House of Commons

Committee of Public Accounts

Managing debt owed to central government

Seventh Report of session 2014–15

Report, together with the formal minutes relating to the report

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Committee of Public Accounts

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Committee staff

The current staff of the Committee is Sarah Petit (Clerk), Claire Cozens (Committee Specialist), James McQuade (Senior Committee Assistant), Ian Blair and Sue Alexander (Committee Assistants) and Janet Coull Trisic (Media Officer).

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Summary

Government is owed a massive amount of money but it has failed to take a strategic cross-government approach to managing that debt and getting more money paid to the Exchequer. Failure to minimise debt impacts directly on Government borrowing. Government inaction has led to large volumes of old debts building up in departments which are unlikely to be collected. While the Treasury and the Cabinet Office say they are belatedly developing a cross-government strategy for debt, we are concerned that the centre has taken so long to drive improvements in debt collection, given that this should be a basic business activity, and given the huge volume of bad debts that are written off each year. The current climate of tight public finances must be an opportune time to make the lasting change to debt management that is needed across government. This will require prompt action to obtain repayments earlier, real co-operation across departments, better data for a more detailed understanding of debtors and their circumstances, and a more strategic approach to the use of debt collection agencies. In this way Government could ensure a more effective approach to preventing, managing and recovering debt.

Conclusions and recommendations

1. Individuals and businesses are in debt to government for overdue tax liabilities, benefits or tax credits overpayments and for other reasons, including outstanding fines and court confiscation orders. There is no official figure for the total amount owed to central government that is overdue. However, the National Audit Office estimated that overdue debt (money owed that is in arrears and legally collectable) was at least £22 billion at 31 March 2013. HM Revenue & Customs (HMRC) was owed the majority of this debt (£15.1 billion), while the Department for Work & Pensions (DWP) and the Ministry of Justice (MOJ) account for nearly all of the remainder. Debt owed to government has reduced by around £5.5 billion in the last four years. However this is a result of reductions in HMRC's balance and it disguises increases in all other major debt holding departments, and most of the debt owed is old. Responsibility for debt management lies in departments, while at the centre of government HM Treasury (the Treasury) and the Cabinet Office are expected to provide strategic oversight. Since 2011, the Fraud, Error and Debt Taskforce, an expert panel chaired by the Minister for the Cabinet Office, has been developing a cross-government view of debt management. The Cabinet Office's Efficiency and Reform Group has set out an ambition for government to save £10 billion by 2014–15 from initiatives on fraud, error and debt combined.

2. **Despite the enormous sums involved there is no central strategy for managing debt owed to government.** While the ministerial taskforce included debt in its remit in 2011 there is still no published strategy or objectives for debt management across government. Strategic management of debt is hampered by the centre not collecting figures for debt across all departments and quangos, and by the Treasury not monitoring departmental debt forecasts, effectiveness of debt collection agencies, or reviewing the risks of debt when considering new policies. This lack of attention has resulted in government's debt balances and losses being higher than necessary, and in government borrowing more as a consequence. We feel frustrated by the delay and inaction over recent years but welcome the Treasury's commitment to produce central guidance on managing debt that will encompass the recommendations made by the National Audit Office, including the suggested key performance indicators.

   Recommendation: ***The Treasury must ensure that it produces a comprehensive and effective strategy for managing debt, and related guidance, without further delay.***

3. **The Cabinet Office struggled to explain what savings it is seeking to achieve through better debt management.** The Cabinet Office set out an ambition for government to save £10 billion by 2014–15 through initiatives on fraud, error and debt combined. In the evidence session the Cabinet Office accepted that the wording of the target was confusing, but confirmed in response to detailed questioning that the debt element of the £10 billion target was to save £700 million in 2014–15 from managing debt better compared to a baseline of 2009–10. However, in subsequent written evidence the Cabinet Office stated that the £10 billion figure actually refers to "improvements between 2010–11 and the end of 2013–14 through efforts to reduce levels of fraud, error and debt, as well as improved tax compliance". We are

concerned, given the different answers we have received, that this target is unlikely to be clearly understood by those charged with delivering the savings required and will therefore fail to drive the changes needed.

Recommendation: ***The Cabinet Office should set out clearly what savings it expects both government as a whole, and individual departments and agencies, to achieve over a defined period from managing debt better.***

4. **Departments have not focused sufficiently on debt management, allowing overdue debt to accumulate and age unnecessarily, so that it becomes much more difficult to collect.** Debt has been increasing over the past six years in all departments except for HMRC. Some of this came from improvements in the amount of debt recovered, but a significant proportion was secured by writing off or deciding not to pursue £3.5 billion of tax credits debts and other debts it considers "uncollectable". A large proportion of government debt is old, with 61% of HMRC's debt and 88% of DWP's debt over 180 days old at 31 March 2013. The older the debt the more difficult it becomes to collect. Departments have different definitions of debt, the level of which is not always reported to their boards and is not set out clearly in their accounts. Some debt has sat in arms-length bodies like the Student Loans Company or Child Maintenance Enforcement Commission and is regarded simply as "terribly difficult". As a result, the treatment of debt has been characterised by neglect and periodic large write-offs or remissions. This creates unfairness and injustice in the system which damages Government's ability to collect monies due. The Treasury recognises the need for a tighter financial focus on debt, for a set of standard key performance indicators on debt management, and for more transparent reporting on debt. DWP has moved its debt operations from shared services to a core part of finance, and committed to reporting debt more transparently in its annual report and accounts.

Recommendation: ***The Treasury should ensure appropriate key performance indicators for debt management are applied across government. Departments and agencies should be required to report performance in this area to their Boards and in their annual reports and accounts.***

5. **Departments lack the information needed to target their debt collection activities and resources appropriately.** The completeness, timeliness and accessibility of data on debtors and their circumstances is generally poor across government, limiting departments' ability to tailor collection activities to individual debtors. For example, the National Audit Office reported that data on 97% of HM Courts and Tribunal Service debtors were missing one or more key fields. HMRC noted that the introduction of new "Real Time Information" systems provided accurate monthly information on people's incomes, which had resulted in more cash being collected. However, departments still do not have a 'single view' of the total amount each individual debtor owes them, let alone a single view of what an individual debtor owes to government as a whole, partly because of the barriers that remain to sharing data across central government and with local authorities. A comprehensive view of what individuals owe across government is needed to ensure debtors are treated fairly and consistently and to prevent the possibility of one department's pursuit of a debtor creating greater costs elsewhere.

Recommendation: ***Departments should implement systems that collect the data they need to manage and target their debt recovery resources effectively and reflect debtors' circumstances and ability to repay. The centre should ensure that departments share information and coordinate their debt management activities with a view to developing a single view of what each debtor owes to government as a whole.***

6. **Departments and the centre were not able to demonstrate that they had sufficient understanding of the benefits and risks of using debt collection agencies.** Departments use debt collection agencies to collect unpaid debts when they lack the capacity or specialist skills to pursue the debts. Some £1.2 billion of debt was passed to debt collection agencies on a payment by results basis in 2012–13. Debt collection agencies have collected approximately 22% of the amounts sent to them, with considerable variation according to the type of debt. They typically have retained 7% of the debt they collect as their fee. The use of debt collection agencies is set to expand significantly with the introduction of a "debt market integrator", intended to provide a single route for all government departments to access private sector debt services. The Cabinet Office and HMRC acknowledged that they were still learning how and where to make use of debt collection agencies' resources and expertise and how to ensure debt collection agencies perform effectively across the board. We were concerned about the risks of vulnerable debtors being pursued inappropriately and government transacting unwittingly with unsuitable companies. HMRC told us that debt collection agencies must comply with departmental standards, and that they would take action against any that did not meet their obligations. HMRC subsequently provided more details on the quality monitoring and compliance checks that are applied.

Recommendation: ***Departments need to be intelligent customers of debt collection agencies, and must be vigilant in monitoring agencies' performance and ensuring appropriate standards are followed in their interactions with debtors. The Cabinet Office should ensure departments are aware of the benefits and risks attached to using debt collection agencies and monitor the risk of the market being captured by a small number of suppliers.***

1 The centre's strategic approach to debt

1. On the basis of a report by the Comptroller and Auditor General we took evidence from the Cabinet Office, HM Treasury (the Treasury), HM Revenue and Customs (HMRC) and the Department of Work and Pensions (DWP) on the management of debt owed to central government.[1] Individuals and businesses are in debt to government for overdue tax liabilities, benefits or tax credits overpayments and for other reasons, including outstanding fines and court confiscation orders. There is no official figure for the total owed to central government that is overdue. However, National Audit Office data suggest that overdue debt (money owed that is in arrears and legally collectable) identified by government was at least £22 billion at 31 March 2013. HMRC was owed the majority of this debt (£15.1 billion), while DWP and MOJ were owed nearly all of the remainder. Responsibility for debt management lies in departments, while at the centre of government the Treasury and the Cabinet Office provide strategic oversight.[2]

2. The centre of government has been working to improve government debt management since 2011, when the ministerial taskforce chaired by the Minister for the Cabinet Office added debt alongside fraud and error to its remit. The Cabinet Office has encouraged a number of new pilot initiatives to improve debt management, such as funding incentives to encourage departments to collect more debt, strengthening controls around debt write-offs and remissions (when departments decide not to pursue debts, primarily on value for money grounds), use of analytics to understand better debtor behaviour, and using debt collection agencies.[3]

3. The Cabinet Office and Treasury acknowledged that they needed to take a more systematic, strategic approach to managing debt and told us that they accepted the conclusions in the National Audit Office's report. The two central departments admitted that there is still no published strategy or objectives for debt management across government, but considered that there were four guiding principles to managing debt, namely: effectiveness; efficiency; fairness and sensitivity to vulnerable debtors; and debt prevention through better policy design. The Treasury confirmed that it would be producing specific guidance for all departments on debt as part of its new consolidated budget guidance. This will set out a high-level ambition and vision for tackling debt across government.[4]

4. The Treasury acknowledged that there is no systematic measure of debt at the centre, or a record of how much debt is held or written off by all departments and quangos. The Treasury does not systematically monitor departmental debt forecasts, or focus on debt in its routine discussions with departments on spending risks.[5] The clearest example of this is the design of tax credits—HMRC acknowledged that the design had "baked in" error and fraud which then created debt. Moreover, the original design actually required HMRC to

1 C&AG's Report, Managing Debt owed to central government, HC 967 Session 2013–14, 14 February 2014

2 C&AG's Report, paragraph 1

3 Qq1, 2

4 Qq1,2, 17, C&AG's Report, paragraph 3.14

5 Qq2, 17, 87–90, 109

continue paying someone even when they owed the Revenue money.[6] The Treasury previously admitted that this was endemic to the way tax credits work.[7] Although Ministers have now agreed changes allowing payments to be stopped at an earlier stage, the effect of the original design is that tax credits debts are still being created twice as quickly as they are being collected. HMRC acknowledged that the issue would not be completely resolved until tax credits are replaced by Universal Credit. [8]

5. The Cabinet Office set out an ambition for government to save £10 billion by 2014–15 through initiatives on fraud, error and debt combined. But it was not clear to us how much of this was expected to be saved specifically by better debt management across government. In the evidence session the Cabinet Office accepted that the wording of the target was confusing, but confirmed in response to detailed questioning that the debt element of the £10 billion target was to save £700 million in 2014–15 from managing debt better compared to a baseline of 2009–10. [9] However, in subsequent written evidence the Cabinet Office stated that the £10 billion figure actually refers to "improvements between 2010–11 and the end of 2013–14 through efforts to reduce levels of fraud, error and debt, as well as improved tax compliance".[10]

6. The Cabinet Office was confident that the overall savings of £10 billion would be achieved, noting that £6.5 billion had been achieved for fraud, error and debt in 2012–13. HMRC acknowledged that the £700 million debt target was tough, but were confident that it would be achieved, principally through recovering more tax credits debt. The latest figures would be published in HMRC's 2013–14 Annual Report and Accounts. The Cabinet Office also undertook to clarify more precisely the position on achievements and targets to the Committee, following the finalisation of its 2013–14 savings figures. [11]

6 Qq59–62

7 *Whole of Government Accounts 2011–12*, Committee of Public Accounts, HC 667, 2 December 2013, paragraph 10

8 Qq59, 60, C&AG's report paragraph 2.10

9 Qq64–81, C&AG's report paragraph 2.2

10 Cabinet Office supplementary evidence to Committee, letter from Stephen Kelly to Chair, 15 May 2014

11 Qq67, 81, 100, 101, Cabinet Office supplementary evidence

2 Departmental management of debt

8. With the exception of HMRC, the amount of debt owed to government has been increasing in the past six years across departments, including an increase of £0.8 billion in DWP. The majority of debt owed to government is old, with 61% of HMRC's debt and 88% of DWP's debt over 180 days old at 31 March 2013, and over £8 billion (46%) of government debt more than one year old. HMRC is the only department to have reduced its debt balance. However, whilst there has been some improvement, a significant proportion of the fall comes from writing off or remitting £3.5 billion of tax credits debt and other debt it considers "uncollectable". HMRC told us that in 2013–14 these actions had reduced the debt that was over 18 months old by 31%.[12]

9. Overall, the management of debt owed to central government has been characterised by neglect, followed by periodic large write-offs or remissions. This has meant that government's debt balances and losses are higher than necessary, and government has to borrow more as a consequence. Tight public finances now mean that it is more important than ever that this is addressed. The Cabinet Office and Treasury acknowledged that historically debt has been a "Cinderella" issue; an operational issue not seen as "exciting" by civil servants. Accordingly, it has not been given enough priority compared to high-profile spending reform issues. Departments have different definitions of debt, it is not always reported to their boards, and it is not transparently set out in their accounts.[13] The Treasury noted that some key debt balances had been regarded as "terribly difficult" to pursue, and sat outside departments in arm's length bodies, such as the Legal Aid Agency, Child Maintenance Enforcement Commission or the Student Loans Company.[14]

10. The neglect of debt undermines policy objectives, for example by leaving fines unenforced, and creates injustice in the treatment of citizens when debts are left for a number of years. It can also allow growing balances owed to government to go unnoticed. For example, payments due from other countries for health treatment provided to their citizens in the UK, or student loans which should have been identified as eligible for repayment. [15]

11. Departments are now recognising the need for a tighter financial focus on debt. DWP reported that it was taking debt recoveries more seriously. Debt management had previously been carried out in a shared service organisation, but it was now seen as core business within the DWP finance group. DWP has established a debt management board that reports to the departmental board, and there is increasing scrutiny by Non-Executive Directors. The Department also told us that its total debt was likely to show a small decline in 2013–14—the first for at least 10–15 years. The Department committed to reporting debt more transparently in its annual report and accounts. [16]

12 Qq37, 57 C&AG's report figures 4 and 13

13 Qq19–21

14 Q48

15 Qq47, 112–115, C&AG's report figure 6

16 Qq22, 107, 118

12. The Treasury noted that it would develop a consistent measure of debt across departments and mandate the set of standard key performance indicators on debt management outlined in the National Audit Office report. The Treasury agreed with the need for more transparent reporting on debt, including debt forecasts and disclosure of material credit risks. Treasury said it would be an important part of the role of the new Director General for Spending and Finance to lead on cross-government debt management. [17]

13. The quality of data on debtors is generally poor across government, partly due to legacy IT not designed to collect the key information fields needed for debt management, and poor quality input data. This limits departments' ability to tailor collection activities to individual debtors. The National Audit Office noted that a pilot study had found that 97% of HM Courts and Tribunal Service debtor records were missing one or more key fields. Data problems can also be the consequence of process design. HMRC noted that tax credits are retrospectively assessed, with families telling HMRC what they think they are going to earn and what they think their outgoings will be. HMRC assesses tax credits on that basis, but is often unsighted on people's changing circumstances. [18]

14. HMRC and DWP highlighted the improvements offered by the new "Real Time Information" system introduced this year which will provide the departments with accurate monthly information on people's incomes, combined with greater use of telephone and digital interactions with citizens about changes in their circumstances. Using these approaches to amend payments at an earlier stage would, they believe, prevent £800 million of tax credits debt from being created in the first place. HMRC told us it was able to be proactive in challenging behaviours of people who regularly try to run behind on their tax liabilities, though it would never try to take more than it thought people could properly manage and would accept long return periods when appropriate. As a consequence of this more proactive approach debt crystallises earlier and HMRC expects its debt balance to rise again in the next year. However, the Department considered that Real Time Information had allowed it to collect an extra £5 billion of cash in 2013–14. DWP reported that it was also beginning to use HMRC's information to make earlier contact with debtors and where necessary pursue them through their employer and recover money through their earnings. [19]

15. Departments are unable to extract a 'single view' of what individual debtors owe them, let alone a view across government. DWP highlighted the importance of developing a single-customer view of the amounts owed to the Department to enable it to deal with individual debtors on a case-by-case basis, and assess how much the person is able to afford to pay back.[20]

16. Departments use debt collection agencies to provide additional capacity to chase debts they had not pursued because of low rates of return, or for a quicker follow up "to catch the

17 Qq1, 109–111, C&AG's report figure 9, HM Treasury supplementary evidence to Committee, letter from Sharon White to Chair, 15 May 2014

18 Q60, C&AG's report figure 14

19 Qq23, 27, 31, 37, 60–63

20 Qq38, 47

debt while it is fresh" with claimants known to have previous problems. Some £1.2 billion of debt was handed over to debt collection agencies in 2012–13. This represents about 1.5% of the UK's market for managed debt, so there is capacity for government to make more use of this approach. On average, in pilots, debt collection agencies had collected approximately 22% of the amount of debt allotted to them, though with considerable variation. Debt collection agencies are on payment-by-results contracts and typically charge about 7p for every £1 collected. Government is set to expand significantly the use of debt collection agencies with the new "debt market integrator", a framework contract arrangement intended to provide all government departments with a single route to access private sector debt services. Additionally, the Chancellor's Autumn Statement 2013 announced an increase in the use of debt collection agencies by HMRC, which plans to use them to collect an additional £500 million of mainly tax credits debt, which the Department considers to be a challenging target. [21]

17. The Cabinet Office and HMRC acknowledged that they were still learning how and where to make best use of debt collection agencies' skills and expertise. Departmental pilots were currently "in an exploratory period", testing the effectiveness of using debt collection agencies at different points in collections, and understanding which type of organisation is best placed to collect which type of debt.[22] The development of the "debt market integrator", should allow for more market intelligence, and enable government to be more scientific and have greater predictability in collection.[23]

18. While the use of debt collection agencies presents an opportunity to draw on resources, skills and experience from the private sector, it requires careful selection and monitoring of the providers' standards and performance. We probed departments on their due diligence processes. HMRC and DWP stated that debt collection agencies must comply with the same criteria, hardship standards and principles as their own debt management activities. They assured us that they would take action against debt collection agencies not meeting their obligations. HMRC later provided additional details, stating that it picked debt collection agencies with care and monitored and evaluated them, particularly around data security, and that it carried out checks on providers' compliance with tax and social security obligations, although EU law did not allow it to exclude non-UK domiciled companies. [24]

21 Qq3, 4–11, 12, 33, 35, 60, HMRC supplementary evidence to Committee, letter from Lin Homer to Chair, 19 May 2014, C&AG's report paragraph 2.26

22 Qq12, 31

23 Qq35, 53

24 Qq25, 49–52, HMRC supplementary evidence to Committee, letter from Lin Homer to Chair, 19 May 2014

Formal Minutes

Wednesday 9 July 2014

Members present:

Mrs Margaret Hodge, in the Chair

Mr Richard Bacon
Guto Bebb
Mr David Burrowes
Jackie Doyle-Price
Chris Heaton-Harris
Meg Hillier
Mr Stewart Jackson
Anne McGuire
Austin Mitchell
Nick Smith
John Pugh
Justin Tomlinson

Draft Report (Managing Debt Owed to Central Government), proposed by the Chair, brought up and read.

Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 18 read and agreed to.

Conclusions and recommendations agreed to.

Summary agreed to.

Resolved, That the Report be the Seventh Report of the Committee to the House.

Ordered, That the Chair make the Report to the House.

Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

[Adjourned till Monday 14 July at 3.00 pm

Witnesses

The following witnesses gave evidence. Transcripts can be viewed on the Committee's inquiry page at www.parliament.uk/pubaccom.

Wednesday 7 May 2014 *Questions*

Mike Driver, Director General, Finance, Department for Work and Pensions, Lin Homer, Permanent Secretary, HM Revenue and Customs, Stephen Kelly, Chief Operating Officer for Government, Cabinet Office, and Sharon White, Second Permanent Secretary, HM Treasury Q1–119

List of printed written evidence

The following written evidence was received and can be viewed on the Committee's inquiry web page at www.parliament.uk/pubaccom. DEB numbers are generated by the evidence processing system and so may not be complete.

1	Cabinet Office	(DEB0004)
2	Cabinet Office & HM Treasury	(DEB0005)
3	Cabot Credit Management	(DEB0006)
4	Her Majesty's Revenue And Customs	(DEB0002)
5	Treasury	(DEB0003)

List of Reports from the Committee during the current Parliament

All publications from the Committee are available on the Committee's website at www.parliament.uk/pubaccom.

The reference number of the Government's response to each Report is printed in brackets after the HC printing number.

Session 2014–15

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Third Report	Tax reliefs	HC 282
Fourth Report	Monitor: regulating NHS Foundation Trusts	HC 407
Fifth Report	Infrastructure investment: impact on consumer bills	HC 406
Sixth Report	Adult social care in England	HC 518