

Child Support Agency, Department of Human Services:

INVESTIGATION OF A PARENT'S 'CAPACITY TO PAY'

August 2010

*This is an abridged version of report 11|2010.
The full report has not been made publicly available due to
the technical nature of its content.*

Report by the Acting Commonwealth Ombudsman,
Ron Brent, under the *Ombudsman Act 1976*

REPORT NO. **11|2010**

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INTRODUCTION

This is an abridged version of a detailed report of this office's investigation into the Child Support Agency's (CSA) investigations of a parent's 'capacity to pay' under Part 6A, Division 3 of the *Child Support (Assessment) Act 1989*. Our investigation commenced in May 2009. A draft of the full report with detailed analysis, conclusions and recommendations to improve the CSA's administration was provided to the Department of Human Services (DHS)¹ on 31 May 2010.

BACKGROUND

In most cases, the CSA assesses child support payable by individual parents using a legislative formula, based on a parent's taxable income, as reported to the Australian Taxation Office (ATO). The CSA can, however, decide not to apply the usual child support formula provisions to a case if it is satisfied that the formula does not produce a fair level of child support because of a parent's income, earning capacity, property or financial resources. Through the Change of Assessment (CoA) process, the CSA can look beyond a parent's taxable income if it considers there are special circumstances, and take into account the totality of the parent's financial situation.

Most CoA processes are initiated by the payer or payee in the particular child support case. Either parent can do this by making a CoA application to the CSA. However, the CSA is also entitled to initiate a CoA process. The CSA's 'financial investigators' are responsible for conducting Capacity to Pay (CTP) investigations in specific cases to determine whether referral for a CoA process is warranted.

The cases that the CSA selects for CTP investigations are those for which it has information to suggest that a parent has financial resources that would allow them to contribute more to the support of their children than is reflected by the application of the usual child support formula.

According to the CSA, a CTP investigation may be appropriate if a parent:²

- has substantial property but a small amount of child support income
- has legitimately arranged their financial affairs to minimise their taxation liability
- receives income which is not assessable or is exempt from taxation
- received a lump sum payment that is not included in the child support income amount.

Some common situations for CTP investigations are those where a parent is involved in salary sacrificing arrangements; has a low personal income, but has organised their business affairs through a partnership or corporate structure; or where their current taxable income is reduced by past year losses. CTP investigations aim to discover whether the parent received a personal financial benefit through these arrangements that would make their current child support assessment unfair.

¹ The CSA is a program within the Department of Human Services.

² See chapter 2.6.14 of *The Guide*, published on the CSA's website at www.csa.gov.au/guidev2/TheGuideMaster.aspx?content=2_6_14.

COMPLAINTS TO THE OMBUDSMAN

The two case studies below demonstrate some of the issues in the complaints that we have received and investigated about the CSA's CTP process.

Case study one

An accountant complained to us on behalf of his client, Mr A, who was a payer in two child support cases. The complaint was that the CSA had not afforded Mr A procedural fairness in a CoA process that followed a CTP investigation.

The CSA's financial investigator had made several telephone calls to Mr A to discuss the investigation of his business income, but for a variety of reasons they did not actually manage to have a conversation. The financial investigator analysed the information included in Mr A's tax returns and made a recommendation on that basis. The CSA sent Mr A a letter advising him that 'the CSA is considering changing your child support income amount from \$50,052 to the new income amount of \$103,989'. The letter did not explain how the CSA had arrived at the recommended figure. The letter said that Mr A should contact the CSA if he wanted to have a conference with the person who would be considering the recommendation.

Mr A telephoned the CSA and attempted to speak to the financial investigator about the opportunity to participate in a conference. The financial investigator was unavailable when Mr A called. Mr A left a message asking the financial investigator to call him, but his call was not returned. The CSA proceeded to make a decision to increase the child support assessment, without making any further attempt to contact Mr A.

Case study two

Ms B is the new wife and authorised representative of a payer (Mr C) selected by CSA for a CTP investigation. Mr C pays child support to his former wife for the children of their marriage. Ms B and Mr C share a complex business arrangement of two interlinked companies which supply goods and services to each other. Ms B is a director of one company, and Mr C is the director of the other. The CSA's financial investigator recommended that Mr C's child support assessment be increased to take into account the financial benefits that they believed accrued to Mr C as a result of the arrangements that he and Ms B had put in place to run their businesses.

Ms B complained to this office that as a part of the CTP investigation, the CSA had requested detailed financial information about her company and her earnings, yet had refused to provide her with the opportunity to comment on how the CSA intended to take that information into account in working out Mr C's child support. Furthermore, as Mr C's authorised representative, the CSA discussed details of Mr C's income and financial affairs with Ms B over a number of months, yet refused Ms B's request to take part in the CoA conference. The CSA advised Ms B to tell Mr C what to say about her own companies and financial affairs during the conference. Ms B said that Mr C was not fully aware of the financial details of both companies and believed that he might be disadvantaged if he was not able to properly present his case to the CSA.

We advised the CSA of our concerns about the way it intended to conduct the CoA process. Although Ms B was not entitled to represent Mr C in the CoA conference, it seemed unreasonable to deny her an opportunity to provide information about her involvement in Mr C's business affairs. As a result of our investigation, the CSA undertook to allow Ms B to provide further evidence about her financial information to the senior case officer via telephone.

As can be seen from these case studies, the CSA's CTP investigations can be intrusive. If a parent does not participate in the process, the CSA may make a change based solely on the information that it has been able to glean from other

sources, and make assumptions about the parent's expenses and personal expenditure. If parents do not provide up-to-date information about their circumstances, this can undermine the accuracy of the CSA's eventual decision about the assessment.

The CTP process also involves the CSA disclosing information to each parent about its conclusions about their former partner's current financial situation. Such a disclosure is required by the child support legislation. Nevertheless, it has the potential to damage the relationship between the parents. The CSA's investigation and any consequential adjustment to child support may imply that a parent has deliberately organised their financial affairs to affect the child support assessment. On the other hand, if the information that the CSA discloses is subsequently found to be wrong, this can lead to frustration and disappointment for both parents.

OUR INVESTIGATION

In May 2009 we notified the CSA of our intention to conduct an own motion investigation into the CSA's administration of the CTP process. Our investigation examined the CTP case selection criteria, the CTP investigation process and the way that the CSA portrays the process externally. We also examined a sample of 34 cases where the CSA's financial investigators had recommended that a CoA decision be made after a CTP investigation.

Our investigation identified many areas of the CSA's CTP process that we believe could be improved. The recommendations we made to address them are at pages 6 to 8 of this report. The CSA has responded positively to the recommendations and has already implemented some of them (see page 9).

CTP case selection criteria

We concluded that the CSA policies and procedures for selecting cases prioritised cases where the CTP investigation will increase the amount of child support payable. The CSA advised us that this prioritisation was largely the result of the additional CTP investigations it conducted under the 'Income Minimisers' program, discussed in more detail on page 5 of this report.³ We accept the CSA's explanation, however, we remain convinced that the CSA needs to be even handed in the way that it deals with its customers, and have recommended that it change its CTP selection procedures.

We consider it is appropriate for the CSA to continue to target cases where a parent's overall financial resources are greater than their taxable income would suggest. However, the CSA should not prioritise its CTP investigations on the basis of the parent's role (i.e. payer or payee). In other words, the CSA should also investigate cases where the payee parent appears to have additional financial resources (see recommendations 1 and 14).

Better tools and support for financial investigators

There were many cases in our sample where we considered the financial investigator's analysis of the information they had gathered was flawed. The following case study is an example.

³ Under the heading *The CSA's portrayal of the CTP process and the parents it investigates*.

Case study three

The financial investigator treated a depreciation amount as the parent's income, without having any regard to the size of the business's overall trading loss. This analysis was flawed as a matter of simple arithmetic—disregarding the depreciation figure still meant that the business had traded at a loss. In any case, the CSA's policy is that an amount claimed for depreciation will only be 'added back' if the sum is available for the parent's day-to-day living expenses.

We believe the CSA should review the tools that it has available to support its financial investigators. Better training and consolidated policy information for financial investigators would enhance the quality of CTP investigations (Recommendations 6, 7 and 8). The CSA also needs to develop better forms and computer support for financial investigators to use to capture information from parents and from third parties (Recommendations 3 and 5).

Improve quality assurance arrangements

We also consider that the CSA needs to review its arrangements for checking the quality of a financial investigator's recommendations and correspondence. The CSA already had in place a quality assurance process for CTP investigations. We had some concerns about the rigour of those arrangements and noted that planned quality assurance checks were not always carried out as intended. Recommendations 8 and 12 address these shortcomings.

Advice to parents about the investigation

In our view, the CSA does not provide adequate information to parents about the CTP investigation process or the factors that the CSA takes into account during an investigation. Nor were we satisfied that the CSA provided parents with a sufficiently detailed summary of the information that it uses to form the view that an assessment is unfair. This places parents at a disadvantage in any CoA process that follows the CTP investigation.

We believe the CSA needs to improve the quality of its general information about the CTP process (Recommendations 2, 4, 5 and 6). It should also provide parents with a detailed summary of the specific financial information that it intends taking into account (Recommendations 10 and 11).

Routinely gathering information about a parent's new partner

We noted that one of the forms the CSA sends to all parents subject to a CTP investigation asks the person to provide financial information about their new partner. This is usually not relevant to the CTP investigation. We recommend that the CSA amend the form to avoid routinely collecting this information (Recommendation 5).

Integrating the process with CSA's arrangements to respond to fraud

We consider that the CSA's CTP processes failed to adequately deal with the possibility that an investigation could uncover fraudulent activity, which would warrant action beyond just varying the child support assessment.⁴ We believe the CSA needs

⁴ We have previously investigated the CSA's response to allegations of customer fraud: see Report 12|2008 www.ombudsman.gov.au/files/investigation_2008_12.pdf.

to revise its CTP procedures to ensure that any case of suspected fraud is referred for further specialised assessment (Recommendations 1 and 9). We also believe the CSA should review the forms used for CTP investigations to warn parents that it is an offence to provide false information (Recommendation 5).

The CSA's portrayal of the CTP process and the parents it investigates

As noted earlier, the CSA maintains that it appropriately prioritised the investigation of payer parents where it was likely that a CTP investigation would increase the amount of child support, because of targets set as part of its Income Minimisers program. The Income Minimisers program was intended to deliver 6,300 extra CTP investigations, and \$93.2 million extra in child support payments between 1 July 2008 and 30 June 2010.

However, the CSA's publicity of the Income Minimisers program suggested that it would target both payer and payee parents for investigation.

It also created the impression that parents under CTP investigation are those who deliberately attempted to avoid their child support responsibilities. This was not borne out by the cases that we examined in our sample. The CSA's CTP investigations include many where parents had perfectly legitimate business arrangements for taxation purposes, and the question of their motivation was usually irrelevant.

While the Income Minimisers program has now ended, the CSA continues to conduct CTP investigations. In future, we believe the CSA must be balanced in the way that it presents the results of its CTP investigations and in its communication with the parents involved in cases under investigation (Recommendations 4 and 13).

RECOMMENDATIONS

We provided a draft of the full report of this investigation to DHS on 3 May 2010. The Deputy Secretary, Child Support program responded positively to the report and the 14 recommendations in it, which are reproduced below.

The CSA accepted 13 of the Ombudsman's recommendations, and noted one.⁵ The CSA's response to this report is included at page 9.

Recommendation 1

That the CSA review its case selection methodology to ensure that the CTP process is administered in a manner that is consistent with the objects of the Assessment Act, and especially to:

- give equal priority to cases where the parent with additional resources is the parent receiving child support (where the CTP process is likely to reduce the child support assessment)
- give appropriate attention to the more difficult cases

⁵ The CSA 'noted' but did not accept recommendation 11, which it considered was outside the scope of this investigation. Nevertheless, the CSA has undertaken to examine its procedures to address our concerns about its approach to 'earning capacity'.

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- ensure that cases involving possible customer fraud are appropriately referred for further assessment.

Recommendation 2

That the CSA consider the best way to provide to parents involved in CTP investigations detailed and consistent information about:

- the investigation process
- the extent of any information that the CSA will disclose to the other parent
- factors the CSA will take into account in considering whether the current child support assessment is unfair because of a parent’s income, earning capacity, property and financial resources.

Recommendation 3

That the CSA explore ways to better capture the information gathered by financial investigators, preferably integrated into the CSA’s computer records for the customer.

Recommendation 4

That the CSA review the CTP introduction letter to provide parents with clearer and more detailed information about the CTP process, and to identify the person conducting the investigation.

Recommendation 5

That the CSA review the *Assets and Liability Form* with the following aims:

- to avoid routinely collecting information about the personal and financial affairs of people who are not parties to a child support case
- to improve the form as a tool for gathering complex financial information from a parent about their business and financial affairs, appropriately distinguishing between personal and business expenditure
- to warn parents that it is a serious offence to provide the CSA with false and misleading information.

Recommendation 6

That the CSA review its written policy and procedural information relevant to the CTP process, especially to:

- separate the policy and procedural information for financial investigators
- incorporate relevant and appropriate parts of the *Financial Investigator’s Companion* into chapter 2.6.14 of *The Guide* (about reason 8—a parent’s income, property, financial resources, or earning capacity).

Recommendation 7

That the CSA develop more detailed guidelines, for the purpose of CoA reason 8, about the appropriate treatment of:

- financial resources, capital amounts and sums not presently realisable
- corporate entities in which a parent has an interest.

Recommendation 8

That the CSA ensure that people working as financial investigators have the appropriate training to understand financial information, and that they are given appropriate feedback about any recommendation that is not adopted. The CSA should also monitor the rate at which financial investigators' recommendations are accepted/rejected and use this data in performance assessment and program evaluation.

Recommendation 9

That the CSA amend its CTP Procedural Instruction to ensure that cases involving possible fraudulent financial arrangements are appropriately referred for further assessment.

Recommendation 10

That the CSA review its procedures and guidelines for providing parents with a detailed summary of the information that it used to form the view that the child support assessment is unfair because of a parent's income, earning capacity, property or financial resources. The purpose of the review would be to:

- clarify whether s 98M(2) of the Assessment Act requires that each parent be sent the same summary of information
- ensure that each parent receives sufficient detail about the information that the CSA gathered about both parents' financial situations to allow them to provide meaningful input to the CoA process
- develop a standardised format for the summary, to clearly and logically present the information, with calculations explained, sources of information identified and specify period(s) to which the information relates.

Recommendation 11⁶

That in any case where the CSA is likely to take into account a parent's earning capacity in a CoA process, the CSA should provide to the parent:

- a written notice of the criteria for such a decision
- advice about the need to provide evidence that their decision about their working arrangements was not motivated by a desire to affect their child support assessment
- suitable time to gather evidence about the reasons for their decision about their working arrangements.

Recommendation 12

That the CSA review its quality assurance arrangements for CTP investigations, to ensure that:

- a sample of financial investigator investigations is regularly reviewed, with particular emphasis placed on checking the technical quality of recommendations and written communication to parents explaining recommendations and the basis upon which they had been made

⁶ The CSA did not accept recommendation 11. However, the CSA has 'noted' our concerns about its approach to a parent's 'earning capacity', which underpinned that recommendation and undertaken to examine its procedures to address them.

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- staff performing quality assurance checks are sufficiently objective and not directly involved in supervising or providing day-to-day support to financial investigators
- regular reports of quality assurance processes are prepared and include recommendations for strategies to improve areas of weakness
- the CSA monitors the implementation of recommendations to ensure they result in measurable improvements.

Recommendation 13

That the CSA review the name and description of the Income Minimisers program to better reflect the nature of the cases that it actually investigates, both to reduce the possible impression of bias and to acknowledge the fact that many people subject to investigation have not actively sought to avoid their child support obligations.

Recommendation 14

In conjunction with Recommendation 1 (that the CSA review the CTP case selection criteria), the CSA should consider whether the current CTP targets are appropriate for ensuring fair and reasonable outcomes for the Income Minimisers program.

CSA RESPONSE TO RECOMMENDATIONS

Reproduced below is the CSA's response to this report.

The Child Support Agency (CSA) agrees with 13 of the 14 recommendations outlined in your report, and notes the remaining recommendation.

The CSA agrees the Capacity to Pay (CTP) process is a key tool for improving the accuracy, and through this the equity, of child support assessments as they impact on both paying and receiving parents.

However, the CSA notes that customers who believe they may be paying too much or receiving too little child support can make their own application for a Change of Assessment (CoA). In this respect, the CSA notes that only 1290, or less than 6%, of the 22,494 CoA applications finalised in 2008–09 were initiated by the CSA. The remaining 94% of changes to assessments arose from applications by customers of the CSA.

The CSA would also like to emphasise that the Income Minimisers Program, to which you refer in your report, was a specific program introduced as part of the *Child Support Reforms—Improving Compliance* 2006–07 Budget measure.

The goal of the *Improving Compliance* measure was to achieve an increase in the collection of child support. It is for this reason the Income Minimisers Program was necessarily and appropriately focussed on targeting people with the capacity to pay additional child support. This measure lapsed at the end of the 2009–10 program year.

Further, the CSA has made a number of changes to the CTP process since the commencement of your investigation, including:

- The CSA has completed a review of the targeting of CTP investigations and is refining the case selection criteria (Recommendations 1 and 14);
- The CSA has updated the Capacity to Pay Procedural Instruction (PI), including additional references to referral of fraud allegations and a link to the PI on Fraud Allegations (Recommendation 1);
- The CSA has revised the Assets and Liabilities Form (ALF), removing collection of third party information and adding a statement regarding penalties for provision of fraudulent information (Recommendation 5);
- The CSA has implemented a revised Quality Assurance process which mirrors the Ombudsman's recommendation (Recommendation 12); and
- The CSA has changed the name and description of the 'Income Minimisers Program' to 'Capacity to Pay' following the lapsing of the *Child Support Reforms—Improving Compliance* 2006–07 Budget measure at the end of the 2009–10 program year (Recommendation 13).

The CSA is continuing to work on the implementation of the other recommendations in your report.