



Report

Date: 5 August 2016

Security Level: IN CONFIDENCE

To: Hon Anne Tolley, Minister for Social Development

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Correcting entitlements to the Accommodation Supplement

Purpose of the report

- 1 This report sets out options for addressing the historic error affecting the calculation and payment of Accommodation Supplement (AS) entitlements since 1993. This paper seeks key decisions from you, to inform the overall approach to addressing this issue. The decisions in this paper will be used to inform a paper to Cabinet on the approach to addressing the error.

Recommended actions

It is recommended that you:

1. **note** there are approximately 127,000 clients who receive or have received AS between 1993 and December 2014 who are affected by the error;

YES/NO

2. **note** this paper sets out options to correct entitlements to AS;

YES/NO

3. **note** that some of the decisions which relate to addressing the error sit within the Ministry of Social Development's (MSD's) operational discretion but are set out in the paper for your consideration and endorsement;

YES/NO

Approach to calculating entitlements

4. **note** that MSD intend to develop an automated system, underpinned by a data tool, to assess the impact of the error on AS entitlements for affected clients; and that this approach applies the same steps as a manual process, but is more efficient, less costly, and less burdensome for staff;

YES/NO

5. **note** that a net approach will be used, meaning that any overpayments clients may have received will be offset from the final lump-sum back-payment, to correct underpayments;

YES/NO

Exempting back-payments from cash asset and income tests

6. **agree** to exempt lump-sum payments, including income derived from these payments, from income and cash asset testing when assessing clients' ongoing eligibility to financial and benefit assistance for a period of 12 months from the date of payment;

AGREE/DISAGREE

7. **agree** to give effect to recommendation 6 by amending the:
- Social Security (Income and Cash Assets Exemptions) Regulations 2011;
 - Social Security (Temporary Additional Support) Regulations 2005;
 - Social Security (Long-term Residential Care) Regulations 2005; and
 - the Ministerial Direction on Special Benefit.

AGREE/DISAGREE

Process for writing off overpayments

8. **agree** that, in line with the options available under the Social Security Act 1964, MSD should not recover any overpayments of AS made to both existing and former clients given that these payments resulted from an administrative error;

AGREE/DISAGREE

9. **note** that section 86(1A)(d) of the Social Security Act 1964 allows the Minister for Social Development and the Minister of Finance to authorise the write-off of classes, descriptions, or kinds of debts (for public finance purposes);

YES/NO

10. **agree** that MSD work with Treasury to provide advice to establish overpayments of AS as a class of debt for the purposes of writing this debt off under section 86(1A)(d) the Social Security Act 1964 in early September 2016 to align with 2015/16 reporting deadlines;

AGREE/DISAGREE

Correcting entitlements for current clients (Stage One)

11. **note** that MSD has corrected rates of payment for all 94 clients that were receiving lower AS entitlements than they were entitled to;

YES/NO

12. **note** from that August 2016 MSD will commence the process for correcting entitlements for current clients who are being overpaid;

YES/NO

13. **note** that MSD will, within its operational discretion, provide clients receiving an overpayment of AS with a transition period of no more than three months (from the date they were advised of the error) in which to adjust to their correct, lower, rate of entitlement;

YES/NO

14. **note** that affected clients will be transferred to their correct rate of AS sooner if they experience a change in their circumstances during the transition period;

YES/NO

Correcting entitlements for clients affected by the error (Stage Two)

15. **agree** that lump sum payments will be made to current and former clients where they have received a net underpayment of their AS entitlements in the past;

AGREE/DISAGREE

16. **agree** that in late 2016, MSD will automatically process historic net underpayments of AS entitlements for the 22,000 people who are current clients (meaning MSD has their relevant details);

AGREE/DISAGREE

17. **agree** that former clients who may have had an underpayment of their historic AS entitlements, will need to engage with MSD in order to have their past entitlements assessed, with a view to granting any back payments that may be owed;

AGREE/DISAGREE

18. **agree** that MSD will develop a proactive communications approach to make it easy for potentially affected former clients to come forward and identify whether their past AS entitlements have been affected by the error, including the use of an online portal;

AGREE/DISAGREE

19. **note** that after six months, MSD will review the communications plan to assess the number of clients, if any, that are yet to come forward and provide advice on our ongoing approach for these clients, including whether there is a continuing need to operate the portal;

YES / NO

Financial implications

20. **note** that the negative impact of the underpayment of AS, approximately \$29m, will need to be a recognised expense against the 2015/16 year because that is when the issue was identified;

YES/NO

21. **note** that correcting the financial impact of the error will need to be reflected in the Vote: Social Development (Accommodation Assistance) appropriation which the Minister for Social Housing holds responsibility for;

YES/NO

22. **note** that the Minister for Social Housing will need to seek approval under section 26C of the Public Finance Act to remedy any unappropriated expenditure in the Benefits or Related Expenses, Accommodation Assistance for the year ended 30 June 2016;

YES/NO

23. **note** the process under section 26C of the Public Finance Act requires relevant forms to be signed by the Minister of Social Housing by 23 September 2016 in order to form part of the Appropriation (Confirmation and Validation) Bill;

YES/NO

24. **agree** that MSD officials will prepare advice for the Minister for Social Development, Minister of Finance and Minister for Social Housing in September 2016, on an approach to address the financial impacts of the error, subject to your approval of the overall approach to managing the error;

AGREE/DISAGREE

Consultation and feedback

25. **agree** that MSD prepare a draft Cabinet paper to keep your Cabinet colleagues informed of the proposed approach to correct entitlement to AS, consistent with the direction you provide on this report;

AGREE/DISAGREE

26. **agree** to forward a copy of this report to the Minister for Social Housing given the implications of the proposals in this paper on Vote: Social Development (Accommodation Assistance) and the actions which she will be required to undertake to correct entitlements to AS; and

AGREE/DISAGREE

27. **agree** to forward a copy of this report to the Associate Minister for Social Development.

AGREE/DISAGREE



Ruth Bound
Deputy Chief Executive
Service Delivery

8/8/16
Date

Hon Anne Tolley
Minister for Social Development

Date

Background

- 2 This report provides advice on an issue affecting the accuracy of payment for Accommodation Supplement (AS) that dates back to 1993. This is when AS was first introduced.
- 3 The issue is a result of an aggregation of operational processing errors that have accumulated since 1993. The error resulted from staff not updating a code for the type of accommodation clients were paying for (rent, board or mortgage) when their situation changed. The system did not provide a prompt to staff to update this code when they were updating clients' accommodation costs. When the error was identified in 2014, a system fix was put in place to prevent the same error from reoccurring.
- 4 This report provides advice on MSD's recommended approach to resolving historical under and over payments. The base assumption for this advice is that MSD will make back-payments to all clients who were underpaid and will not recover debts from clients that have been overpaid.

Scale of the number of existing and former clients affected by the issue

- 5 As at 1 June 2016, there are approximately 127,000 clients who receive, or have received, AS between 1993 and December 2014, that are affected by the error. The potential cost of underpayments to all affected clients is approximately \$29 million, while the potential cost of overpayments is around \$53 million.
- 6 The following table sets out the number of existing and former clients who have had their entitlements affected by the error, and the potential over or underpayments of AS entitlements for each of the affected groups.

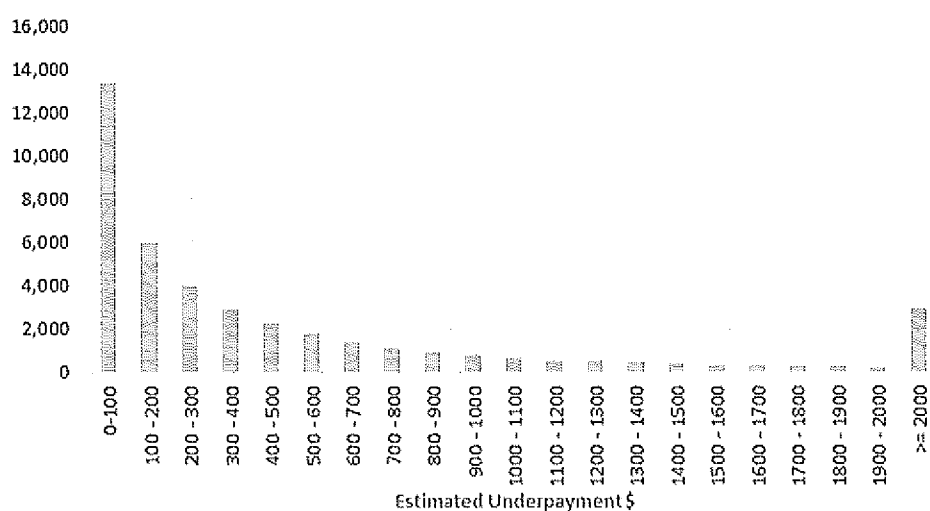
Total number of clients who had their AS entitlements affected by the error - 127,000				
Total number of affected current clients- 51,000		Total number of affected former clients- 63,000		Total number of clients that received their correct AS rate of payment, but had incorrect details - 13,000 ¹
Portion of this group potentially overpaid - 57% (29,000)	Portion of this group potentially underpaid - 43% (22,000)	Portion of this group potentially overpaid - 57% (36,000)	Portion of this group potentially underpaid - 43% (27,000)	
Total cost of overpayment for this group - \$28m	Total cost of underpayment for this group - \$14m	Total cost of overpayment for this group - \$25m	Total cost of underpayment for this group - \$15m	

- 7 The numbers in the table above differ to those in the report provided to you on 8 April 2016 [REP/16/4/324]. The difference reflects the fact that data between 1993 and 1996 is now included in the analysis, and a number of improvements have been made to the quality of the AS calculation. These are still estimates, and subject to a degree of change.
- 8 The graph below shows the distribution of the estimated underpayments for clients affected between 1996 and December 2014 (when the error was fixed). This excludes those affected between 1993-1996, due to incomplete client level data during this period. The graph highlights that a large majority of the affected clients were underpaid less than \$1,000. Around 2,800 clients were potentially underpaid \$2,000 or more, with an average underpayment of \$3,885 for these clients.

¹ There are clients who are affected by the error but continued to receive the correct AS rate because the same rate of AS would have been paid if the client was not affected by the error.

Estimated Number of Clients Underpaid

For those receiving AS prior to December 2014



MSD will use an automated calculation to determine the correct rate of AS that should have been paid to affected clients

- 9 The automated calculation will use a data tool to assess the impact of the error on entitlements for affected clients. The data tool will extract information from our SWIFTT payment system to determine:
 - the rate of AS which was paid whilst the error was affecting the client's rate of AS
 - the rate of AS which should have been paid while the error was affecting the client's rate of AS.
- 10 Using a data tool to calculate the amount of under or overpayments would achieve the same outcome as a manual assessment but is more efficient, less costly, and significantly less burdensome for staff. This is because the same logic and process would be applied for either a manual or data driven calculation.
- 11 Client level data is incomplete prior to July 1996. MSD only has snapshots of client data that were taken at least once per month, while some data is simply missing. This reduces MSD's ability to calculate the exact amount of AS which has been under or overpaid for a minority of clients. This issue exists for both a data based approach and a manual assessment.
- 12 MSD will take extra steps to provide additional assurance to the accuracy of the calculation in situations where the amount being paid is relatively high and for clients affected between 1993-1996. Additional steps will be undertaken for clients who fall into the following categories:
 - were affected between 1993-1996
 - have estimated underpayments of over \$2000
 - were also paid Special Benefit or Temporary Additional Support
 - may have already had the error corrected.
- 13 Initial estimates indicate that there may be around 30,000 clients that fall across the exceptions group set above. MSD still needs to undertake further work to determine what additional steps are most appropriate to manage risks associated with each of these groups, and how any operational impacts will be managed.

A 'net' approach to be used to calculate the lump-sum payment

- 14 There are some clients that will have received both an under and overpayment of their AS entitlements. MSD intends to apply the standard approach of issuing a 'net' rate of back-payment, also known as the net approach. A net rate means that any overpayments

affected clients may have received will be offset from the final lump-sum back-payment to correct underpayments in AS entitlements.

- 15 MSD considered applying a gross approach where it would pay the full amount of the underpayment without off-setting it against any overpayments affected clients may have received. This approach was considered in order to establish a greater degree of consistency in writing off overpayments for all clients. This is because there are some clients that received both an under and an overpayment, while others just received an overpayment or an underpayment.
- 16 On balance, MSD considers that a net approach will provide the most equitable outcome in addressing the impact of the error on clients, while also maintaining the need to be fiscally responsible. The net approach is also consistent with approaches MSD has taken in the past.
- 17 MSD seeks your endorsement to apply a net approach in determining any lump sum payment that may be owed to affected clients.

Exempting back-payments from cash asset and income tests

- 18 Clients owed back-payments will be paid a lump sum. These lump-sum back-payments, and any income derived from them, may affect eligibility or entitlement to some forms of financial assistance as they are normally treated as cash assets and income under current rules.
- 19 As the back-payments result from an MSD error, it would be unfair to penalise clients for receiving their back-payment as a lump sum. MSD recommends that all back-payments (and income derived from them) are made exempt from all forms of asset and income testing under the Social Security Act 1964 and related regulations for 12 months. The 12 month exemption period is consistent with other similar cash asset and income exemptions currently applied in the welfare system.
- 20 The alternative option to the proposed approach would be to not exempt back payments to correct for the error on AS entitlements for affected clients. MSD considers that such an approach would not be equitable on clients as lump sum payments are correcting for an administrative error outside of the clients control.
- 21 MSD seeks your approval to exempt lump-sum payments, including income derived from these payments, to correct for the AS error when assessing clients' eligibility to financial and benefit assistance for a period of 12 months from the date the lump sum is paid. The exemption is sought because these payments are being made to correct for an administrative error that is outside of the client's control.
- 22 This exemption would require an amendment to the Social Security (Income and Cash Assets Exemptions) Regulations 2011, which would need to be made in advance of the back-payments being made. Amendments would also be required to the:
 - Social Security (Temporary Additional Support) Regulations 2005
 - Social Security (Long-term Residential Care) Regulations 2005
 - Ministerial Direction in relation to Special Benefit.
- 23 Amendments to the Social Security (Income and Cash Assets Exemptions) Regulations 2011 would flow through to any cash asset and income tests for social housing. The exemptions would also cover Special Needs Grants, Advances and Recoverable Assistance Payments.
- 24 Your approval is sought to progress amendments to the regulations to implement the proposed exemption for lump sum payments made to clients affected by the error.

Writing off overpayments

- 25 As the overpayment results from an MSD error, it would be unfair to expect clients to repay any monies which they received in good faith and which occurred through no fault of their own.

- 26 MSD proposes to use the powers set out under 86(1A)(d) of the Social Security Act 1964 in respect of debts created due to the AS error. This section of the Act allows the Minister for Social Development and the Minister of Finance (Joint Ministers) to establish a class of debt that can be written off for public finance purposes.
- 27 MSD considered other approaches for the treatment of the debt associated with the AS overpayments. These are set out below:
- the application of section 86(9A) of the Act to write off the debt. This provision provides that MSD may not recover any debt caused by error if the debtor received the sum in good faith, changed his or her position in the belief they were entitled to the sum and it would be inequitable in all the circumstances, including the debtor's financial circumstances to permit recovery. However, use of section 86(9A) requires an individual assessment of the debtor's financial circumstance to be made to determine whether it would be inequitable in all the circumstances to recover the debt. Completing an individualised assessment would be administratively burdensome for MSD to compete.
 - MSD could develop new legislation that would validate the overpayments resulting from the error. However, this option would need to progress through a legislative process which would take comparatively more time to complete.
- 28 On balance, MSD recommends the option for Joint Ministers to approve a class of debt for the purposes of writing off the overpayments of AS. This approach will have the least operational impact on MSD, will provide the most efficient and practical way to address overpayments, and will provide certainty to affected clients quickest.
- 29 Your decision is sought on progressing the write off of overpayments of AS entitlements using the powers for Joint Ministers established under section 86(1A)(d) of the Social Security Act 1964. If you approve this approach, MSD and Treasury will prepare advice in August 2016 on the use of the provisions for Joint Ministers to establish a class of debt to write off the overpayments of AS as debt. Use of these provisions will require officials to draft an authorisation for the Minister of Finance and the Minister for Social Development to specify the overpayments of AS entitlements to be written off as debt.

Sequencing of remedial action

Stage one: Correcting current client's rate of payment

- 30 As MSD has already corrected the records of the 94 clients who were being underpaid, the focus of stage one will be the remaining 325 clients that continue to receive a higher rate of payment than entitled.
- 31 This will involve a face-to-face meeting with these clients where they will be advised of the impact it will have on their situation. As part of this process, case managers will assess whether these affected clients have entitlement to other assistance.
- 32 MSD will provide a three month transition period for clients who are being overpaid to allow them to adjust their circumstances ahead of their rate of payment being corrected. The Chief Executive has the discretion under the Social Security Act 1964 to provide this transition payment meaning this does not require Cabinet approval. Under this approach, clients would be transitioned to their correct rate of AS sooner, where they experience a change in their circumstances during this period.
- 33 MSD will begin to contact and work with the 325 clients receiving overpayments of AS in August 2016.

Stage two (Part A): Addressing past underpayments for current clients

- 34 There are around 22,000 clients currently in receipt of assistance from MSD who are due a back-payment. Because we have up to date contact and bank account details MSD is able to issue payments more quickly to these clients. MSD will develop a communications plan to advise these clients, including a conversation at their next appointment and/or sending a confirmation letter.

- 35 MSD will implement an automated payment solution for most clients that will generate a lump sum payment based on the amount calculated from the data model. We continue to assess how best to process clients in the exceptions category (such as the 1993-96 group).
- 36 MSD seeks your agreement to pay lump sum payments to affected existing clients that received underpayments in their historic AS entitlements from October 2016.

Stage two (Part B): Addressing past underpayments for former clients

- 37 There are around 27,000 former clients where MSD does not have up to date contact or bank account information. Back-payments for these clients will be managed through a 'come forward' approach where clients will be required to engage with MSD to identify whether their past AS entitlements may have been affected by the error.
- 38 MSD is developing a communications plan to provide advice on how potentially affected clients, no longer in receipt of any current financial assistance, will be able to check whether their historic AS entitlements were impacted by the error. Our focus is on making it as easy as possible for affected clients to come forward and test whether their historic entitlements are affected by the error. It is important to note that a number of these clients may now be deceased or living overseas, or in some cases may be in prison. MSD is working through the detail around how to address the impact of the error for former clients in these situations.
- 39 It is proposed that the communications plan includes:
- using the contact information we do have for those clients that may be current
 - working with advocacy groups and leveraging their communication channels
 - an online portal will be set up to allow clients to come forward and confirm whether their historic AS entitlement was affected by the error. Where they are affected, clients will be provided with clear instructions on the steps required to receive any back-payments they may be owed in their AS entitlements.
 - MSD is currently investigating the possibility of publishing a list of the affected clients' Social Welfare Numbers (SWN) online. Clients who may be affected would then be able to check for themselves whether their SWN appears on the list and that they have been affected by the error. MSD will consult with the Office of the Privacy Commissioner and other stakeholders such as the Beneficiary Advocates Group before publishing SWN's.
- 40 MSD proposes that the process to correct historic AS entitlements for clients who have received inaccurate AS payments as a result of the error will begin from late 2016. This timing is required in order to allow for the development of the online portal that will manage enquiries from potentially affected former clients whose past entitlements may have been impacted by the error.
- 41 After six months, MSD will review the communications plan to assess the number of clients, if any, that are yet to come forward and provide advice on our ongoing approach for these clients. This includes a review on whether the online portal will need to continue beyond six months.
- 42 To address the impact of the error on past AS entitlements for former clients, MSD seeks your endorsement that:
- potentially affected clients, who may have had an underpayment of their historic AS entitlements as a result of the error, will need to engage with MSD to have their past entitlements assessed for the purposes of granting any back payments that may be owed
 - following the assessment, lump sum payments will be made to former clients where they have received an underpayment of their AS entitlements in the past
 - use of the portal will be reviewed after six months from when it is implemented and that the review point will be used to determine whether there is an ongoing need to operate the portal.

Associated IT costs

- 43 The total associated IT cost for MSD's proposed approach to correct the error is approximately \$0.400 million. Of the total cost \$0.145 million relates to establishing the online portal function that will provide an avenue for clients not in receipt of any current assistance to come forward and identify whether their past entitlements are affected by the error.
- 44 This cost, along with any operational costs identified to implement the approach, can be met within MSD's existing baseline.

Reviews of decision

- 45 The approach MSD proposes does not preclude any client who has received AS at any point since 1993 from lodging a review of the decision.

Financial Implications

- 46 Following discussions with Audit NZ and The Treasury, it is proposed that MSD will provide for the costs of the AS payment system error in its 2015/16 Crown accounts once the final amounts are confirmed.
- 47 As the underpayments were identified in 2015/16, it needs to be recognised as an expense in that year and will have a negative impact of about \$29m on the 2015/16 operating balance before gains and losses (OBEGAL). As it is not possible to appropriate these expenses before 30 June 2016, they will need to be validated in the Appropriation (2015/16 Confirmation and Validation) Bill.
- 48 Correcting the financial impact of the error, as proposed, will need to be reflected in the Vote: Social Development (Accommodation Assistance) appropriation that the Minister for Social Housing holds responsibility for.
- 49 Approval under section 26C of the Public Finance Act will be sought to remedy any unappropriated expenditure in the Benefits or Related Expenses, Accommodation Assistance for the year ended 30 June 2016 as a result of expenses in excess of the amount of the appropriation. This process requires relevant forms to be signed by the Minister of Social Housing by 23 September 2016 and supported by a written authorisation which will be tabled in the House.
- 50 As MSD will not recover any overpayments resulting from the error (see paragraphs 25 to 29), under the generally accepted accounting practices, this will result in the fair value of the subsequent debt having a nil value in the Crown accounts. Therefore there will be no appropriation impact from writing off the debt.
- 51 MSD will prepare advice for the Minister for Social Development, Minister of Finance and Minister for Social Housing in September 2016 to address the financial and appropriation impacts of the error, subject to your approval of the overall approach set out in this paper.

Crown Law advice on the proposed approach

52 Section 9(2)(h) Legal professional privilege

53

There are a number of risks involved with correcting an error of this scale and complexity

- 54 Correcting an error of this scale and complexity inevitably involves managing a wide range of risks. Key risks that we are managing with our proposed approach are summarised below:

Risk	Action/Mitigation
The automated calculation underpinned by the data tool does not work as expected, meaning that some clients payments are calculated incorrectly	Use of exceptions and manual checks where data may be less reliable Data tool has been subject to testing
A systemic error is found in the data tool which means it cannot be relied on for calculating payments to large groups of clients	Option of using manual processes more widely where needed (though this is potentially costly where large numbers are involved)
Incomplete data from the 1993-1996 period means that some clients may receive correct payments for underpayments made during this period	
Large numbers of clients who receive payments then seek reviews of those decisions, creating significant additional work for the business	Partially mitigated by the standard three month window that applies to lodging complaints, and the fact that clients will need to produce additional information to support a claim
Large numbers of unaffected clients who have received AS seek a review of their AS entitlements, creating significant additional work for the business	Use of a portal, which will help to distinguish affected people from other people who have received AS in the past
The approach to calculating and making payments is subject to legal challenge by clients/beneficiary advocates	Elements of the proposed approach have been tested independently with Crown Law, and will continue to be as we refine the detail. Beneficiary advocates will be included in the process to develop an implementation plan, which should help to ensure their concerns are addressed
Public confidence in MSD is reduced by errors in calculating and making payments, or perceptions that MSD is not doing everything reasonably possible to 'make it right'	MSD will adopt a transparent approach to communicating what it is doing to address this issue, including what people can do if they believe that they have received an incorrect amount. The inclusion of beneficiary advocates in the development of the implementation plan should also help to build confidence.
Privacy issues raised around client information being used in the public portal	MSD plans to work with the Office of the Privacy Commissioner to determine what information can appropriately be used in the portal (e.g. client Social Welfare Numbers).
Some people may seek to make false claims for payment using other people's details	Implementation plan will include identity checks
This corrective activity impacts other Service Delivery priorities	The use of automation is intended to reduce resource impacts on MSD. Service Delivery will manage any resourcing pressures to ensure that other high priority work areas are not disrupted.

Next Steps

- 55 MSD officials propose to develop a Cabinet paper based on the decisions you make on this report. It is proposed that the Cabinet paper will set out the overall approach to addressing the error. Officials will work with your office on confirming a date for the Cabinet Social Policy Committee to consider the Cabinet paper. Officials will also provide advice in September 2016 on the use of the Joint Ministers provisions to write the overpayments of AS off as debt, as well as the financial and appropriation impacts of correcting for the error. This advice and the subsequent decisions taken by Ministers will be used to inform the Cabinet paper.