



Report

Date: 19 August 2016

Security Level: IN CONFIDENCE

To: Hon Anne Tolley, Minister for Social Development

Draft Cabinet Paper: Correcting entitlements to the Accommodation Supplement

Purpose of the report

- 1 This report provides you with the draft Cabinet paper *Correcting entitlements to the Accommodation Supplement* for your consideration and consultation with your Cabinet colleagues.

Recommended actions

It is recommended that you:

- 1 **note** you were provided with the report *Correcting entitlements to the Accommodation Supplement* [REP/16/07/701 refers] on 8 August which proposed an approach to correct entitlements to the Accommodation Supplement (AS);
YES/NO
- 2 **note** the attached draft Cabinet paper *Correcting entitlements to the Accommodation Supplement* (Appendix 1) to implement the decisions you made on the August report for your consideration and comment;
YES/NO
- 3 **agree** to consult your Cabinet colleagues on the attached draft Cabinet paper;
AGREE/DISAGREE
- 4 **note** the draft Cabinet paper has implications for the Minister of Finance:
 - 4.1 he will be required to jointly approve, with you, the establishment of a class of debt to be written-off under section 86(1A)(d) of the Social Security Act 1964; and
 - 4.2 any unappropriated expenses will be included in the Appropriation (2015/16 Confirmation and Validation) Bill;**YES/NO**
- 5 **agree** to consult the Minister of Finance on the attached draft Cabinet paper;
AGREE/DISAGREE
- 6 **note**, as the responsible Minister for the Accommodation Assistance appropriation, the Minister for Social Housing is required to certify the forms submitted under 26C of the Public Finance Act 1989 if the final paper is approved by Cabinet;
YES/NO

- 7 **agree** to consult the Minister of Social Housing on the attached draft Cabinet paper;
AGREE/DISAGREE
- 8 **indicate** if you want the final Cabinet paper *Correcting entitlements to the Accommodation Supplement* to be submitted to the Cabinet Office jointly from you and the Minister for Social Housing;
YES/NO
- 9 **note** MSD will provide a final version of the Cabinet paper on 30 August for lodging with the Cabinet Office on 1 September 2016 so it can be considered at the Social Policy Cabinet Committee on 7 September; and
AGREE/DISAGREE
- 10 **Agree** to send a copy of the report to the Associate Minister for Social Development.
AGREE/DISAGREE



Sacha O'Dea
General Manager
Working Age Policy Group

19/8/16

Date

Hon Anne Tolley
Minister for Social Development

Date

Background

- 2 This report provides the draft Cabinet paper *Correcting entitlements to the Accommodation Supplement* (Appendix 1) for your consideration and consultation with your Cabinet colleagues.
- 3 The Accommodation Supplement (AS) 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. When the error was identified in 2014, a system fix was put in place to prevent the same error from reoccurring.
- 4 On 8 August 2016 the Ministry of Social Development (MSD) provided you with the report *Correcting entitlements to the Accommodation Supplement* [REP/16/07/701 refers] which proposed an approach to correct entitlements to the AS.

Adjustments to the proposed approach since the 8 August report

- 5 Since the 8 August 2016 report, MSD has continued to develop its business processes in order to implement the proposed approach to correct entitlements to AS. This has meant that the work is managed in four phases.
- 6 The four phases are as follows:
 - Phase one: correcting entitlements for current clients who continue to be overpaid AS (~278 clients)
 - Phase two: correcting entitlements for current clients that were historically underpaid their AS entitlements (~22,000)
 - Phase three: correcting entitlements for former clients that were historically underpaid their AS entitlements (~27,000 non-current clients)
 - Phase four: debt-write off for historical overpayment of AS entitlements (29,000 current clients and 36,000 non-current clients)
- 7 The attached Cabinet paper has been drafted to reflect decisions made, and comments provided, on the August report. Consistent with your feedback regarding the proposal to publish Social Welfare Numbers (SWNs) online, and additional consultation with MSD's legal team, we have removed this proposal and refined the proposed approach to contacting non-current clients as described from paragraph 46 of the attached draft Cabinet paper.

Ministerial Consultation

- 8 The proposed approach to correct entitlements to AS will require actions by the Minister for Social Housing and the Minister of Finance. The Minister for Social Housing is responsible for the appropriation for Accommodation Assistance. Therefore, it is the Minister for Social Housing who needs to certify, under section 26C of the Public Finance Act 1989, the unappropriated Accommodation Assistance expenditure which will result from correcting entitlements to AS.
- 9 Given the Minister for Social Housing's responsibility for the Accommodation Assistance appropriation, you may wish to consider whether the attached draft Cabinet paper should come jointly from you and the Minister for Social Housing.
- 10 You and the Minister of Finance will need to jointly authorise the establishment of the AS error overpayments as a class of debt to be written off under s86(1A)(d) Social Security Act 1964.

Next steps

- 11 In order to meet the deadlines associated with the Public Finance Act, the following schedule is proposed:

Date	Action
22 – 26 August 2016	Ministerial consideration of Cabinet paper (including consultation with the Ministers of Finance and Social Housing)
31 August 2016	Final Cabinet paper to Minister for Social Development
1 September 2016	Cabinet Paper <i>Correcting entitlements to the Accommodation Supplement</i> lodged with the Cabinet Office
7 September 2016	Cabinet Social Policy Committee consideration of <i>Correcting entitlements to the Accommodation Supplement</i>
12 September 2016	Cabinet consideration of <i>Correcting entitlements to the Accommodation Supplement</i>
15 September 2016	Report to the Minister for Social Housing seeking certification of the application under section 26C of the Public Finance Act (decision required by 22 September) Report to you and the Minister of Finance to agree to create a class of debt to be written-off under section 86(1A)(d) of the Social Security Act (decision required by 25 September)
23 September 2016	Officials submit signed and certified section 26C application to the Treasury to form part of the Appropriation (2015/16 Confirmation and Validation) Bill
25 September 2016	Joint Ministerial decision (by the Minister of Finance and the Minister for Social Development) to establish a class of debt to be written-off under section 86(1A)(d) which is reflected in the Ministry of Social Development's Annual Report

Appendix

- 12 The draft Cabinet paper *Correcting entitlements to the Accommodation Supplement* is attached as Appendix 1.

File ref: SO-BE-06-16-2903

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Responsible manager: Section 9(2)(a) Policy Manager, Income Support Policy

Chair
Cabinet Social Policy Committee

CORRECTING ENTITLEMENTS TO THE ACCOMMODATION SUPPLEMENT

Proposal

- 1 This paper advises Cabinet of an issue affecting the accuracy of payment of the Accommodation Supplement which dates back to 1993. I seek Cabinet's support for the proposed approach to correct entitlements to the Accommodation Supplement for current and former clients affected by this issue.

Executive summary

- 2 The Accommodation Supplement (AS) is a weekly payment to help subsidise housing costs for low income beneficiary and non-beneficiary households with limited income and assets.
- 3 In 2014, the Ministry of Social Development (MSD) identified a significant error in its assessment and payment system that affected client entitlements for AS. The error resulted in the calculation and payment of inaccurate AS entitlements for some clients. The impact of the error meant that some affected clients received less AS than they were entitled to, while others received more. When the issue was identified, MSD took immediate action to fix the error in the payment system so that new clients would receive correct AS entitlements. This was put in place in December 2014.
- 4 While the fix to the payment system meant new clients would receive their correct AS entitlement, it did not retrospectively adjust the entitlements of current clients affected by the error. The error impacts around 127,000 existing and former clients that have received AS since 1993. Of the affected clients, MSD estimates more have been overpaid their AS entitlements than underpaid.
- 5 In order to maintain the public's trust and confidence in the social welfare system, I consider it essential to correct entitlements to AS in an equitable manner that is administratively efficient and reduces cost to clients and the Crown. My view is this is best achieved through the following phased approach:
 - 5.1 Phase one: correcting entitlements for current clients who continue to be overpaid AS (~278 clients);
 - 5.2 Phase two: correcting entitlements for current clients that were historically underpaid their AS entitlements (~22,000 current clients);
 - 5.3 Phase three: correcting entitlements for former clients that were historically underpaid their AS entitlements (~27,000 former clients); and
 - 5.4 Phase four: debt-write off for historical overpayment of AS entitlements (29,000 current clients and 36,000 former clients).

NOT GOVERNMENT POLICY – DRAFT AS AT 19 AUGUST 2016

- 6 In June 2016 MSD corrected the records of the 94 current clients who were being underpaid their AS entitlement. Therefore, the focus of phase one is on the remaining 278 clients that continue to receive a higher rate of payment than they are entitled to.
- 7 MSD [has¹] notified the 278 current clients to apologise and advise that the amount of AS the client was receiving was incorrect and has been reduced. MSD have provided a transition payment for these clients to allow them to adjust their circumstances. The Chief Executive has the delegated authority under the Social Security Act 1964 to make these payments.
- 8 Of the 49,000 current and former clients who received an underpayment of their AS entitlements, a significant majority 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. Work is currently underway to enable commencement of phases two and three from November 2016.
- 9 While the error is an operational matter, I intend to take strong oversight of the process to address the issue in order to ensure that no one receives less than their correct AS entitlements.
- 10 The total fiscal cost to correct AS entitlements for affected existing and former clients is estimated to be no more than \$29 million. Of this total amount, approximately \$14 million relates to correcting entitlements for current MSD clients that continue to receive financial support, while around \$15 million relates to clients that are no longer in receipt of financial support from MSD.
- 11 MSD does not have current contact details for those clients that are no longer in receipt of financial support. In response, MSD has developed a comprehensive communications strategy to encourage as many affected former clients as possible to enquire into their entitlement to a lump sum back-payment of AS. As a consequence of the opt-in nature of the back-payments to former clients, we expect up to \$15 million of the funds that will be appropriated to meet the costs of correcting AS entitlements will be spent.
- 12 MSD will provide for the above costs in its 2015/16 Crown accounts once the final amounts are confirmed. This will result in unappropriated expenditure under Benefits or Related Expenses, Accommodation Assistance, for the year ended 30 June 2016 as the additional expenditure will exceed the final voted appropriation prepared for the 2015/16 Supplementary Estimates. Validation by Parliament under section 26C of the Public Finance Act 1989 will be required for the excess amount of expenditure.
- 13 Receipt of back-payments of AS may affect the recipients' entitlements to social security assistance. I am of the view that the granting of back-payments (including any income derived from these payments) to correct this error should not impact on the financial circumstances of affected clients given that the issue was caused by an administrative error that is entirely outside of their control. Therefore, I propose that regulations are made under the Social Security Act 1964 to exempt the correcting payments, and any income derived from them, from being deemed income and/or cash assets for a period of 12 months after receipt.
- 14 Subject to the regulations to exempt lump sum back-payments of AS from income and cash asset testing being in effect, MSD will commence the process of correcting historic underpayments of AS for affected clients from November 2016.
- 15 I have made public statements to provide assurance that MSD will not seek to recover any overpayments of AS entitlements as a result of the error. This is to reflect that these

¹ MSD intends to notify clients before the final Cabinet paper is lodged

NOT GOVERNMENT POLICY – DRAFT AS AT 19 AUGUST 2016

payments were made as a result of an operational error and that clients received the payments in good faith. In order for MSD not to be required to recover any overpayments resulting from the error, it will seek joint ministerial authority under section 86(1A)(d) of the Social Security Act 1964 to approve the creation of a class of debt to be written-off for public finance purposes.

- 16 The fair value of a debt under generally accepted accounting practices has a nil value given the debt is not being collected. Therefore there will be no appropriation impact from writing off the debt. This will be the first time s86(1A)(d) has been used.

Background

- 17 The Accommodation Supplement (AS) is a non-taxable weekly payment which helps people with their rent, board or the cost of owning a home. AS provides a 70 per cent subsidy for housing costs that exceed 25 percent of the recipient's income (for renters or boarders) or 30 percent of the recipient's income (for homeowners), up to a set maximum amount. The payment was introduced in 1993 and is administered by the MSD.
- 18 The level of assistance provided through AS depends on the recipient's income, accommodation costs, benefit payment rate, where the recipient lives and family size. AS is a non-taxable payment that is asset tested. It is income tested for New Zealand Superannuation and Veteran's Pension recipients and for non-beneficiaries. The total cost of AS was around \$1.1 billion in 2015/16 and currently supports approximately 290,000 households.

Issue affecting the payment of the Accommodation Supplement

- 19 In 2014, MSD identified a significant error in its assessment and payment system that affected the accuracy of AS entitlements for some of its existing and former clients. The error allowed case managers, in some instances, to record inconsistent information about a client's circumstances that resulted in the payment of incorrect AS entitlements.
- 20 The issue specifically related to how a client's living circumstances were recorded in the Information Technology (IT) payment system. A key part of the assessment of clients' eligibility to AS is based on their living situation relating to whether they board, rent or pay a mortgage. The error allowed incorrect information about the client's living situation to be recorded in the IT system and resulted in the payment of inaccurate AS entitlements. This meant some of the affected clients received less AS than they were entitled to, while others received more. The payment error dates back to 1993 when AS was first introduced.
- 21 When the error was identified, immediate action was taken to correct the IT system so that AS entitlements were being paid correctly. This change ensured that any new clients being granted AS from December 2014 were receiving their correct entitlements.
- 22 Since implementing the system fix, MSD has been working to understand the scale of the issue; develop options to correct AS entitlements; and work through legal, procedural and operational implications to ensure the proposed solution is workable. Given the number of affected clients, and amount of time the error was in effect, this has been a significant piece of work.
- 23 MSD has a duty to administer the Social Security Act 1964 in accordance with the law and I am satisfied that it takes that responsibility seriously. The AS payment issue arose because of poor implementation design decisions made in 1993 rather than a technical IT system fault or policy issue. MSD have assured me they have robust quality assurance processes in place that make it very unlikely an error of this nature and scale will be repeated.

NOT GOVERNMENT POLICY – DRAFT AS AT 19 AUGUST 2016

Scale of the impact of the AS payment issue

24 In assessing the scale of the impact of the AS payment issue, MSD has had to rely on records which date back to 1993. In the period between 1993 and 2014, when the system error was in effect, there have been various changes to legislation, policy and the way records are kept. The records MSD have relied upon in undertaking this work are official records and there are no better sources of information available.

25 There are three key groups of concern that are affected by the error. These are:

- existing AS clients that continue to receive an incorrect rate of AS;
- current clients whose historic AS entitlements were affected by the error; and
- former clients whose historic AS entitlements were affected by the error.

Existing AS clients continuing to receive incorrect AS rates

26 As at 1 August 2016, there were 278 clients that were receiving an incorrect rate of payment in their AS entitlements; all of whom were receiving a higher rate of payment than they were entitled to.

Current and former clients that have past AS entitlements that were affected by the error

27 MSD advised me that, as at 1 August, there are approximately 127,000 clients who receive or have received AS between 1993 and December 2014 who are affected by the error (including the 278 identified above). The total cost of underpayments to all affected clients is up to \$29 million, while the total cost of overpayments is around \$53 million since 1993.

28 Table One sets out further detail on the number of existing and former clients who have had their entitlements affected by the error. The table also sets out the potential over or underpayments in AS entitlements for each of the affected groups.

Table One – Number of current and former clients affected by the error since 1993

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
Portion of this group overpaid – 57% (29,000)	Portion of this group underpaid – 43% (22,000)	Portion of this group overpaid – – 57% (36,000)	Portion of this group 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 ²	

29 MSD has applied a net approach to calculate the fiscal impacts of the issue. This means that in instances where a client has been subject to both overpayment and underpayment of their AS entitlements these have been offset against each other. This also means that client numbers in each category have been subject to a net approach, that is, if a client was subject

² As MSD is reliant on former clients coming forward to receive their lump sum back-payment AS entitlement, the uptake by former clients may be less than forecast. However the communications strategy described at paragraph 47 below has been designed to facilitate as many affected former clients as possible to enquire into their entitlement to a lump sum back-payment of AS.

NOT GOVERNMENT POLICY – DRAFT AS AT 19 AUGUST 2016

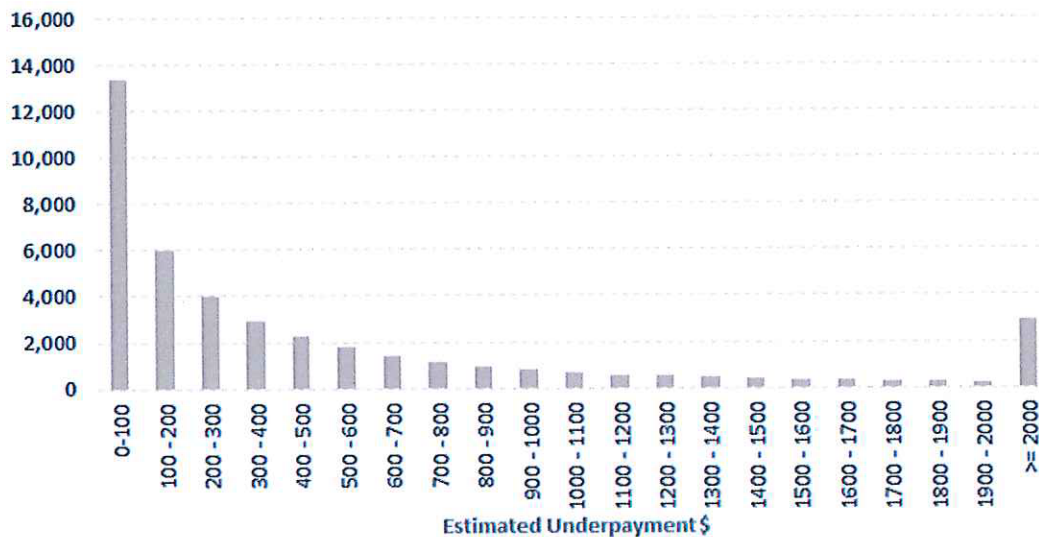
to both under and over payments then they are counted and included in the category that the net impact resulted in (e.g. either the underpayment or the overpayment category, not in both).

- 30 Graph one shows the distribution of the estimated underpayments for clients affected between 1996 (the graph excludes those affected between 1993 and 1996 – due to incomplete client level data) and December 2014 (when the error was fixed). 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.

Graph one – Distribution of the estimated underpayments for clients affected by the error between 1996 and December 2014

Estimated Number of Clients Underpaid

For those receiving AS prior to December 2014



Principles to inform response to the AS payment error issue

- 31 In order to maintain the integrity of the social welfare system, I consider it is important MSD takes appropriate steps to correct AS entitlements for those clients who received an underpayment of their AS. Affected clients were legally entitled to receive AS payments at the correct rate at the time, but did not receive their correct entitlements through any fault of their own. It is important that vulnerable families receive the entitlements they are owed
- 32 If MSD does not correct the entitlements, there is a substantial risk that MSD would receive a great number of individual requests for a review of entitlements, as was seen with the commencement date issue in 2015. This would lead to an unsustainable burden on the operational arm of MSD which could undermine the quality of service delivery in other areas.
- 33 Given the complexity and scale of the AS payment issue, I consider a systematic response is most appropriate. Therefore, MSD needs to take a fair and practical approach in addressing the impact of the error for this group.
- 34 The large number of former clients affected by the error creates a significant administrative challenge that needs to be appropriately managed.

NOT GOVERNMENT POLICY – DRAFT AS AT 19 AUGUST 2016

- 35 To support the approach to addressing the error, MSD will be using an automated calculation underpinned by a data tool to assess the impact of the error on entitlements for affected clients. The data tool takes client level data spanning the 23 year period and calculates a client's AS entitlement on a net basis.
- 36 There is no legislative basis to limit the period subject to correction. Therefore, if MSD corrects entitlements it is most appropriate to correct the entire period that the payment system error was in effect. Furthermore, a net approach works most appropriately if it is applied to the entire time period that the fault was in effect.
- 37 Consideration was given to whether MSD should solely use a manual assessment process to assess the impact of the error on clients. However, a manual process would apply most of the same steps and logic as the automated approach, but it would take much longer to complete and would be more costly. The manual process would also be open to human error.
- 38 I am of the firm view that we need to take a client centric approach in correcting the impact of the error. It is important that any approach to address this issue is administratively efficient without unfairly disadvantaging clients for an administrative error that was outside of their control.

Approach to addressing the impact of the error for affected clients

Overview of the approach

- 39 Taking into account the principles above, MSD has proposed the following phased approach to resolve the AS issue:
- 39.1 Phase one: correcting entitlements for current clients who continue to be overpaid AS (278 current clients);
- 39.2 Phase two: correcting historic entitlements for current clients that were underpaid their AS entitlements (~22,000 current clients),
- 39.3 Phase three: correcting historic entitlements for former clients that were underpaid their AS entitlements (~27,000 former clients), and
- 39.4 Phase four: debt-write off for historical overpayment of AS entitlements (29,000 current clients and 36,000 former clients).
- 40 While the AS payment error is an operational matter, I intend to take strong oversight of this issue to ensure that no individual receives less than their entitlements.

Phase one: correcting entitlement for current clients who continue to be overpaid AS

- 41 My first priority has been to ensure that all current clients receive their correct AS entitlements. The fix to the payment system in December 2014 was designed to prevent the same error occurring for any new clients receiving AS entitlements. However, the system did not retrospectively correct the entitlements of clients who were already receiving AS at the point the fix to the system was put in place. This meant there was a portion of clients that were not receiving their correct AS entitlements. Some of these clients were being underpaid, while others were being overpaid.
- 42 In June 2016, MSD updated and corrected AS entitlements for the 94 clients who were receiving lower rates of AS than they were entitled to.

NOT GOVERNMENT POLICY – DRAFT AS AT 19 AUGUST 2016

- 43 There are approximately 278 clients who continue to receive a higher rate of AS than they are entitled to. I recognise that many of these affected clients will have established their household budgets around the rate of AS entitlements they are currently receiving. Reducing AS to those clients receiving overpayments is likely to have some impact on the budgets of these households.
- 44 MSD has notified the 278 current clients to apologise, and advised that the amount of AS the client was receiving was incorrect, and has been reduced. MSD have provided a transition payment for these clients to allow them to adjust their circumstances. The Chief Executive has the delegated authority under the Social Security Act 1964 to make these payments.

Phase two: correcting historic entitlements for current clients that were underpaid their AS entitlements

- 45 The second phase will focus on correcting underpayments for current MSD clients (22,000) that are continuing to receive financial support. Addressing the impact of the error for current clients will be administratively easier as MSD already engages with and holds current details for individuals in this group. Generally, MSD will be able to automatically process any underpayments that are owed to these current clients. The total cost of correcting underpayment to this group is approximately \$14 million. Steps to correct entitlements for this group will start from November 2016 and will be completed before Christmas.

Phase three: correcting historic entitlements for former clients that were underpaid their AS entitlements

- 46 The next phase is to correct AS entitlements for former clients who historically received an underpayment (~27,000). The total cost of correcting underpayments to this group is approximately \$15 million. Addressing the error for these clients is more complex as MSD do not have current contact details for clients who are no longer in receipt of a benefit and there are privacy risks associated with sending personal information to a last known address.
- 47 However, in order to facilitate greater uptake by former clients who may be entitled to a lump sum back-payment of AS, MSD has developed a comprehensive communications strategy to inform these people. MSD will use its existing channels of engagement with stakeholders to communicate the error. This will include stakeholder engagement with beneficiary advocates and organisations such as Citizens' Advice Bureaux, social services agencies, disabled people's organisations and Age Concern.
- 48 An online portal will be established that will allow potentially affected former clients to identify whether their past entitlements are affected by the error. The portal will require the client to provide current details like a postal address and bank account number. If the former client is impacted, MSD will then be able to pay them their lump sum back-payment of AS entitlement.
- 49 It is intended that the online portal will be functional from late 2016. Where affected former clients do not have their own internet access or have difficulty using computers, they will be able to use the portal in MSD service centres and be supported by staff as necessary. Use of the portal will be reviewed after six months from when it is implemented. This review point will be used to determine whether there is an ongoing need to operate the portal.
- 50 As a consequence of the opt-in nature of the back-payments to former clients we expect up to \$15 million, which is to be appropriated to meet the costs of correcting AS entitlements, will be spent.

NOT GOVERNMENT POLICY – DRAFT AS AT 19 AUGUST 2016

- 51 It is important to note that there is likely to be some fluidity between those individuals that fit within phase two and three, given that clients' circumstances are subject to change.

Phase four: debt write-off for historical overpayment of AS entitlements (29,000 current clients and 36,000 former clients)

- 52 I have publicly stated that MSD will not be recovering any overpayments of AS that resulted from the error. I am of the view that no current or former client should have their circumstances affected as a result of an administrative error that was outside of their control.

- 53 There are two key issues that need to be addressed in relation to the treatment of overpayments. The first issue relates to the process by which the overpayments are written off to satisfy the requirements of the Social Security Act 1964. The second issue relates to the accounting treatment of the overpayments on the relevant appropriations to satisfy the requirements of the Public Finance Act 1989.

Process for writing off the overpayments

- 54 Alongside addressing the appropriation impact of the error, steps also need to be taken to formally write off the overpayment as a debt under the Social Security Act. Section 86(1A)(d) of the Social Security Act 1964 empowers the Minister for Social Development and the Minister of Finance jointly to give a written authorisation to establish a class of debt that is to be written off for public finance purposes.
- 55 MSD, in consultation with the Treasury, will draft an authorisation to establish a class of debt to be written off for the Minister of Finance and the Minister for Social Development. This will be the first time the power to establish a class of debt under section 86(1A)(d) has been utilised. In order to provide appropriate transparency, I propose that this authorisation, once signed, be presented to the House.
- 56 If joint Ministers agree to utilise powers under section 86(1A)(d) of the Social Security Act and establish a class of debt to be written off for public finance purposes, MSD will need to update its client records to show the total overpayment of AS and that this overpayment has been written off under Section 86(1A)(d).

Impact of the overpayments on appropriations

- 57 As MSD will not recover any overpayments resulting from the error, 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.

Exempting lump sum back-payments from determining ongoing eligibility to financial assistance

- 58 Granting lump sum back-payments to correct the AS entitlement error, may affect eligibility or entitlement to some forms of financial assistance which are cash asset and/or income tested. I am of the view that the granting of back-payments (including any income derived from these payments) to correct this error should not impact on the financial circumstances of affected clients given that the issue was caused by an administrative error that is entirely outside of their control.
- 59 On this basis, I seek Cabinet's agreement to exempt back-payments in order to correct the error when assessing clients' eligibility to financial assistance. This exemption, specifically

NOT GOVERNMENT POLICY – DRAFT AS AT 19 AUGUST 2016

targeted to those affected by the AS IT payment system error, will last for a time period of 12 months following the provision of any lump sum back-payments entitlements to affected clients. The exemption would apply to the lump sum as well as any income earned off that sum during the 12 month period.

- 60 The exemption will also prevent the lump sum payments from having any flow on impacts to Income-Related Rents and the Residential Care Subsidy. I also propose an amendment to the Ministerial Direction for Special Benefit to ensure that these back-payments do not impact on affected clients receiving Special Benefit.

Risks

- 61 The phased approach to correct AS entitlements, as set out in this paper, has been developed to be administratively efficient (for example the use of automated data calculation tools and online portals). However, there is a risk that client behaviour may put pressure on front-line staff either through a large number of clients seeking a review of their entitlements; or by large numbers of clients trying to access the portal or case managers at one time. MSD will have specifically targeted elements within their communications strategy to respond to, and alleviate, these risks.
- 62 The use of an online portal to process and pay former clients presents some security risks. However, MSD will mitigate the risk by ensuring appropriate security measures are in place before the portal goes live.

Calculating over and underpayments – legal advice

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

64

Implementation

- 65 The implementation will be carefully managed by MSD. MSD has developed a comprehensive communication strategy which will ensure the right information gets to impacted clients. The Ministry will use its existing channels of engagement with internal and external stakeholders to communicate the error.
- 66 The IT cost for MSD 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. In addition, there will be some departmental costs

NOT GOVERNMENT POLICY – DRAFT AS AT 19 AUGUST 2016

associated with the staff needed to implement the approach to correcting the error. All of the implementation related costs will be met within MSD's baseline.

Consultation

- 67 This paper has been prepared by MSD. The Treasury and the Crown Law Office have been consulted on this paper. MSD has also consulted with beneficiary advocates over the approach set out in this paper. The Department of Prime Minister and Cabinet has been informed.

Financial implications

- 68 MSD will provide for the costs resulting from the error in its 2015/16 Crown accounts. MSD will seek validation by Parliament, under section 26C of the Public Finance Act 1989, to remedy any unappropriated expenditure in the Benefits or Related Expenses, Accommodation Assistance appropriation for the year ended 30 June 2016 as a result of expenses in excess of the amount of the appropriation. MSD's application under section 26C of the Public Finance Act will need to be certified by the Minister for Social Housing. There is no appropriation impact for the AS overpayments as the fair value of the debt has a nil value.
- 69 MSD will also account for the underpayments of AS as part of the 2015/16 Crown accounts. The approximate cost to the Crown of addressing the underpayments resulting from the error is up to \$29 million. This cost will have an impact on the operating balance in 2015/16.
- 70 Due to the different income and cash asset testing thresholds for the various supplementary benefits, and the dynamic nature of income support, it is not possible to reliably estimate the number of clients whose benefit entitlements would likely be affected by a lump sum payment. Therefore, the financial impact of the income and cash asset exemption proposed at paragraph 59 is unknown. No changes to appropriations are required as the exemption will maintain the current forecasted level of recipients.

Human rights implications

- 71 This paper has no human rights implications.

Legislative implications

- 72 This paper proposes amendments to the Social Security (Income and Cash Assets Exemptions) Regulations 2011, the Social Security (Temporary Additional Support) Regulations 2005 and the Social Security (Long-term Residential Care Subsidy) Regulations 2005 to exempt back-payments associated with correcting clients' entitlements to AS, and any income derived from them, from the cash asset and income tests for assistance under the Social Security Act 1964. The proposed amendments to these regulations will ensure that affected clients do not have their financial entitlements affected by back-payments made to correct for the error in granting AS. This will give effect to the decision sought from Cabinet set out in paragraph 59 of this paper.
- 73 In order to make the regulatory amendments set out at paragraph 72 above, I request that Cabinet invite me to instruct the Parliamentary Council Office on the required regulations.

NOT GOVERNMENT POLICY – DRAFT AS AT 19 AUGUST 2016

Regulatory impact and compliance cost statement

- 74 [A regulatory impact statement (RIS) has been completed for the proposal to ensure that affected clients do not have their financial assistance impacted by back-payments made to correct for the error in granting AS entitlements.]

Gender implications

- 75 This paper has no gender implications.

Disability perspective

- 76 This paper has no disability implications.

Publicity

- 77 MSD has already contacted and addressed those 94 affected clients that were receiving underpayments in their AS rates following the correction of the error in December 2014. [In August 2016, MSD notified the 278 clients, who were receiving overpayment of their AS entitlements, of the changes to their AS entitlement. In the letter notifying of the changes to their entitlements, MSD has advised that affected clients will be provided with a transition payment to allow sufficient time to plan and prepare for any adjustment to their entitlements. This approach to transitioning clients is consistent with the Social Security Act 1964.
- 78 MSD has developed a communication strategy to outline how both potentially affected current and former clients will be able to check whether their historic AS entitlements were impacted by the error. The focus will be to ensure that potentially affected clients have the right advice to make it as easy as possible to come forward and check their entitlements.

Recommendations

- 79 It is recommended that the Committee:
1. **note** that in 2014 the Ministry of Social Development (MSD) identified a significant error in its assessment and payment system that affected the accuracy of client entitlements to the Accommodation Supplement (AS) that dated as far back as 1993;
 2. **note** that when the system error was identified, MSD took immediate action in December 2014 to implement a system fix so that new clients would receive their correct AS entitlements;
 3. **note** that while the system was enhanced to correct entitlements for new clients, it did not retrospectively correct entitlements for clients receiving inaccurate AS entitlements as a result of the error prior to December 2014;
 4. **note** that there are approximately 127,000 clients who receive or have received AS between 1993 and December 2014 who are affected by the error;
 5. **note** that the process to correct for the impact of the error on clients receiving the AS prior to December 2014 will occur through four phases:
 - 5.1 Phase one: correcting entitlements for current clients who continue to be overpaid AS (278 current clients);

NOT GOVERNMENT POLICY – DRAFT AS AT 19 AUGUST 2016

- 5.2 Phase two: correcting historic entitlements for current clients that were underpaid their AS entitlements (~22,000 current clients);
- 5.3 Phase three: correcting historic entitlements for former clients that were underpaid their AS entitlements (~27,000 former clients); and
- 5.4 Phase four: debt write-off for historical overpayment of AS entitlements (29,000 current clients and 36,000 former clients) ;
- 6. **note** that MSD has corrected rates of payment for all 94 current clients affected by the error that were receiving lower AS entitlements than they were entitled to;
- 7. **note** that MSD [has] provided the 278 current clients receiving an overpayment of AS a transition payment to allow sufficient time to plan and prepare for any adjustment to their entitlements;
- 8. **note** that MSD will automatically process lump sum back-payments to correct historic underpayments of AS entitlements for current clients;
- 9. **note** that potentially affected former clients, who may have had an underpayment of AS entitlements as a result of the error, will need to engage with MSD in order to have their past entitlements assessed for the purposes of granting any lump sum back-payments that may be owed;
- 10. **agree** to amend the Social Security (Income and Cash Assets Exemptions) Regulations 2011, the Social Security (Temporary Additional Support) Regulations 2005, the Social Security (Long-Term Residential Care) Regulations 2005 and the Ministerial Direction on Special Benefit to exempt back-payments for correcting clients' entitlements to the Accommodation Supplement and any income derived from them in the 12-month period from cash asset and income tests for assistance under the Social Security Act 1964;
- 11. **invite** the Minister for Social Development to amend the Ministerial Direction on Special Benefit to give effect to the decision in recommendation 10;

Financial recommendations

- 12. **note** that MSD will provide for the costs of the AS underpayment error by incurring the costs in the 2015/16 Crown accounts as required by the current generally accepted accounting practice standards;
- 13. **note** that MSD's approach to address the underpayment of AS entitlements will have the following impact on the operating balance:

	Sm - increase/(decrease)				
	2015/16	2016/17	2017/18	2018/19	2019/20 & Outyears
Operating Balance Impact	29.000	-	-	-	-
Debt Impact	-	-	-	-	-
No Impact	-	-	-	-	-
Total	29.000	-	-	-	-

- 14. **note** that providing for the costs of the AS underpayment payment error in 2015/16 will result in MSD incurring unappropriated expenditure in Benefits or Related Expenses,

NOT GOVERNMENT POLICY – DRAFT AS AT 19 AUGUST 2016

Accommodation Assistance appropriation for the year ended 30 June 2016, as a result of expenses in excess of the amount of the appropriation;

15. **agree** that any unappropriated expenses as noted in paragraph 13 above be included in the Appropriation (2015/16 Confirmation and Validation) Bill for validation by Parliament;
16. **note** that MSD will seek validation by Parliament under section 26C approval, to be certified by the Minister for Social Housing, for any expenditure in excess of the appropriation under the Public Finance Act as a result of the above financial provision;
17. **note** there is no appropriation impact from the AS overpayment error as the fair value of the debt has a nil value under generally accepted accounting practices;
18. **note** that MSD will be absorbing the administrative costs of identifying and paying affected clients who have been underpaid their AS entitlements;

Process for writing off overpayments

19. **note** that MSD intends to pursue the use of section 86(1A)(d) of the Social Security Act 1964 which allows the Minister for Social Development and the Minister of Finance to jointly authorise the write-off of classes, descriptions, or kinds of debts (for public finance purposes) and that the Chief Executive's duty to recover debt does not apply to debts that are written off through this process;
20. **note** that MSD and the Treasury will provide advice and seek, from the Minister for Social Development and the Minister of Finance, a written authorisation (to be tabled in the House) that specifies that overpayments resulting from the error will be established as a class of debt and written off for public finance purposes under the authority provided in 86(1A)(d) of the Social Security Act 1964; and

Legislative implications

21. **invite** the Minister for Social Development to instruct the Parliamentary Counsel Office to draft regulations to give effect to decisions in recommendation 10.

Authorised for Lodgement

Hon Anne Tolley
Minister for Social Development