**

*Step 8 of the HMRC staff action guide* on dealing with disputes states that telephone records should be checked if the claimant mentions a call in their dispute. In our experience HMRC do not always do this and it is therefore advisable to make it clear in any dispute that HMRC should listen to all relevant recordings and if necessary refer HMRC to their own guidance on this subject.

Unfortunately, despite HMRC repeatedly saying that all telephone calls are recorded, this is not always correct particularly in relation to the early tax credit system. In a number of cases in 2003 and 2004, calls to the helpline that were diverted to a private supplier were not always recorded. The scale of the problem was revealed in the answer to a Parliamentary question by David Laws MP on 20 February 2007 (see col 612W in Hansard for that date). The response from Benefits and Credits was:

> ‘The private sector advisers dealt mainly with generic, non-claimant specific enquiries. They received the same training as the HMRC staff to enable them to do this.’

However, it would have been very difficult to filter accurately the generic from the claimant-specific, particularly where the same call contained elements of both.

Following a campaign by LITRG and others, [tax credit officials have agreed](https://www.charteredinstitute.org.uk) that where an issue arises as to whether a claimant telephoned the helpline at that time to report a change in circumstances or a mistake in their payments, in the absence of any tape recording of the call the claimant will usually be given the benefit of the doubt, with any ensuing overpayment being written off.
3.10 Second disputes and next steps

Second disputes

If the original dispute decision is negative and the claimant has further evidence in support of the overpayment, a further (second) dispute can be sent to HMRC. During the 2013/14 tax year, HMRC introduced a time limit for secondary disputes. Claimants now only have 30 days from the letter refusing their original dispute to send any further evidence unless there are exceptional circumstances why they missed this deadline.

It is not clear whether HMRC will accept new, previously undiscovered evidence as ‘exceptional circumstances’. LITRG often see cases where a data protection request turns up evidence that HMRC staff have not used or looked at in a dispute which supports the claimant’s argument. If HMRC have not taken account of all available evidence, then advisers should argue that this counts as an exceptional circumstance.

It is advisable that this second dispute makes it absolutely clear what the further evidence is and why it changes the previous dispute decision.

In line with the new policy for original disputes, no suspension of recovery will take place whilst any second dispute is considered.

Next steps

While there are rights of appeal against awards and other decisions on tax credit entitlement, there is no statutory right of appeal against the exercise by HMRC of their discretion in relation to an overpayment recovery. That is not to say there is no legal or other remedy. If HMRC refuse a request to write off an overpayment resulting from their error, the following steps may be taken.

- Consider whether the statutory official error provisions apply (if you have not already done so). See Section 3.11.

- Make a formal complaint under HMRC’s complaint procedures. These are described in the factsheet Complaints and putting things right which supplanted Code of Practice (COP) 1 in April 2007. More information about complaints can be found below in Section 3.12.

- If the internal complaints route produces a result that is unsatisfactory to the claimant, refer the matter to the Adjudicator. The Adjudicator acts as a ‘fair and unbiased referee investigating complaints about [HMRC and certain other departments] after their own efforts to resolve matters have failed’. It is important to note that the Adjudicator cannot rewrite HMRC policy and procedure; she can only determine whether the existing policies and practices of the Department have been applied fairly.

- If the claimant is dissatisfied with the Adjudicator’s decision, the claimant’s MP can refer the matter to the Parliamentary Ombudsman whose brief is to investigate cases of maladministration by Government departments or other public bodies resulting in injustice.
Although there is no statutory right of appeal against HMRC’s exercise of their discretion, there is one judicial remedy – that of judicial review. See section 3.13 for further information.

### 3.11 Official error

This is not the 'official error' test as understood by those who have experienced tax credit overpayments due to HMRC error or delay. Official error in this context is defined as an error relating to tax credit made by:

- an officer of the Board;
- an officer of the DWP or Department for Social Development (in Northern Ireland); or
- a person providing services to any of those departments (eg the IT contractor),

to which neither the claimant nor any person acting for the claimant materially contributed.

A decision may be revised by reason of official error at any time within five years of the date of decision. Prior to 6 April 2010, the time limit was five years from the end of the tax year to which the decision related.

This is a useful alternative to an appeal where the only problem is a clear mistake in the award on which both sides can agree and which HMRC can simply correct retrospectively without the panoply of an appeal. It is also an important tool where the appeal time limit has passed and, from 6 April 2013, the dispute time limit has passed. See section 3.7 above.

There appears to be no right of appeal against a decision by HMRC not to revise the original decision under the official error rules, although there may be a possibility of judicial review action (see section 3.13 below).

There is no clear policy from HMRC on whether they will suspend recovery whilst they consider an official error request, however advisers should ensure they try and negotiate this with DMB if it is not done automatically by TCO.

Official error should be requested by writing to CSSG, Tax Credit Office, Preston PR1 4AT. Advisers need to make it clear that the request is under the official error provisions so that the dispute time limit is not incorrectly applied.

### 3.12 Complaints

*The complaints process*

Where HMRC has handled a case badly or if a dispute has failed, there is a complaints procedure which also provides for payment of compensation if a claimant has lost out financially, or suffered anxiety or distress, as a result of HMRC’s error or delay.

HMRC’s complaints procedure was originally set out in a code of practice, COP1. There have been numerous revisions of COP1 over the past few years, each one giving less information than its predecessor. The current version, which is no longer designated a code of practice, is in the form of a factsheet but, like many HMRC publications bearing that title, it is largely devoid of facts. The current factsheet version is available [here](#).

Points to note about this procedure are:
To make a complaint, write or speak to the person or office you have been dealing with, putting 'complaint' at the top of your letter if you are writing. You can also complain by fax or in person but not by email. You are asked to **tell them as much as you can about your complaint, including what went wrong, when it happened, who you dealt with, and how you would like it settled.**

- If the response of the local office is unsatisfactory, ask the office to look at your complaint again. It will be referred to a **senior officer who has not been involved**, who will **take a fresh look at it and how HMRC have handled it**, then **give you a final decision. This second review is often called a 'Tier 2 complaint'.**

- If you are not happy with the response of the senior officer, you can ask the **Adjudicator** to look into your complaint.

- If you are unhappy with the Adjudicator’s decision, you can also ask your MP to refer the matter to the **Parliamentary Ombudsman**.

One very important point about the complaints process is that HMRC policy is not to suspend recovery whilst the complaint is being dealt with even if it goes to the Adjudicator or Ombudsman. Advisers should speak to DMB to see if they are willing to suspend, in some cases they might agree, in others they may stick to their official policy. In such cases, advisers must ensure that the claimant engages with DMB so as to avoid the case continuing along the recovery route and potentially reaching county court.

**Your Charter**

HMRC’s Charter was introduced in 2009 and has statutory backing in the Finance Act 2009. Although it does not replace existing rights and remedies, it is a useful addition especially in the complaints process.

There are nine rights for claimants and three responsibilities upon claimants. The Charter can be viewed in full on the [HMRC website](https://www.hmrc.gov.uk).

When sending a complaint to HMRC, it can help to refer to the Charter, specifically identifying where HMRC have not met their obligations.

**Compensation**

If you have suffered financial loss, or particular anxiety or distress, you should consider claiming compensation.

On **financial loss**, the factsheet says that HMRC will consider refunding any reasonable costs you have had to pay as a direct result of HMRC’s mistakes or unreasonable delay. It lists, as examples, postage, phone calls, and professional fees. The former COP1 also listed under this head travelling expenses and financial charges. You should keep evidence of all such costs (receipts etc) and show them to HMRC when asked.

If the extra costs have arisen because HMRC mistakes or delays result in your receiving a late notification of a tax credit overpayment, the department may decide not to collect the full amount owed, but strict conditions apply.

On payments for worry and distress, the factsheet has this to say:

‘If you think our actions have affected you particularly badly, causing you worry or distress, tell us..."
straight away. We may be able, in some cases, to make a payment to apologise’.

The former COP1 added:

‘These payments, which are not intended to put a value on the distress you have suffered, will usually range from £25 to £500’.

Under the former COP1 there was a third head of compensation for poor complaints handling:

'If we handle your complaint badly or take an unreasonable time to deal with it, we may pay you compensation, on top of any reasonable costs, to reflect this. These payments will usually range from £25 to £500.'

That paragraph no longer appears in the factsheet but there is no reason why poor complaints handling cannot be one of the factors to be considered in determining the amount of compensation for worry and distress.

If you are negotiating compensation for yourself, you do not have to accept what HMRC offer. Look at the case studies in the Adjudicator's Annual Reports to get an idea of the kind of sums that are agreed after reference to the Adjudicator's office.

3.13 Judicial review

Although there is no statutory right of appeal against HMRC’s exercise of their discretion, there is one judicial remedy – that of judicial review, exercisable by the High Court. One advantage of this method is that the initial threat of proceedings, or failing that an application for permission, can concentrate the mind of the defendant. Another advantage is that the procedure can be expedited so that it can work much faster than other remedies. The drawback is that if the Department does not back down in the preliminary stages, going ahead with the procedure can be expensive for the claimant, even if CLS funding is obtained. It is also a specialist area where expert legal representation is required. There is a very useful basic guide to the judicial review procedure on the website of the Public Law Project.

If some kind of administrative review jurisdiction could be exercised at a lower level within the judicial structure – e.g. by a specialist tribunal more accessible to those on low incomes – access to justice in this important area would be greatly enhanced. The Tribunals, Courts and Enforcement Act 2007, which entered into force on 1 April 2009, empowers the Upper Tribunal to exercise judicial review as well as the High Court in particular types of application. Whether this will be effective in increasing access to judicial review remains to be seen.
4.1 Methods of recovery

As explained above, HMRC may recover overpayments under the TCA 2002, Section 29(3) to (5), in one of three ways:

- by deduction from any tax credit award made to the claimants (referred to as ‘ongoing’ recovery which can only take place if the same claim on which the overpayment occurred is still in payment);
- by direct recovery; or
- through PAYE coding.

It should be noted that claimants do not have a choice between ‘ongoing’ and ‘direct’ recovery. The recovery method used is determined by the circumstances of the overpayment.

If the claim on which the overpayment occurred is still in payment, ongoing recovery will be used by the Tax Credit Office. If that claim has ended, or if the claim is a ‘nil’ award (entitlement exists but no payments are due as income is too high) then HMRC will send the debt to their Debt Management and Banking arm for collection by direct recovery. This is the case even if a claim ends and then re-starts for some reason (e.g. a claimant splits with their partner, makes a single claim and gets back together making a new joint claim – the overpayment from the original joint claim cannot be recovered from the new joint claim).

It is worth noting that HMRC announced in the Autumn 2012 statement that they would be introducing new IT to allow ‘cross claim’ recovery whereby overpayments on a claim that has ended
can be recovered from a future new claim even if it is made in a different capacity (for example an overpayment from an old single claim will be recovered against a new claim as a couple). It is expected that this will commence in April 2014.

HMRC have published a guide for intermediaries online which explains how HMRC handle tax credit overpayments, including their direct recovery policies.

4.2 Direct Recovery

Direct recovery cases are dealt with by Debt Management and Banking (DMB) which is a separate arm of HMRC to the Tax Credit Office (who deal with ongoing recovery issues). DMB collect tax debt as well as tax credit debt although the processes for each are different.

HMRC revised their guidance around tax credit direct recovery cases in 2010 and their policy is much more understanding towards claimants and more generous than the previous guidance. That said, its success very much relies on its implementation by staff.

The direct recovery process

The following table gives an overview of the direct recovery process. Further detailed information can be found in the HMRC guide for intermediaries.

<table>
<thead>
<tr>
<th>STEP</th>
<th>PROCESS</th>
<th>EXPLANATION</th>
</tr>
</thead>
<tbody>
<tr>
<td>STEP 1</td>
<td>Notification of overpayment – TC610</td>
<td>When a claim ends, for whatever reason, and any overpayment is outstanding, the tax credit system will issue a TC610 notice to pay form once any appeal period has passed (normally 30 days). The TC610 advises the claimant that the amount is owed to HMRC and normally gives 42 days to pay. It advises claimants that overpayments can be spread over 12 months but does not set out any longer payment options. It encourages claimants to contact the payment helpline on 0845 302 1429. The payment helpline is part of the contact centre directorate in HMRC. A sample of the TC610 can be found on page 11 of the HMRC intermediaries guide.</td>
</tr>
<tr>
<td>STEP 2</td>
<td>Debt passed to Debt Management and Banking (DMB)</td>
<td>If no response is received to the TC610, and no dispute has been filed, the debt will be passed from the Tax Credit Office system to Debt Management and Banking’s IDMS system.</td>
</tr>
<tr>
<td>STEP 3</td>
<td>Reminder letter sent by DMB</td>
<td>A reminder letter, IDMS 99 will be sent automatically.</td>
</tr>
<tr>
<td>STEP 4</td>
<td>A further reminder letter sent by DMB.</td>
<td>If no response is received to the TC610 or the previous reminder (IDMS 99), a further letter will be sent asking for payment.</td>
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</table>
| STEP 5 | Debt Management Telephone Centre (DMTC) will attempt telephone contact | DMTC will contact the claimant to discuss the overpayment and request payment.  
If DMTC establish that the claimant cannot make a payment arrangement (based on the financial hardship criteria below) they will suspend collection for 12 months or consider remission.  
See the [HMRC intermediaries guide](#) for further information (Pg. 5) |
| STEP 6 | Personal contact | If the claimant has refused to pay in full or no contact could be made by telephone, the Debt Technical Office (DTO) will review the case to ensure the overpayment is due and also to see if any of the special rules applying to household breakdowns or dual recovery applies (see below for further information).  
If no contact can be made, it may be referred to a field officer for a visit. A payment arrangement can still be agreed at this stage. |
| STEP 7 | Legal proceedings | If no contact can be made, or the claimant refuses to make a payment arrangement, HMRC will consider referring the debt to a private debt collection agency, coding out the debt through the person’s tax code or using their distraint powers. They may also use the County Court, although distraint is their preferred approach. |

**Time to pay arrangements**

The TC610 (see Step 1 in the table above) normally gives claimants 42 days to pay the amount stated. Often in tax credit cases the amount due can be several thousands and most claimants will not be able to pay it immediately.

The TC610 informs claimants that the debt can be repaid over 12 months, but does not set out any longer payment options. Even 12 months is not long enough for most tax credit claimants with substantial overpayments.
What claimants are not told at this point is that DMB have a time to pay system that allows repayments over much longer periods.

Previously, DMB staff were instructed to ask for income/expenditure details for time to pay arrangements that lasted more than three years. Guidance, given to staff in March 2010, means that full income/expenditure details are no longer required, except if repayments will take longer than 10 years.

The following time to pay options are available:

1. **12 months**

   HMRC should readily accept an offer to repay the debt in twelve monthly instalments. No additional questions should be necessary.

2. **Over 12 months up to 10 years**

   Claimants can ask HMRC to repay over any period up to 10 years without providing full income and expenditure details. HMRC staff are instructed to follow the ‘Tax Credits Negotiating Framework’ in dealing with these requests. A copy of this is available in Section 5 of the [HMRC intermediaries guidance](#).

   Staff are encouraged to try and set up a direct debit arrangement for any time to pay agreements. Generally, repayments of less than £10 per month will not be accepted unless they will clear the debt in less than three years. If a claimant cannot afford £10 per month, then DMB should suspend recovery for twelve months and then review the situation at the end of that period. If the claimant is still unable to pay more than £10 per month following their twelve-monthly review, HMRC should consider writing off the debt on grounds of financial hardship. This new guidance does not affect time to pay arrangements already in place for less than £10 per month unless they stop for any reason.

3. **10 years or more**

   DMB staff are instructed to get a full income/expenditure breakdown where claimants request time to pay agreements that will last longer than 10 years. This is most likely to be needed where the overpayment debt is large and the claimant has a low income. As with shorter arrangements, payments of less than £10 per month will not be accepted and HMRC should suspend the debt in those cases and review after twelve months.

   If a claimant has agreed to repay over a period longer than 10 years, provided payments are made as agreed, HMRC will write off any debt remaining at the 10-year point.

   A copy of the income/expenditure form used by HMRC can be found in the [HMRC intermediaries guide](#). In assessing ability to repay, HMRC state that they will compare actual expenditure with figures produced by the Office of National Statistics and seek an explanation from the claimant where their figure is higher. This should not be done for expenditure that the claimant does not have any control over unless they appear excessive. This includes things
like rent, mortgage, secured loans, council tax, court fines, pension payments, life assurance, HP or conditional sale, TV licence, maintenance and child support.

**Other methods of recovery**

HMRC have the power to use charging orders against a claimant’s residence where a debt is owed. The current guidance states that this will not be considered in stand-alone tax credit debt cases but may be considered if there is another HMRC debt as well.

**Enforcement proceedings and debt collection agencies**

The final step in the direct recovery process involves HMRC commencing legal proceedings, normally in the county court, to obtain judgement for the debt.

Previously, HMRC’s preferred approach was to take claimants to the County Court and obtain a County Court Judgement (CCJ). However, in the last year HMRC have changed their approach and their preferred method of enforcement is distraint which involves the seizing of goods where HMRC believe the person has the means to repay but refuses.

A factsheet on distraint is available on the HMRC website. It should still be possible to negotiate a time to pay arrangement right up until the very last stage of the recovery process, although it is advisable that claimants make some attempt to discuss their case with HMRC rather than ignore the demands. If the claimants thinks they should not have to repay, a dispute can be lodged, but it may be necessary to liaise with DMB to ensure they know what is happening and try and negotiate suspension of recovery directly with them. Although official TCO policy is that they will not suspend recovery action on receipt of a dispute (policy implemented for disputes received from 15 July 2013) it is still worth asking DMB if they will suspend in such cases. If they refuses then a time to pay arrangement should be set up until the outcome of any dispute is known. This is especially important if distraint is the next step in the process.

In addition, HMRC say that they may refer the case to private Debt Collection Agencies (DCA). This approach was piloted in 2011, and in the Autumn Statement 2012 HMRC confirmed they would once again pilot payment by results using a third party DCA. Claimants will receive a final letter from HMRC urging them to make contact and agree a time to pay arrangement (over the default 12 months or longer if circumstances dictate) before the case is referred to the DCA.

Once the debt is passed to the DCA the same time to pay guidance should be followed as outlined in this section. Where a claimant asks for hardship provisions to apply or disputes the overpayment in any way, the case should be passed back to HMRC.

Although distraint and private DCA are now the preferred method of enforcement, HMRC still reserve the right to take claimants to County Court.

In the past, some claimants who were taken to county court were not given the opportunity to challenge the recovery of the overpayment or even explain if they didn’t understand why they had been overpaid. Even at this stage it is possible that HMRC have given an incorrect explanation or have made a mistake in dealing with the overpayment. Some judges treated tax credit cases in the same way as ordinary tax debt, which meant that if HMRC produced a certificate of debt that was enough to gain judgement against the claimant.
This approach is incorrect. Tax debt cases follow a special procedure called CPRPD7D meaning they do not follow the normal allocation process. Critically CPRPD7D does not apply to tax credits overpayments which basically means that the claim should follow the normal court processes including allowing the claimant to raise a defence and requiring HMRC to answer the points of that defence. A full explanation of the importance of this can be found in an article we wrote in 2008 which explains the procedure.

We still strongly caution against allowing overpayments to reach the county court, but clarification of the status of tax credit debt cases means that claimants may have an opportunity to challenge aspects of HMRC’s case. It remains far from clear how far the courts will go in examining the papers and whether they will consider the test under COP 26. On that basis we prefer to ensure cases are dealt with before proceedings are started.

From April 2012, HMRC began charging costs on cases entered in the county court in England and Wales. Alternative arrangements are in place in Scotland and Northern Ireland. Previously HMRC were unable to recover their costs in going to the county court and obtaining judgement. These changes now align HMRC’s position with that of other creditors. This change came as a result of a consultation exercise carried out between 1 July 2010 and 23 September 2010. The consultation looked at the principle of charging costs where debt cases are entered in the county court in England and Wales and judgment is awarded in their favour.

Following the consultation exercise, changes were introduced to the Ministry of Justice’s (MoJ) Civil Procedure Rules to award fixed costs to HMRC in successful court claims for recovery of tax. A summary of responses was published in January 2011.

**Recovery from DWP benefits**

The Financial Secretary to the Treasury announced, via written ministerial statement in September 2009, that a pilot would take place in 2010 to trial the recovery of HMRC tax credits and self-assessment debts from certain DWP benefits. HMRC then announced an expansion of that pilot and from 14th March 2011 they contacted around 4000 tax credits claimants and 4000 self-assessment customers with letters offering them the opportunity to join the scheme. Advisers should note that this is a voluntary scheme and claimants can choose not to take part.

HMRC have not yet confirmed whether this process will be used as part of their normal processes and no results of the extended pilot have been published.

In the Autumn Statement 2012, HMRC announced a new pilot with DWP looking at ways of recovering money where debts are owed by the same person to both HMRC and DWP.

DWP will be recovering tax credit overpayment debts from Universal Credit awards automatically.

**Recovery via PAYE tax code**

Section 29 Tax Credit Act 2002 has always contained a provision allowing HMRC to recover tax credit overpayments by adjusting the person’s tax code. The legislation states that in this respect tax credit overpayments are to be treated the same as underpayments of tax.
HMRC never used this method of recovery until 2011 when they set up a small pilot. In the earlier years of the system, HMRC prioritised debt recovery by value. Since 2009 they have moved away from this approach and used a campaigns based approach with attempts to segment the overpayment population based on behaviour and risk. As a result of this new approach, they have started to use new mechanisms for debt collection, one of which is collection via the PAYE tax code.

A change to the PAYE regulations was needed to enable debts to be collected in this way from those in PAYE employment or those in receipt of a UK-based pension. A consultation document was issued on the detailed regulations and the raising of the recovery limit to £3000. The responses to this consultation were published on the HMRC website. The regulations came into force on 20 July 2011. As a result, DMB will now identify tax credits direct recovery overpayments that are suitable for collection via an adjustment to the claimant’s PAYE tax code. This will apply to anyone in PAYE employment or in receipt of a UK-based pension who does not have an overpayment exceeding £3000. The first debts will be included in the 2012/13 code from 6 April 2012. It will continue to be used in 2013/14.

It should be noted that this method of recovery is voluntary, however HMRC will only allow the claimant to refuse if they offer to repay via another method.

The HMRC guidance explains the process as follows:

'DMB will issue a letter, to the selected customers, which explains that HMRC are considering collecting the tax credit overpayment by adjusting their tax code and increasing the amount of tax they will pay in the next tax year. The letter asks the customer to call DMB on 0845 302 1421 within 30 days, from the date of the letter, if they do not want HMRC to take this action. The customer can contact DMB to discuss an alternative method of repaying the overpayment. DMB will not be aware of other financial commitments the customer has and it may be that in some circumstances agreeing a time to pay for the tax credits overpayment is more appropriate. If the customer does not contact DMB then checks will be made to ensure a code adjustment can be made. Existing safeguards that limit the amount that can be collected through PAYE will be preserved.

In a joint household award, two people will be named in the letter. DMB will attempt to adjust the tax code of the first named person. However, if this cannot be done DMB will then attempt to adjust the tax code of the second named person. Where the code can be adjusted a form P2 Coding Notice will be sent to the customer around January / February.

If the code cannot be adjusted DMB will write to the customer and request an alternative method of repaying; normally by direct debit.

Where a couple are no longer together (Household Breakdown) DMB will not attempt to collect the overpayment by adjustment to either of their tax codes. In these circumstances DMB will expect each former partner to pay 50% of the overpayment. (But please refer to the guidance below if one former partner wants to pay more than 50%).'
The letters sent to claimants will not explain which year the debt relates to or how the debt is calculated, however a Statement of Liability should be enclosed with the letter stating the amount due. Any interest payable would be dealt with separately and not through adjusting the tax code.

- If the claimant is experiencing financial hardship, they should contact DMB immediately.
- Where there is a household breakdown during the year, coding will continue until customers contact HMRC to object and request that the coding out is cancelled.
- The existing safeguards that exist to prevent excessive deductions from salary via PAYE will still apply. In addition, there is a priority order for including sums owed to HMRC. Underpayments arising under PAYE and income tax liabilities from submission from a self-assessment return will be included in the code ahead of any debts.

The inclusion of debts in a person’s tax code means that their net pay will be reduced. If the claimant is receipt of means-tested benefits this could mean that they may receive more of the other benefits if they are based on net income. Each benefit has different rules, so care should be taken to check the position.

### 4.3 Ongoing recovery

**The ongoing recovery process**

Tax Credit Office is responsible for ongoing recovery cases. Ongoing recovery is used where the claim which gave rise to the overpayment is still in payment.

Under the current version of COP26, there are certain limits on the amount by which payments of tax credits can be reduced in order to recover an overpayment which arose in the previous year (cross-year overpayment). Those limits, which depend upon a claimant’s income, are as follows:

- 10% of the award payment for claimants on maximum tax credits;
- 100% for claimants receiving only the family element of child tax credit; and
- 25% for all other claimants.

Sometimes HMRC will adjust an award during the award period in order to try to prevent an overpayment from accruing. In such cases the limits set out above apply to restrict recovery.

HMRC will reduce, or even stop, payment of tax credits where the claimant reports a change in circumstances or income that results in a lower entitlement, or entitlement ceasing altogether. In some cases, because the above percentages above apply to in-year overpayments as well as those that go across tax years, a claimant will continue to be paid even though they have received their entitlement for the year. This will mean that their overpayment is increased. If this happens it should be clear on the award notice and the claimant can contact HMRC to request that they stop payments for the remainder of that tax year so as not to increase the overpayment any further. Recovery and payments will re-commence in the following tax year.
Potential overpayments that are identified during the award period in this way are loosely termed in-year overpayments.

Financial hardship in ongoing recovery cases

In certain circumstances, HMRC will agree to reduce the recovery percentages further, or collect an overpayment over a longer period, or write off an overpayment altogether if the claimant is experiencing particular financial hardship.

Any financial hardship in ongoing recovery cases is dealt with by the Tax Credit Office. The first step is for the claimant to contact the tax credit helpline (0345 300 3900) to ask that the recovery percentage is reduced or the overpayment is written off on hardship grounds. The helpline should refer the case to the Tax Credit Office who will make a decision on whether the recovery rate can be varied.

If the claimant receives the family element only (or family and baby element), HMRC will not normally adjust the rate of recovery. Nor will they do so if the overpayment was caused by deliberate fraud or error.

If a decision on hardship is required, TCO will pass the case to Debt Management and Banking (DMB) who will contact the claimant to check what is affordable. Once this information has been gathered, HMRC will decide whether to vary the recovery rate or remit (either fully or partially) the overpayment. The criteria used to determine this will be the same as that for direct recovery (see section 4.4 below). Once a decision has been made by DMB, they will inform TCO who will write to the claimant.

If advisers have all of the relevant information collected, they can write to the Tax Credit Office, Preston, PR1 4AT to make a request in writing.

4.4 Financial hardship

The information in this section applies to both direct and ongoing recovery cases. Some claimants will not be able to afford to make any repayments to HMRC or will only be able to offer less than £10 per month. If that is the case, there are two potential options available. The first involves getting HMRC to suspend recovery of the overpayment until the financial situation improves or, in cases where there is unlikely to be any improvement in the claimant’s financial situation, the second option is to ask HMRC to write off the debt on financial hardship grounds.

Prior to March 2010, HMRC’s policy on financial hardship was practically non-existent. It was unclear to advisers when HMRC would write off overpayments on grounds of financial hardship and very few claimants were successful when requesting this. In addition, there was no clear process for such requests which meant they were often left for months with a back office team with whom neither advisers nor claimants could make any contact.

Since March 2010, DMB has revised its approach to the recovery of tax credit overpayment debt, which includes a much clearer policy on financial hardship and also more clarity around how this should be requested.

Claimants who are unemployed with no assets or savings
In such cases, HMRC should suspend recovery for 12 months. At the end of that period, the case should be reviewed and if there is no likelihood that circumstances will improve, consideration should be given to writing off the overpayment or, at the very least, suspending it for a further 12 months. If circumstances have improved, HMRC will seek a time to pay arrangement (see above for more details).

Pensioners are not mentioned as a specific group in the new HMRC guidance; however, where a pensioner is in receipt of pension credit and there is no realistic chance that their situation will improve, we believe the same criteria should be applied.

*Claimant is on sickness/incapacity benefit*

Where a claimant is in receipt of a sickness benefit such as incapacity benefit or employment and support allowance, cannot afford to offer any repayment to HMRC and there is little prospect of them ever gaining employment, HMRC should write off the outstanding overpayment. If there is some prospect that the claimant may be able to enter employment in the future, recovery should be suspended for 12 months and the situation reviewed at the end of that period.

*Claimant unable to meet living expenses*

In situations where a claimant cannot meet essential living expenses such as water, gas and electricity, they should request that the overpayment recovery be suspended until their circumstances improve. Where there is no likelihood that this will happen, a request for the overpayment to be written off on financial hardship grounds should be made. In our experience this is most likely to succeed where evidence of their current situation is given to HMRC.

*Financial hardship process*

The above information regarding financial hardship applies to both direct recovery and ongoing recovery cases.

The process for those subject to ongoing recovery is outlined in section 4.3 above.

For those in the direct recovery process, DMB are tasked with recovering the debt and it is with them that initial contact should be made to discuss financial hardship. Specifically claimants or their advisers should contact the Debt Management Telephone Centre (DMTC) (0845 366 1206) and the case should then be referred to a Debt Technical Officer. The DTO should then assess the case based on the information received or by contacting the claimant for further information. Any letter sent to the claimant should include a phone number for the DTO dealing with the case. The claimant should be informed by letter of the outcome, regardless of whether the decision is to temporarily suspend recovery or to write off the overpayment in full.

If DMTC refuse to consider hardship or make a referral to a DTO, the HMRC intermediaries guidance on the HMRC website should be quoted and a complaint made (see section 3.12 above).

*4.5 Couples*
Couples and overpayment recovery

The law says that an overpayment debt for a couple can be collected by HMRC in full (but only once!) from either the claimant or their partner. The stated policy of HMRC where this has happened following a household breakdown is to write to both members of the former couple (making every effort to trace any former partner for whom they do not have an up-to-date address).

If the claimant believes that there should be a difference in what they and their former partner should pay, then HMRC will take into account the circumstances of both of them and may ask each of them to pay a different amount, or one of them to pay the full amount. Alternatively, they can agree between them to pay different amounts and inform HMRC of this decision.

Prior to August 2009, HMRC policy was to allow each party to repay 50% of the overpayment. However, when confirming this agreement in writing, HMRC reserved the right to return to the partner who was engaging with them for the other 50% if they could not trace the other partner.

LITRG, along with other representative bodies, expressed concern that HMRC often pursued the engaging partner with vigour whilst the other partner remained ‘untraceable’. This often meant the mother with care of the children had to repay the whole joint overpayment debt where the absent partner was difficult to trace.

Since August 2009, HMRC have implemented a much fairer policy in these situations. As before, provided a person engages with HMRC, they will allow repayment of 50% of the joint debt. Provided that this 50% is paid (either by lump sum or on a payment plan) HMRC will not pursue that person for the remaining 50%. Instead they will pursue the other partner, and if they cannot collect the money will not go back to the engaging partner to collect it.

It is important to note that the law still allows HMRC to pursue either partner for the full amount of the joint debt. Also, this process is not well advertised by HMRC, so you should ensure that you ask Debt Management and Banking if you think it applies.

Notional offsetting

Sometimes, tax credit claimants who form a couple or who become single, either because they separate or because one partner dies, are slow in reporting the change to HMRC. Yet in many cases, if they had acted promptly they would have continued to be entitled to tax credits, albeit in a different capacity.

Until 18 January 2010, HMRC would recover the whole of any overpayment arising on the old claim, but give no credit for what the claimant would have received had they made a new claim at the right time.

From 18 January 2010, HMRC introduced a new policy that means tax credits recipients who start to live together, or who become single after being part of a couple, but are late reporting the change to HMRC, can reduce the overpayment on their old claim by whatever they would have been entitled to had they made a new claim promptly.

This new policy applies to overpayments arising from 18 January 2010, but also to overpayments that were still outstanding as of that date. So, if an overpayment has been repaid in full prior to 18
January 2010, the new policy will not apply. However, if any part of it remains unpaid, offsetting can be applied to it.

To request notional offsetting, claimants should contact the tax credit helpline to ask for their case to be referred to the ‘notional offsetting (or notional entitlement)’ team in the Tax Credit Office.

Note that the notional entitlement set-off will not cover the three months by which the claimant will be able to backdate their new claim. Normally HMRC will grant the three months backdating automatically, but if that doesn’t happen, they will need to ask for it.

On the whole HMRC policy is to be lenient and not charge a penalty where the failure to report has resulted from a mistake or misunderstanding. If HMRC think the claimant has been negligent in not reporting, and they are left with a net overpayment even after notional entitlement has been applied, they may be charged a penalty against which they can appeal.

If the failure to report is dishonest, the penalty may well be substantial and in extreme cases notional entitlement will not be given.

4.6 Dual recovery

Some people will be paying back two overpayments, one via ongoing recovery and another via direct recovery. This often happens where there is an overpayment on an old claim, and a new overpayment on a current claim. Since August 2009, HMRC have implemented a new policy which means that any direct recovery action should be suspended until the ongoing recovery ends.

Whilst we welcome this policy, HMRC are not proactive in telling claimants about it. If this applies, you should ask Debt Management and Banking to suspend the direct recovery action. Further details can be found in the HMRC intermediaries guide and in the Debt Management Banking Manual Online.

4.7 Special circumstances

Cases involving mental health issues

HMRC have produced some information for cases involving claimants with mental health issues. The following is reproduced from the intermediaries guidance:

HMRC will deal with mental health cases carefully and sympathetically to avoid distress to the customer.

HMRC will need a letter from a health care professional or mental health social worker explaining the mental health problem to enable it to deal with these cases. The evidence should include the nature of the illness and as far as possible, whether the illness is likely to be long-term (for example, schizophrenia) or where the prospects for recovery are expected to be good.

If the information has not been provided HMRC will need to write to the claimant or third party asking for the documentary evidence. Only in exceptional circumstances will the evidence received be insufficient to relieve the claimant from responsibility for payment.

If the mental health problems existed at the time the overpayment occurred then Benefits and Credits can consider whether exceptional circumstances are such that writing off the overpayment is appropriate. If the mental health problems exist at the time the overpayment is being recovered then DMB will review the circumstances:
In exceptional circumstances, for example where a claimant is seriously ill or a close family member is ill, a request can be made to HMRC to suspend recovery of the overpayment until such time as the claimant is able to discuss their financial situation fully with HMRC. Claimants or their advisers should phone the debt management telephone centre (0845 3661206) to explain the situation if this applies.

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### Appendix A – HMRC manuals

HMRC publish a range of internal manuals that give more detail about their policies, processes and operations. The following manuals are relevant to tax credits:

1. **Tax credit technical manual (TCTM)**
2. **Tax credit manual (NTC)**
3. **Tax credit claimant compliance manual (CCM)**
4. **Debt management and banking manual (DMB)**

From an overpayment point of view the following parts are particularly useful:

1. **Notional offsetting**
2. **Dual recovery**
3. **Claimants with mental health issues**
4. **Cases involving domestic violence**

### Appendix B – Historical changes in tax credits recovery

<table>
<thead>
<tr>
<th>With effect from/for</th>
<th>Change</th>
<th>Source</th>
</tr>
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<tbody>
<tr>
<td>November 2005 onwards</td>
<td>Manual suspension of collection of disputed overpayments introduced</td>
<td>PMG statement to Treasury Sub-Committee, 26 October 2005</td>
</tr>
<tr>
<td>13 February 2006 onwards</td>
<td>Top-up payments offered to people whose income rises by more than £2,500 with effect from 13 February</td>
<td>PMG statement to Treasury Sub-Committee 1 February 2006</td>
</tr>
<tr>
<td>2005-07 and subsequent years</td>
<td>Annual income disregard rises from £2,500 to £25,000</td>
<td>Pre-Budget report December 2005</td>
</tr>
<tr>
<td>April 2006 onwards</td>
<td>Rates of top-up payments reflect rates at which year-end overpayments are recovered (TCTM) ongoing payments of award</td>
<td>PMG statement to Treasury Sub-Committee 1 February 2006</td>
</tr>
<tr>
<td>January 2007</td>
<td>Manual process to enable rates of recovery of in-year overpayments to be aligned with those of cross-year overpayments</td>
<td>Pre-Budget December 2006</td>
</tr>
<tr>
<td>July 2007</td>
<td>Rates of recovery of in-year overpayments aligned automatically with those of cross-year overpayments</td>
<td>Pre-Budget December 2005 as modified by pre-Budget December 2006</td>
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</tbody>
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Further guidance for cases involving claimants with mental health issues can be found in the tax credit section of the DMB manual.